

Employers and remote working organization in a post-COVID-19 world:

## The frightening spectrum of foreign taxable presence

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«Life is wide, limitless. There is no border, no frontier.» — Bruce Lee

**F**urther to the unprecedented COVID-19 crisis, the working environment has been deeply affected and moved toward new working organization trends. As the movement restrictions turned into temporary standards in Luxembourg, for many cross-border employees home working has become the new organization of work. In order to swiftly adapt the existing legal framework to this unexpected situation, the convention on the legal framework for teleworking of 2 February 2021<sup>(1)</sup> (Convention) recently entered into effect.

The taxation of cross-border employees working from their country of residence during the COVID-19 period has been largely discussed further to the various cross-border agreements concluded by Luxembourg, Belgium, Germany and France and is not the purpose of the present article. However, the question of the risk of Permanent Establishment (PE) and fiscal attraction outside Luxembourg remains unanswered for many Luxembourg employers willing to continue with the cross border home working in the post-COVID-19 period.

On 21 January 2021, the secretariat of the Organisation for Economic Co-operation and Development (OECD) released updated guidance on tax treaties and the impact of the COVID-19 pandemic<sup>(2)</sup> (OECD Analysis) confirming that the COVID-19 situation should generally not create PE risks for employers or a change of the fiscal residency of the employers. However, this analysis is limited to the COVID-19 period and does not cover the future impacts of teleworking abroad after the pandemic. This question is especially important for countries such as Luxembourg with a major portion of cross-border workers and more than 80% of the workers employed in the tertiary sector<sup>(3)</sup> which is more adapted to teleworking. Luxembourg employers may therefore be affected by new tax obligations that could arise if their employees constitute a PE outside Luxembourg or if the residency of their company is challenged further to the adoption of this new work organization. Now that the page of the COVID-19 pandemic is nearly being turned and that teleworking will likely become the new “normal” organization of work, it is time to consider the related potential risk of foreign permanent establishment and fiscal attraction.

### What is teleworking and what is a PE during and after the COVID-19 crisis?

Facing the legal void in the field of remote working, the Convention brings some clarification on the concept, providing that the teleworking should be «the organization or performance of work, generally



using information and communication technologies, so that tasks which would normally be carried out at the employer's premises are performed elsewhere.»

The Convention makes a distinction between occasional teleworking (e.g., teleworking during the COVID-19 pandemic) and regular teleworking (e.g., teleworking representing in average more than 10% of the annual working time of the employee after the COVID-19 pandemic).

The right to tax Luxembourg companies and workers in a cross-border situation is determined by the double tax treaties concluded by Luxembourg and its neighboring countries (DTTs). Most of these DTTs are drafted on the basis of the OECD model convention and its commentaries.

According to the OECD Analysis, the COVID-19 pandemic should be seen as a «force majeure» event, which should temporarily impact the application of certain provisions of the DTTs related to PEs and residency.

The DTTs concluded by Luxembourg with Germany, France and Belgium define a PE as: «a fixed place of business through which the business of an enterprise is wholly or partly carried on». The DTTs also provide certain examples of PE such as a branch or an office but they remain silent on whether teleworking should lead to the existence of a PE.

According to the OECD Analysis: A place must have a certain degree of permanency and be at the disposal of an enterprise in order for that place to be considered a fixed place of business through which the business of that enterprise is wholly or partly carried on. Paragraph 18 of the commentary on Article 5 of the 2017 OECD model convention explains that even though part of the business of an enterprise may be carried on at a location such as an individual's home office, that should not lead to the conclusion that that location is at the disposal of that enterprise simply because that location is used by an individual (e.g. an employee) who works for the enterprise. The carrying on of intermittent business activities at the home of an employee does not make that home a place at the disposal of the enterprise. A home office may be a PE for an enterprise if it is used on a continuous basis for carrying on business of that enterprise and the enterprise generally has required the individual to use that location to carry on the enterprise's business.



It has been made clear that cross-border employees that are teleworking from their country of residence during the COVID-19 pandemic should not constitute PEs of their employers.»

The situation may be now different in the post COVID-19 scenario for the cross-border teleworkers that do not have any place of work made available in the country where their employer is located. Indeed, according to Paragraph 18 of the commentary on article 5 of the 2017 OECD model convention: Where, however, a home office is used on a continuous basis for carrying on business activities for an enterprise and it is clear from the facts and circumstances that the enterprise has required the individual to use that location to carry on the enterprise's business (e.g. by not providing an office to an employee in circumstances where the nature of the employment clearly requires an office), the home office may be considered to be at the disposal of the enterprise.

It should also be noted that if the activity of the employer outside Luxembourg has only a preparatory or auxiliary character (e.g. storing, displaying or delivering employers goods or merchandise), it should not be considered as a PE according to the applicable DTTs and the 2017 OECD model convention. Additionally, the OECD report on action 7 on the prevention of artificial avoidance of PE provides that the extended definition of the dependent agent (e.g. sales representative) «should not apply where a person merely promotes and markets goods or services of an enterprise in a way that does not directly result in the conclusion of contracts.»<sup>(4)</sup>

### Risk of having a dependent agent outside Luxembourg

Traditionally, and on the basis of tax treaties concluded before the BEPS Project and the Multilateral Instrument<sup>(5)</sup> (MLI) such as the DTTs concluded by Luxembourg with respectively Belgium and Germany, an agent could be treated as a PE only if the following cumulative conditions are met: (i) the agent must be dependent and (ii) must have, and must habitually exercise, the authority to conclude contracts in the name of the enterprise. However, pursuant to the new DTT with France effective since 1 January 2020, and in compliance with the BEPS/MLI recommendations, the agency PE definition has been very substantially extended to include any person that «habitually

plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise,» to the extent that such contracts are either (i) in the name of the enterprise or for the transfer of property owned by that enterprise; or (ii) for the provision of services by that enterprise.

Based on this new definition, the threshold for the recognition of a PE in France is substantially lowered.

Overall, according to the three DTTs, the activity of the cross-border employee must be «habitual» to be considered a PE.

This was the case for many companies adopting online or distance selling models because of the impossibility to travel and/or meet partners during the COVID-19 pandemic. Under such models, employees may sell goods or services without being physically in contact with the buyers. Assuming that the employees were not concluding these contracts in their country of residence before the COVID-19 pandemic, this activity should not constitute a PE in their country of residence during the COVID-19 pandemic as it is not a «habitual» activity. This conclusion would be different if the employee was already concluding contracts on behalf of its employer in its country of residence before the COVID-19 pandemic. In such a case, the activity of the employee may already be considered a PE activity before the COVID-19 pandemic and should continue to be considered a PE activity during and/or after the COVID-19 pandemic.

In this context, two similar activities carried out during the COVID-19 pandemic could be treated differently depending on whether a PE existed before the COVID-19 pandemic. Similarly, because an employee was not considered a dependent agent during the COVID-19 pandemic does not mean that it will not continue to be considered as a dependent agent after the COVID-19 pandemic.

### Risk of fiscal attraction outside Luxembourg for executives

During the COVID-19 pandemic, directors, managers and other executives of Luxembourg companies may have worked outside of Luxembourg due to government's directives or the inability to travel. This situation may raise questions regarding the place of residency of companies managed outside Luxembourg during the COVID-19 pandemic. Some of these executives may now wish to continue teleworking from their country of residence further to the COVID-19 pandemic and may create concerns regarding the place of residence of the company they manage.

According to article 159 of the Luxembourg income tax law, a company is deemed to be a tax resident company provided that it has either its statutory seat or its central administration in Luxembourg. A company incorporated in Luxembourg shall be therefore deemed to be resident in Luxembourg, unless the company is managed and controlled outside of Luxembourg. In that case, the Luxembourg company may be considered a tax resident in the country where its place of effective management is located.

The DTTs referred to above provide a tie-breaker rule to avoid cases where a company would be considered resident in two countries simultaneously due to a change in the place of effective management.

This tie-breaker rule states that: Where [...] a company is regarded as being a resident of both Contracting States, then it shall be deemed to be a resident of the Contracting State in which its place of effective management is situated.

The tie-breaker rule contained in most DTTs considers the criteria of the place of effective management as decisive to determine the jurisdiction of the residency of a company. In this respect, paragraph 149 of the commentaries on the 2017 OECD model tax convention provides the following regarding the term «place of effective management» that was used before 2017: interpreted by some States as being ordinarily the place where the most senior person or group of persons (for example a board of directors) made the key management and commercial decisions necessary for the conduct of the company's business.

Luxembourg companies with their effective place of management outside Luxembourg during the COVID-19 pandemic cannot be considered as «ordinarily» managed outside Luxembourg. Therefore, the residency of these companies should not be challenged even if their executives were working outside Luxembourg for a temporary period. The situation is different if the executives will continue to exercise their management activities outside Luxembourg after the COVID-19 pandemic on a permanent basis. In such a case, the residency of the Luxembourg companies can be challenged by foreign countries and a risk of PE outside Luxembourg may also arise. The assessment should be carefully monitored as the tendency of the neighboring countries' courts (e.g. in the ValueClick case in France<sup>(6)</sup>) may lead to an extensive interpretation of the concept of PE. The confirmation of the existence of PE by the tax authorities may have a direct impact on the statutes of limitations and the penalty that may apply further to such reassessment.

1) The convention of 20 October 2020 on the legal framework for teleworking, (convention du 20 octobre 2020 relative au régime juridique du télétravail conclue entre l'Union des Entreprises Luxembourgeoises (UEL), d'une part et les syndicats LCGB et OGBL) entered into effect on 2 February 2021 further to the Grand-Ducal Regulation of 22 January 2021 (Règlement grand-ducal du 22 janvier 2021 portant déclaration d'obligation générale de la convention du 20 octobre 2020 relative au régime juridique du télétravail).

2) Updated guidance on tax treaties and the impact of the COVID-19 pandemic, OECD, 21 January 2021, <https://www.oecd.org/coronavirus/policy-responses/updated-guidance-on-tax-treaties-and-the-impact-of-the-covid-19-pandemic-d42be07/>.

3) Emploi salarié intérieur par branche d'activité, 1995-2020, [https://statistiques.public.lu/stat/TableViewer/table-View.aspx?ReportId=12917&IF\\_Language=fr&Main-Theme=2&EldrName=3&RFPPath=92](https://statistiques.public.lu/stat/TableViewer/table-View.aspx?ReportId=12917&IF_Language=fr&Main-Theme=2&EldrName=3&RFPPath=92).

4) OECD, Preventing the Artificial Avoidance of Permanent Establishment Status, Action 7, 2015 Final Report.

5) Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS.

6) On 11 December 2020, in a *Conversant/ValueClick* case, the French Conseil d'Etat, ruled on the question of the characterization of a permanent establishment with regard to both CIT and VAT, of an Irish company operating in the digital sector and benefiting from services rendered by another company of the group established in France.

## Enquête FEDIL

# Les qualifications de demain dans l'industrie 2021

**L**a FEDIL vient de publier les résultats d'une 12<sup>ème</sup> enquête consécutive portant sur les prévisions d'embauche des entreprises dans les secteurs de l'industrie et de la construction du Luxembourg.

L'enquête représente le seul indicateur existant au Luxembourg sur les besoins en qualifications dans les secteurs couverts. Il s'agit donc d'un baromètre économique unique en son genre. La promotion et la recherche de jeunes talents étant une de ses priorités en 2021, la FEDIL considère que l'éducation et la for-

mation sont les principaux vecteurs d'identification, d'appartenance et de promotion sociales. Une orientation adéquate est donc d'une importance stratégique - elle contribue à influencer les chances des candidats sur le marché de l'emploi tout en garantissant aux entreprises un pool de talents qualifiés.

Voilà pourquoi l'enquête, destinée aux jeunes, à leurs parents et aux responsables d'orientation, veut répondre à plusieurs objectifs : cerner les besoins des entreprises, concilier offre et demande de formation dans l'intérêt des jeunes et donner un indicateur fiable aux services d'orientation scolaire et professionnelle.

Finalement, elle constitue aussi un moyen pour adapter la politique de la formation aux réalités économiques. Compte tenu des poussées de l'évolution technologique, il s'agit de s'assurer que la formation professionnelle initiale permette aux jeunes d'acquérir les qualifications recherchées dans le futur.

L'édition 2021 de l'enquête indique un total de 817 prévisions d'embauches pour 62 entreprises dans les deux années à venir, dont 66,34% pour remplacer des départs et 33,66% pour occuper des postes qui viennent d'être créés. Le chiffre total d'embauches prévu est malheureusement le moins élevé depuis le lance-

ment de l'enquête en 1998. Ceci est notamment dû à la crise sanitaire et économique engendrée par la pandémie du COVID-19, ayant causé, entre autres, des manques de prévisibilité et des difficultés de planification en termes de recrutement pour les années à venir.

Les entreprises ont de nouveau signalé une demande très importante de la formation du Diplôme d'aptitude professionnelle (DAP) (46,3% du chiffre total), mais on peut également observer une hausse notable de la demande de la formation du Diplôme de Technicien (DT) (18,4% du chiffre total). La formation du baccalauréat (BAC) reste celle qui est la moins sollicitée

auprès des entreprises industrielles du Luxembourg (2,9% du chiffre total).

Les résultats de l'enquête sont communiqués sous forme de dépliants réalisés sur base du design de la brochure qui dirigent les étudiants ciblés vers l'enquête. La brochure peut également être consultée sur [www.fedil.lu](http://www.fedil.lu).

Plusieurs partenaires institutionnels ont collaboré à cette enquête, à savoir la Chambre de Commerce / House of Training, la Maison de l'Orientation, le ministère de l'Enseignement supérieur et de la Recherche ainsi que l'Agence pour le développement de l'emploi (ADEM).