TAX CASES AFFECTING REMOTE WORKERS AND THEIR EMPLOYERS

Author
Sunita Doobay

Tags
Auxiliary or Preparatory
Digital Nomad Visas
Fixed Place of Business
Home Office
Permanent Establishment
Product Information
Remote Worker

INTRODUCTION

The legacy of the pandemic has demonstrated that an employee does not need to be in the office in order to work efficiently. Employees have adjusted to working remotely. In North America, remote working may mean a location in the suburbs surrounding the location of a business office, or perhaps a nearby state. In Europe, remote working may mean relocation to a different country. To illustrate, an article appearing in *The Guardian*[1] addresses how individuals have been encouraged to relocate to work remotely by the issuances of "digital nomad visas" offered by countries such as Croatia, Estonia, Iceland, and Greece. These visas typically require the applicant to meet minimum income levels, while others may require a minimum level of cash in the bank, as well.

While these programs focus on visa entitlement for foreign programmers and digital engineers, they do not always address the risk of tax for a foreign employer when the individual works exclusively for one company or one group of companies. An employer needs to be aware of the jurisdiction in which each of its remote employees is situated to ensure that the presence of the employee and the activity conducted in the country does not trigger a permanent establishment ("P.E.") for the employer and resulting income tax exposure.

This article addresses several recent cases in Europe and pronouncements by the Canada Revenue Agency ("C.R.A.") in Canada.

DENMARK

In Denmark, the *Skatterådet*, or Tax Council, of the *Skattestyrelsen*, or the Danish Tax Agency, issues binding rulings on tax matters of general public importance. On April 26, 2022, the *Skatterådet*, ruled that the presence of a remote employee of *Spörger*, a German company, resulted in the establishment of of a P.E. in Denmark, thereby subjecting *Spörger* to Danish tax on the profits attributable to the P.E. [2]

The facts in the ruling were as follows. *Spörger* employed a sales employee who resided in Denmark (the "Employee") and who did not wish to move to Germany. The Employee was employed as an area sales manager and tasked to handle certain sales in relation to Africa, Belgium, Germany, the Netherlands, the Baltics and the Nordics. *Spörger* did not obtain any commercial advantage from the Employee

Sunita Doobay is a partner in Blaney McMurtry, L.L.P., Toronto. She advises Canadian and foreign corporations, private equity funds, venture capital funds, and high net worth individuals on sophisticated domestic and international tax planning issues.

[1] Burgen, Stephen. "Spain Plans 'Digital Nomad' Visa Scheme to Attract Remote Workers." *The Guardian*. Guardian News and Media, September 25, 2022.

[2] SKM number SKM2022.250.SR. related to case number 21-0722131, reported here.

performing tasks from Denmark—the Employee's performance of work from Denmark was solely due to personal circumstances.

The Employee reported to *Spörger* management Germany. Denmark had a modest demand for *Spörger* products. To illustrate, the turnover on the Danish market for each of the years in the period 2019-2020, was between 0.05% and 0.16% of *Spørger's* total annual turnover. The Employee's work did not include contact with Danish customers, but only contact with Danish dealers and other business partners. However, where the sale of products took place through individual orders, the Employee could confirm orders from customers where the selling price was within a determined price range.

Regarding the Employee's place of work, § 2(1) of the employment contract stated: "The employee's place of work is with the customers and at his private address (home workplace." The tasks assigned to the employee involved significant travel outside of Denmark and was estimated to have constituted between 50% to 60% of his total working time for the company. When the Employee was not travelling, the Employee's activities on behalf of *Spörger* was carried out from his residence in Denmark. The Employee's work that related to sales into the Danish market constituted a maximum of 5% of the Employee's total work effort.

The *Skatterådet* looked to the definition of a P.E. in the income tax treaty between Denmark and Germany ("DG Treaty") to rule that a P.E. of *Spörger* existed in Denmark.

Paragraph 1 of Article 5 (Permanent Establishment) defines a P.E. to be "a fixed place of business through which a company's business is wholly or partly carried on." The provision is standard and the *Skatterådet* explained the three conditions for a fixed place of business to exist:

- There must be a place of business, which covers all premises, fittings or installations that are actually used to carry out the company's business.
- The place of business must be fixed, which means that a connection is required between the place of business and a specific geographical location, and must not be of a temporary nature.
- The foreign enterprise must wholly or partially carry on its business through the fixed place of business.

Even if all three conditions are met, a P.E. will not exist if he activity carried out could be characterized as being of a preparatory or auxiliary nature. See paragraph 4(e) of Article 5 of the DG Treaty.

In determining that a P.E. existed, the *Skatterådet* determined that *Spörger* gained an advantage from the work being carried out in Denmark the activity that was carried on by the employee from his home in Denmark constituted a surrogate for activity that would have been carried in at office in Denmark. It did not matter that the Employee's work related to the Danish market constituted not more than 5% of his annual time at work when 40-50% of his time at work for each year was carried out from Denmark. The important factors were as follows:

- The Employee had access to his own workspace at his place of residence in Denmark, making his residence a place of business.

- The Employee's employment was not time limited.
- The Employee's work for *Spörger* was continuous and of a long-term nature.

The Employee was tasked with developing and building relationships with dealers in Africa, Belgium, Germany, the Netherlands, the Baltics and the Nordic countries. The Nordic market includes Denmark. Hence, the location of the Employee in Denmark apparently had value for *Spörger*, because Denmark near the Spörger's customers. The work in Denmark is thus not only due to private circumstances.

The tasks the Employee performed from home in Denmark were closely related to the sales activities in connection with customer visits in Denmark and abroad, and was part of the company's core activity. This was also evidenced by the Employee's title as area sales manager. This indicated that the employee's work was of a significant nature, and included more than tasks of a preparatory or auxiliary nature.

FINLAND

On December 3, 2021, the Finnish Supreme Administrative Court held that the activities of three employees of a Swedish company who carried on product promotion activity is Finland did not constitute a P.E. under the income tax treaty in effect among the Nordic countries.[3]

The Swedish company, C AB (the "Company") was part of an Australian group, which researched, manufactured, marketed and sold biopharmaceutical products. The Company was responsible, among other things, for product sales and marketing in the Nordic countries and maintained three employees in Finland (the "Finland Employees"). The Finland Employees were tasked with presenting the company's products to doctors and other medical experts in Finland. The Finland Employees did not have the right to take legal action on behalf of the company, receive orders, or negotiate the sales price specified for the company's products or other contract terms. The company did not have offices in Finland. Rather, the Finland Employees worked from their homes.

The *Verohallinto*, the Finnish Tax Administration, contended that the activity of the three employees in Finland constituted a P.E. of the Company. In the view of the *Verohallinto*, the activity of the three employees in Finland was tied to the sales activity carried on in Sweden. A deficiency it tax was asserted, and the deficiency was affirmed by a lower-level administrative court. That determination was reversed by the Supreme Administrative Court.

The Supreme Administrative Court established that, to evaluate whether an activity is auxiliary or preparatory in nature, attention should be focused on the kind of activity that is practiced in Finland. Activities that are part of the Company's core business cannot be considered auxiliary or preparatory. Core business activities are considered to be activities that form a significant and determining part of the Company's business. In the facts presented, the three employees were not involved in sales. Consequently, the Company cannot be considered to have a fixed place of business in Finland. The activity of visiting doctors and other medical experts to build product awareness are preparatory in nature. The Company's core business is not product presentation and the facts do not show that the product presentation

[3] ECLI identifier: ECLI:FI:KHO:2021:171. Reported unofficially here.

accrued income directly in Finland. The Company's activities in Finland support the operations of the main facility in Sweden.

SPAIN

In January of 2022, the Spanish Tax Authorities ("STA") held that the presence of an employee of a U.K.-based company was insufficient to establish a permanent establishment for the company and that the employee was not a dependent agent of the employee.

The consultant (the "Employer") resided in the U.K. and employed an English national (the "Employee"). Prior to COVID-19, the Employee was based in London, where he material activity generating profits for the business and participating in top management. The Employee was not granted the authority to sign contracts in the name of the Employer or on behalf of the employer. Nor did he ever sign contracts even in the absence of authority.

The Employee owned a house in Spain, where he spent weekends and holidays. The Employee was in Spain in March 2020 when the COVID-19 lockdown in place was announced. When travel restrictions eased, the Employee remained in Spain for personal reasons. Because he was physically present in Spain for more than 183 days during 2020, he became a Spanish resident.

During 2020, he continued to work for the Employer while living in Spain. The Employer did not bear any additional expenses in relation to accommodation nor did the Employer grant any renumeration for carrying out his work in Spain. By the end of 2020, the Employee requested a formal assignment to Spain, which was turned down. The Employee resigned in February 2021.

A ruling was requested by the Employer from the Spanish Tax Authority ("S.T.A.") the Employer did not maintain a P.E. in Spain in 2020 by reason of the presence or the activities of the Employee.

The S.T.A. considered two possibilities under which the Employer might have established a permanent establishment in Spain. One related to the existence of a fixed place of business in Spain from which business activity was carried out. The other related to the existence of a dependent agent in Spain having the power to bind the Employer. The S.T.A. ruled that no P.E. existed.[4]

Fixed Place of Business

The S.T.A. turned to the O.E.C.D. Secretariat Report, "Updated guidance on tax treaties and the impact of the COVID-19 pandemic,"[5] in particular to paragraphs 14 to 19 related to employees working in home offices.

> **Home office**
>
> 14. Whilst noting that the issue of whether a PE exists is a test based on facts and circumstances, in general, a place must have a certain

[4] The ruling is Consultation number V00gg-22 issued by the State Secretary of Finance, General Directorate of Taxes, and is dated January 18, 2022. It appears here.

[5] Available here.

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.

15. Paragraph 18 of the Commentary on Article 5 of the OECD Model 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.

16. During the COVID-19 pandemic, individuals who stay at home to work remotely are typically doing so as a result of public health measures: it is an extraordinary event not an enterprise's requirement. Therefore, considering the extraordinary nature of the COVID-19 pandemic, teleworking from home (*i.e.* the home office) because of an extraordinary event or public health measures imposed or recommended by government would not create a PE for the business/employer, either because such activity lacks a sufficient degree of permanency or continuity or because the home office is not at the disposal of the enterprise. In addition, it still provides an office which in the absence of public health measures is available to the relevant employee. This applies whether the temporary work location is the individual's home or a temporary dwelling in a jurisdiction that is not their primary place of residence.

17. If an individual continues to work from home after the cessation of the public health measures imposed or recommended by government, the home office may be considered to have certain degree of permanence. However, that change alone will not necessarily result in the home office giving rise to a fixed place of business PE. A further examination of the facts and circumstances will be required to determine whether the home office is now at the disposal of the enterprise following this permanent change to the individual's working arrangements.

18. Paragraphs 18 and 19 of the Commentary on Article 5 of the OECD Model indicate that whether the individual is required by the enterprise to work from home or not is an important factor in this determination. Paragraph 18 explains that where 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 (*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. As an

example, paragraph 19 notes that where a cross-border worker performs most of their work from their home situated in one jurisdiction rather than from the office made available to them in the other jurisdiction, one should not consider that the home is at the disposal of the enterprise because the enterprise did not require that the home be used for its business activities.

19. In conclusion, individuals teleworking from home (*i.e.* the home office) as a public health measure imposed or recommended by at least one of the governments of the jurisdictions involved to prevent the spread of the COVID-19 virus would not create a fixed place of business PE for the business/employer.

On the basis of the above, the S.T.A. determined that in 2019, no P.E. existed. However, the Employee remained in Spain throughout 2020. Consequently, the S.T.A. examined whether the Employee's home became available to the Employer for the conduct of its business. Ultimately, the S.T.A. ruled that the Employee's residence was not made available to the Employer as a place of business, based on the following facts:

- The Employee decided unilaterally to continue in Spain.
- The Employer maintained a place available to the Employee in the U.K. where the Employee could carry his work on a face-to-face basis with colleagues in the U.K.
- The Employer did not bear any expenses of the premises in Spain, nor did the Employee receive special pay to carry out work from in Spain; in other words, the Employee never received customary expat stipends.

"Ultimately, the S.T.A. ruled that the Employee's residence was not made available to the Employer as a place of business. . ."

Dependent Agent

The S.T.A. concluded that during the months that the public health measure lasted, factors listed in paragraphs 20 and 21 of the O.E.C.D. updated guidance suggested that the Employee did not "habitually" conclude contracts on behalf of the Employer.

21. An employee's or agent's activity in a jurisdiction is unlikely to be regarded as habitual if they are only working at home in that jurisdiction because of an extraordinary event or public health measures imposed or recommended by government. Paragraph 6 of the 2014 Commentary on Article 5 explains that a PE should be considered to exist only where the relevant activities have a certain degree of permanency and are not purely temporary or transitory. Paragraph 33.1 of the Commentary on Article 5 of the 2014 OECD Model provides that the requirement that an agent must "habitually" exercise an authority to conclude contracts means that the presence which an enterprise maintains in a jurisdiction should be more than merely transitory if the enterprise is to be regarded as maintaining a PE, and thus a taxable presence, in that jurisdiction. Similarly, paragraph 98 of the 2017 OECD Commentary on Article 5 explains that the presence which an enterprise maintains in a jurisdiction should be more than merely transitory if the enterprise is to be regarded as maintaining a PE in that jurisdiction under Article 5(5).

> 22. A different approach may be appropriate, however, if the employee was habitually concluding contracts on behalf of enterprise in their home jurisdiction before the COVID-19 pandemic.

Although the Employee had been in Spain for more than six months in 2020, the data provided was not conclusive on whether the activities carried out by the Employee could be identified as activities of an agent, since it was not indicated that they acted as such. Consequently, the exceptional and temporary change of place where the Employee carried out his employment due to the COVID-19 pandemic did not create a new permanent establishment for the Employer. In reaching its decision, the S.T.A. pointed out that, in last analysis, the existence of a dependent agent who habitually exercises an authority to conclude contracts is a question of fact. If other facts existed, the answer might be different.

CANADA

In Canada, a nonresident is deemed to carry on a Canadian business where the nonresident solicits orders or offers anything for sale in Canada through an agent or servant, whether the contract or transaction is to be completed inside or outside of Canada or partly in or partly outside of Canada.[6] The rule is statutory, and overrides common law decisions reaching an opposite conclusion that no trade or business is carried if no contract is concluded in Canada.

Article 12(1) of the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* ("the M.L.I.")[7] adopts the policy of the Canadian statutory rule. It provides as follows:

> ***Article 12 – Artificial Avoidance of Permanent Establishment Status through Commissionnaire Arrangements and Similar Strategies***
>
> 1. Notwithstanding the provisions of a Covered Tax Agreement that define the term "permanent establishment", but subject to paragraph 2, where a person is acting in a Contracting Jurisdiction to a Covered Tax Agreement on behalf of an enterprise and, in doing so, habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, and these contracts are:
>
>   a. in the name of the enterprise; or
>
>   b. for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use; or
>
>   c. for the provision of services by that enterprise,
>
> that enterprise shall be deemed to have a permanent establishment in that Contracting Jurisdiction in respect of any activities which that

---

[6] Subsection 253(b) of the Income Tax Act.

[7] Available here.

person undertakes for the enterprise unless these activities, if they were exercised by the enterprise through a fixed place of business of that enterprise situated in that Contracting Jurisdiction, would not cause that fixed place of business to be deemed to constitute a permanent establishment under the definition of permanent establishment included in the Covered Tax Agreement (as it may be modified by this Convention).

2. Paragraph 1 shall not apply where the person acting in a Contracting Jurisdiction to a Covered Tax Agreement on behalf of an enterprise of the other Contracting Jurisdiction carries on business in the first-mentioned Contracting Jurisdiction as an independent agent and acts for the enterprise in the ordinary course of that business. Where, however, a person acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, that person shall not be considered to be an independent agent within the meaning of this paragraph with respect to any such enterprise.

Canada surprisingly has opted out of Article 12 of the M.L.I. entirely and has also opted out entirely of Article 13, which targets commissionaire arrangements, Article 14, which targets the splitting up of contracts, and Article 15, which targets independent agents acting almost exclusively for one or more enterprises to which the agent is closely related.

Canada's tax treaties are based on the O.E.C.D. Model Tax Convention on Income and on Capital and provide that a permanent establishment will not be created where the activities of an employee are merely preparatory or auxiliary.

In 2006, the Canada Revenue Agency released Ruling 2006-0173601R3.[8] In the ruling, a foreign bank requested a determination on whether it would be deemed to have a permanent establishment in Canada in the following fact pattern:

- It would maintain a staff of three Canadian resident employees.
- The employees would work in a rented office.
- The purpose of the office would be to promote the Foreign Bank's services to selected Canadian industries and potential Canadian customers, to support the Foreign Bank's customers in Canada, and to liaise with the Foreign Bank head office in the Foreign Treaty Country.
- The Canadian resident employees would have no authority to conclude contracts on behalf of the Foreign Bank relating to its core business operations.
- All services offered by the Foreign Bank to Canadian customers such as traditional financings, term loans, participation in syndicated financings and mezzanine financings would be carried on through offices of the Foreign Bank outside of Canada.

The C.R.A. concluded that the Canadian employees did not generate a permanent establishment for the Foreign Bank because the Canadian employees' activities

[8] The ruling appears here.

were considered to be activities of a preparatory or auxiliary character for the purposes of the Treaty.

In *Knights of Columbus v. The Queen*,[9] the Tax Court of Canada held that the field agents' premises in Canada did not constitute a permanent establishment for the Knights of Columbus, a U.S. corporation. The Court rejected the Minister of National Revenue's assertion that even though the agents were present in Canada, their homes constituted a fixed place of business for the Knights of Columbus.[10] The houses were not available at the disposal of the Knights of Columbus.

While the case remains good law as to its facts, a different conclusion might be reached in different facts. The Knights of Columbus might be viewed as having the agents' premises at its disposal, for example, if the Knights of Columbus paid for all expenses in connection with the premises, required that the agents have a room in the house maintained exclusively as a home office containing specific office equipment and sufficient size to meet with clients. In such circumstances the premises might be viewed as being at the disposal of the Knights of Columbus even if it did not hold a key to the home of its field agents.

"While the case remains good law as to its facts, a different conclusion might be reached in different facts."

9 2008 TCC 307.

10 See paragraph 78 of the opinion.