

International Tax Impacts of COVID-19

May 20, 2020

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Agenda

- I. Introduction
- II. Tax Concessions, Extensions, and Questions Raised in Various Jurisdictions
- III. Practical Considerations for Applying the Arm's Length Principle During an Economic Crisis
- IV. Permanent Establishment Concerns and Country-Specific Guidance
- V. Q&A

Tax Concessions, Extensions and Questions Raised in Various Jurisdictions

Overview

- Sales Tax/VAT
- Tax Audits
- Objections/Protests and Appeals
- Corporate Income Tax and Further Taxpayer Relief
- MAP, APA and CbC Reporting

UK Measures

Sales Tax (VAT) Payments:

- VAT payment deferral: for normal payments due between 20 March 2020 and 30 June 2020.
- No general Customs Duty deferral (unless already within a Duty Deferment Account (DDA), and only by HMRC agreement)
- VAT Returns: No deferral – filings are due as normal.

Tax Audits (VAT or otherwise), objections and appeals: No stated policy changes. Deadlines are not extended.

Other Tax Liabilities (Inc. Corporation Tax): ‘Time To Pay’ agreements can be requested and “will take into account C-19”

- No automatic deferrals
- No extension to filing deadlines

International-Specific Reporting (Transfer-pricing, APA’s / CbC reporting etc.): No stated policy changes or extensions.

UK Measures

Subsidised Payroll: The Job Retention Scheme

- 80% of wages, up to £2,500 per individual per month, for staff placed on “furlough” to the end of June.
- It is estimated that the Scheme will cost £14bn a month.

Business Property Rates: Grants and reliefs.

Personal Income Tax Deferrals

Relief for Small Business Operated by Self-employed Workers (similar to payroll “furlough” scheme)

Various Loan Schemes:

- Government-backed soft-loans, administered by high-street banks
- Interest and capital repayment holidays
- Specifically for funding issues caused by COVID-19

Spain Measures

Payment Extensions/Deferrals

- Self-assessments declaration (VAT, Withholding Taxes, CIT instalments) during 6 months. Max. 30k EUR. Only applicable to SME (6M EUR). First 3 months free, then 3,75% interest. No guarantee
- Assessments carried out by the Tax Authorities. Until May 30th
- Self-assessments and assessments carried out by Tax Authorities during 1 month. For Mini SME (-600k EUR)
- VAT and Utilities Duties for 6 months – Energy suppliers
- Custom tariffs during 6 months. Max. 30k EUR. Only applicable to SME (6M EUR). First 3 months free, then 3.75% interest. With guarantee
- Change of CIT instalment method for SMEs
- VAT reduction for medical equipment and goods (0%) and electronic books (4%).

Spain Measures

Filing Suspensions

- Federal level - No extensions (except Mini SMEs - May 20th)
- Regional and Municipal level - different measures

Audits & Litigations Suspensions

- Audits and other processes - suspended until May 30th
- Statue of limitations - suspended until May 30th
- Appeals - 1 month term starts on June 1st

France Measures

Value Added Tax (VAT)

No possibility to defer or cancel VAT payments. No filing deadline extension.

VAT is a major source of revenue for EU Member States and the first source of revenue for the French Government.

Unlike other EU countries, French Government rejected any possibility to defer or cancel VAT payments. Government made clear that :

- Priority, in terms of relief measures, has been given to direct taxes with direct impacts on businesses, rather than on taxes affecting end-consumers such as VAT ;
- Unlike social contributions and other direct taxes, VAT follows the level of activity of a company: if there is no or less activity, no VAT or less VAT is due ;
- Businesses are mere “collectors” of VAT on behalf of the Government;
- Government needs VAT revenue to continue funding public services and to fund COVID-19 relief measures. Government also needs to keep receiving markets financing.

France Measures

Accelerated VAT Refunds

Whilst businesses shall preferably carry forward their VAT credits, during the lockdown period those claiming VAT credit refunds can benefit from accelerated refund procedures. Tax authorities are strongly committed in speeding up VAT credit refunds. This can be a significant relief measure for businesses in terms of cash flow.

Reduced VAT Rate of 5,5%

Reduced VAT rate of 5,5% (instead of standard 20% rate) is applicable to domestic supplies and EC acquisitions of masks, protective equipment and hydro-alcoholic solutions from March 2020 until December 31, 2021.

Customs Duties

Possibility to defer customs duties payments for businesses facing proven financial difficulties

France Measures

Corporate Income Tax (CIT) & Other Direct Taxes

Businesses facing financial difficulties due to COVID-19 outbreak can **defer payments of CIT and other direct taxes** (TS, CVAE- Business Contribution on Added Value, CFE- Business Contribution on Property) for 3 months, without justification, and without penalties or late payment interests. Said measure is applicable to direct taxes due in March, April, and May 2020. In order to benefit from that measure, a specific form must be sent to the tax authorities.

As an additional relief measure, CIT filing deadline has been extended from May 20, 2020 until June 30, 2020. Payment of CIT balance is also postponed until June 30.

Cancellations of direct tax liabilities (and late payment interests and penalties) are also available on a case-by-case basis for businesses facing severe financial difficulties that cannot be solved with a deferment. Relevant companies must evidence the impossibility to pay direct taxes based on their specific circumstances (decrease of revenue, cash flow situation, other debts to pay, etc.).

France Measures

NB: for large corporations (more than 5000 employees or revenue exceeding €1,5bn in France), deferments and tax rebates are available if the French entities of the Group commit not to distribute dividends in 2020 and if said entities have no subsidiaries (without substantiation) based in a non-cooperative jurisdiction.

Noteworthy is that accelerated refunds of tax credits, especially R&D tax credits (CIR/CII), are available. This is a significant relief measure for businesses in terms of cash flow.

Tax Audits

- Ongoing tax audits were suspended during the lockdown.
- No new audits will start during the COVID-19 State of Emergency
- Suspension of ongoing audits and the absence of new audits go hand in hand with a suspension of statutes of limitations and procedural deadlines.

Germany Measures

General deferral of tax payments for taxpayers which can demonstrate that they are directly and not insignificantly affected may until December 31 ,2020 submit applications for the deferral of taxes which are already due or will become due until that date (December 31,2020).

No definition is provided of directly and not insignificantly impacted other than positive attitude of tax authorities to assess this requirement.

This general measure applies to all taxes including VAT, personal and corporate income tax and local trade tax. Not applicable for withholding tax on for example royalty and interest payments

- Possibility of loss carry back acceleration , i.e. a retroactive reduction in prepayments made for 2019 for both personal and corporate tax purposes if losses are anticipated in 2020.
- Reduction of tax prepayments, if applied for.

Germany Measures

- Bonus payments up to € 1,500 can be made tax free if related to COVID-19 activities.
- Social security contributions, deferral only available if all other avenues are exhausted.
- Tax treaty relief for cross border commuters for NL, Austria and Luxembourg cross border situations
- Waiver of enforcement measures and penalties in situations where tax payers can show direct and not insignificant impact of COVID-19
- Extensive non-tax relevant measures such as subsidies for small business enterprises up to €15,000 and a new €2 billion fund available to start ups and young technology companies.
- Strengthening of venture capital investors through government backed guarantees

Netherlands Measures

- Extension for payment for three months through special request, applicable for all taxes including payroll tax, VAT, and corporate tax
- Introduction of a so-called Corona reserve to facilitate 2020 anticipated loss which can be reflected in not yet filed 2019 corporate return.
- Reduction of penalty interest to 0,01% and waiver of late payment penalty assuming late filing request is made
- EU customs rules applied in line with EU policy, such as no excise on protective equipment etc.
- Non tax related measures include temporary emergency bridging measures which include funds available for compensation of salary costs for businesses that expect 20% reduction in revenue due to COVID-19
- Extension of credit guarantees for companies which face difficulties obtaining bank funding.

Canada Measures

- \$73-billion Wage Subsidies program extended to August
- Tax measures to help with cash flow include:
 - Payment of FY2019 corporate income tax deferred to Sept. 1
 - Remittances of sales taxes (VAT) and customs deferred to June 30
 - CRA expediting payment of SR&ED credits, deferring audits to later

Canada Measures

- International Tax Audits (Transfer Pricing)
 - CRA now resuming transfer pricing audits (June)
 - Prioritizing imminent treaty limits and Statutes of Limitations
 - **Beware:** CRA resuming 3-month requests for TP documentation (mail)
 - Expect high intensity audits/controversy following COVID19
 - LRD arrangements put to the test?
 - Who manages risk under COVID19 in local market? Global/local strategies?
- Domestic Tax Audits
 - Slow; CRA prepared to skip year about to be statute-barred (FY2015)

Canada Measures

- Competent Authority
 - APAs resuming, accepting virtual pre-filing meetings later in 2020
 - Site visits?
 - APAs for low-risk / limited-risk distributors?
 - **Beware:** Rigid new policy on downward adjustments – don't miss your post year-end adjustments for 2019 and year-end adjustments in FY2020!
- Appeals
 - Virtual conferences with CRA Appeals on larger cases
 - Tax Court closed, possibly resuming in June?

U.S. Measures

CIT Extension of Filing Deadline

From the typical April 15 due date to July 15, 2020 / State rules vary by State

CIT Payment Deferral

July 15 for Federal income tax / State rules vary by State

Ongoing Audits

- Will proceed, but without in-person contact (IRS People First Initiative).
- For LB&I examinations, the following will also continue as usual (again, without in-person contact): Compliance Assurance Process, Large Corporate Compliance, FATCA, and Qualified Intermediary programs (April 14 LB&I Memo).

U.S. Measures

New Audits

Generally no new audits unless SOL expiring or the examination arises from taxpayer action. LB&I auditors may expand existing audits to include new tax years, with manager approval.

Auditors are permitted to work on new cases without opening an examination (e.g., audit planning) as long as taxpayer contact is delayed until after the emergency declaration is lifted.

The IRS has made clear that it will take steps necessary to protect all applicable statutes of limitations (e.g., requesting extensions, issuing Notices of Deficiency) (IRS People First Initiative). However, if a statutory period is not expiring during 2020, the IRS says it is unlikely to take such actions before July 15, 2020.

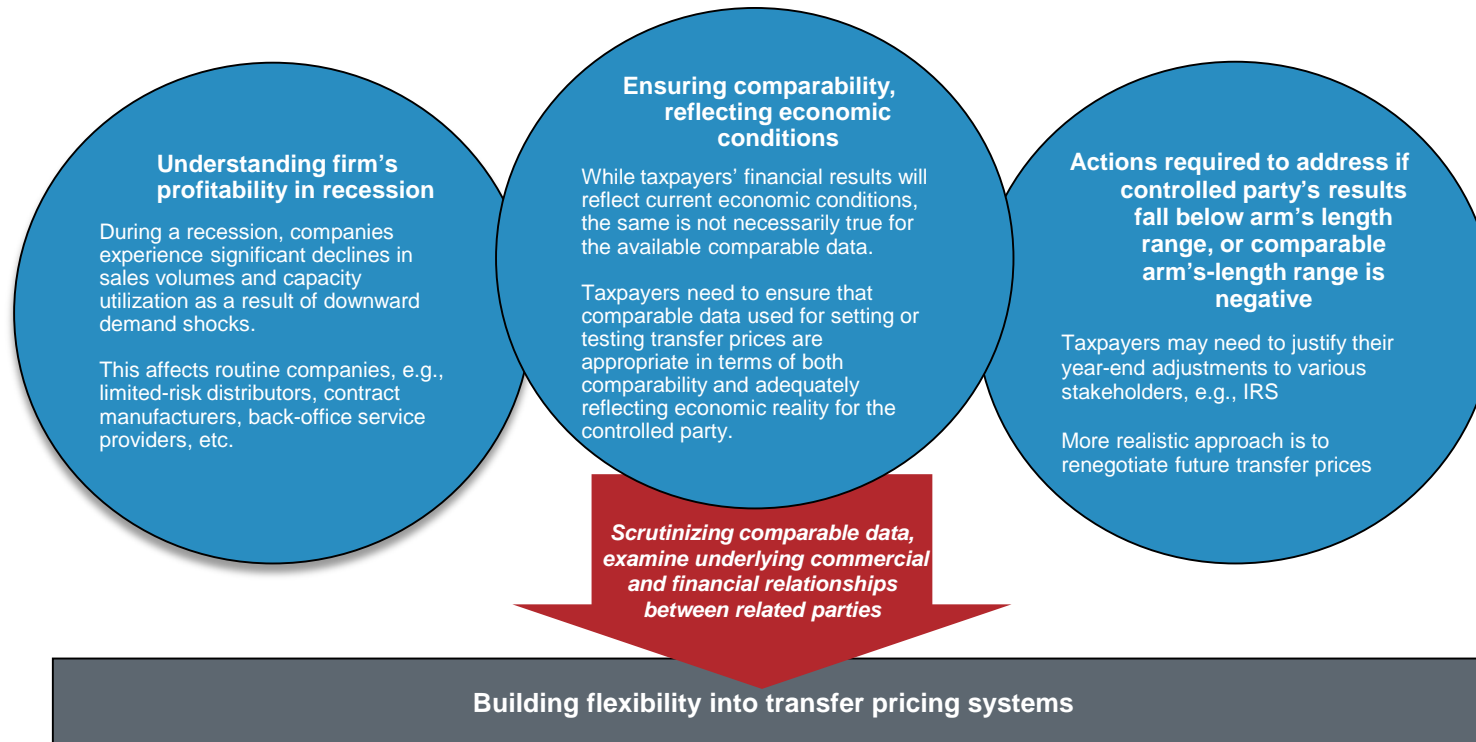
Objections/Protest and Appeals

U.S. Tax Court has canceled all trial sessions through June 30

Practical Considerations for Applying the Arm's Length Principle during an Economic Crisis

Transfer Pricing Adjustments During An Economic Downturn

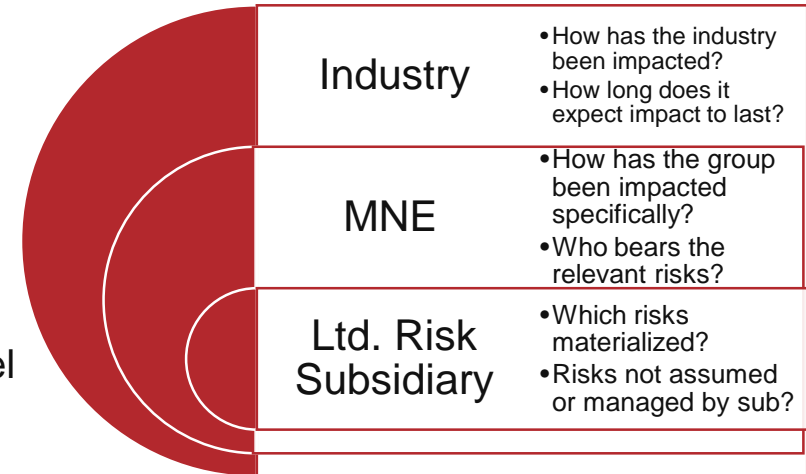
How to address the transfer pricing challenges brought to us by the current economic crisis?



Is There a Need for Adjustment?

Enquiry may include:

- Understanding relevant economic circumstances
 - Understand the impact of COVID on the industry, the MNE in question, and the individual subsidiary under analysis
- Pinpointing the risk
 - What are the particular risks that materialized at the subsidiary level
 - How to quantify the materialization of the risk
- Assessing arm's length parties' behavior
 - Who is contractually obliged to assume that risk (would arm's length parties have agreed to that)
 - Would arm's length parties have re-negotiated pricing as a result of the materialization of such a risk (if so, for how long)
 - Who is actively managing the risk, who is financially equipped to assume the risk



When to Adjust for Negative Impact on Low-risk Entity?

Year-End TP adjustments (adjustment prior to fiscal year end – may be accrued throughout the fiscal year)

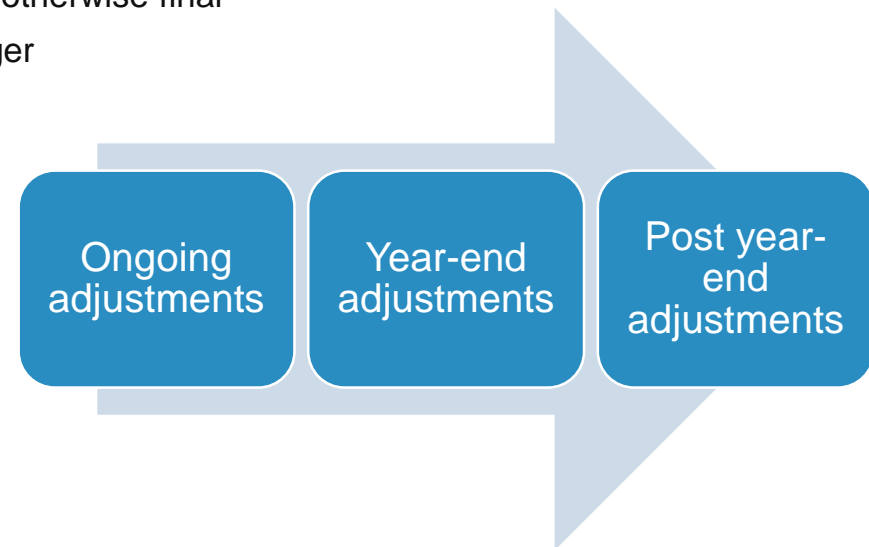
- Advantage: Negative impact on tested party is precisely quantified for the entire year
- Drawback: 2020 benchmark comp data not yet available

Post year-end TP adjustments (after fiscal year end, but before filing tax return)

- Advantage: FY2020 benchmark comp data available and tested party data is otherwise final
- Drawback: Cash flow impact suffered by the subsidiary is extended even longer

Ongoing adjustments (throughout the fiscal year)

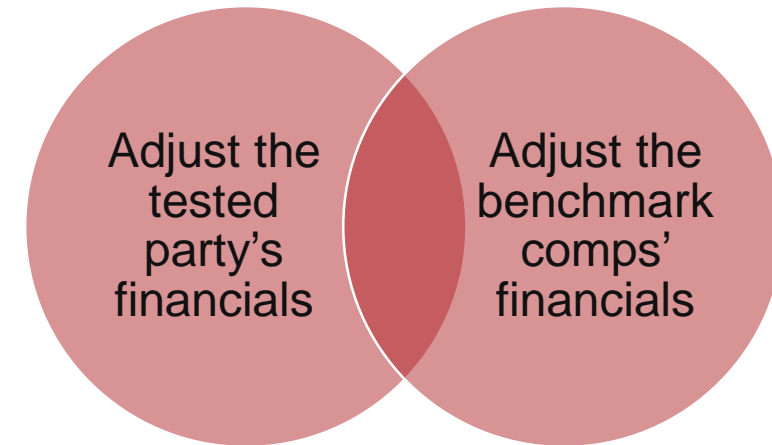
- Advantages:
 - Resolves cash flow impact at source
 - Avoids interest on eventual loans
 - Addresses issue concurrently
- Drawbacks:
 - FY2020 benchmark comp data unavailable
 - Impact of pandemic on tested party in flux



How to Adjust for Ongoing COVID-19 Impact on Limited Risk Subsidiary

Adjustments to tested party financials

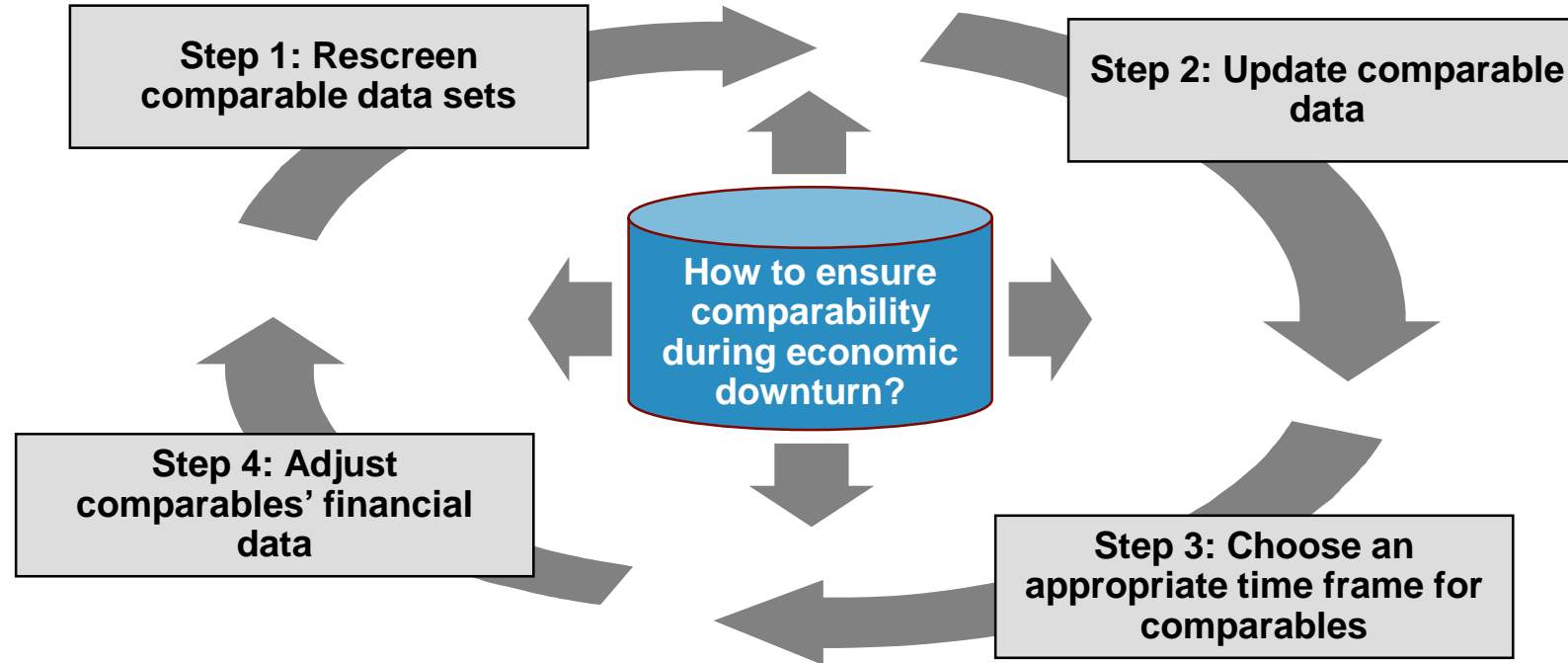
- Identify specific risks to be assumed by foreign related party
- Quantify impact on actual results of controlled party
- Price renegotiation? Amendment to contract?
- Monthly billing vs accruals for year-end adjustment
- Reverting back to pre-pandemic pricing
- Other considerations



Adjustments to benchmark financials of comparables (see following slides)

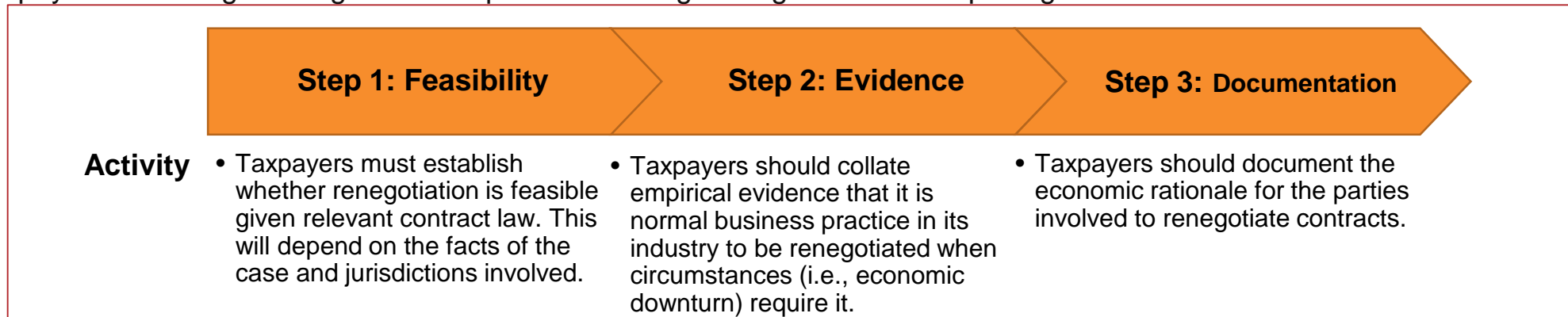
Ensuring Comparability, Reflecting Economic Conditions

To ensure that potential comparable data are comparable and reflect economic reality for controlled parties, a four-step process can be envisaged.



Required Actions

If controlled party's results fall below arm's length, related-party taxpayers should renegotiate their transfer pricing. Additionally, taxpayers need to go through three steps before renegotiating their transfer pricing.



When comparable data indicate that all or part of the arm's-length range is negative, taxpayers need to first assess whether take-or-pay contracts (i.e., commercial arrangements with third parties that insulate them from risk) are prevalent in their industries; then document both the economic and business justification for such arrangements.

If the conclusion arrived at is that a controlled party should receive a guaranteed basic return, then this would indicate some sort of problem with the original comparable data that suggested the arm's length results to be negative.

If the conclusion arrived at is that the risk of loss should be shared among controlled parties, it can be reasonably anticipated that some routine players will need to absorb a portion of the loss.

Managing Challenges

Practical Illustrations

- Operational changes, shuttering facilities, transferring production or other functions out of country
- Store closures, severance pay
- Intercompany loans, credit rating downgrades
- Relocation of risk management function
- Significant discounts/credits offered to clients
- Possible heightened requirements for “Made in America”?

Take-aways

- Transfer pricing risk exposure may not be primary concern during period of business disruption
- Asking questions earlier leaves more options open to mitigating the potential risk exposure

Permanent Establishment and Residency Concerns

Overview

- Introduction to PEs
 - Construction Site PE
 - Agency PE
 - Home Office
- Introduction to Residence Status
 - Company
 - Individuals
 - Cross border workers
- Examples
- OECD's Recommendations for COVID-19 Crisis
- Country-Specific Guidance or Administrative Positions
- Profit Allocation to a Permanent Establishment

Introduction to PEs

Construction Site

- Building site or construction or installation project
- + 6 or 12 months

Agent

- Not independent
- Acts on behalf of the company
- Authority to conclude contracts
- Habitually

Introduction to PEs

Home Office

- Degree of permanency
- Used on a continuous basis for carrying on business activities
- Company does not provide office
- Nature of the employment requires an office

Residence Status of Companies



Residence Status of Individuals



**Permanent
home available**



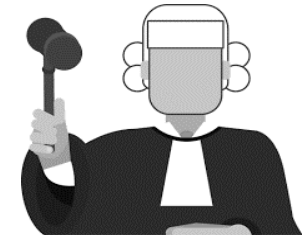
**Center of vital
interests**



Habitual abode

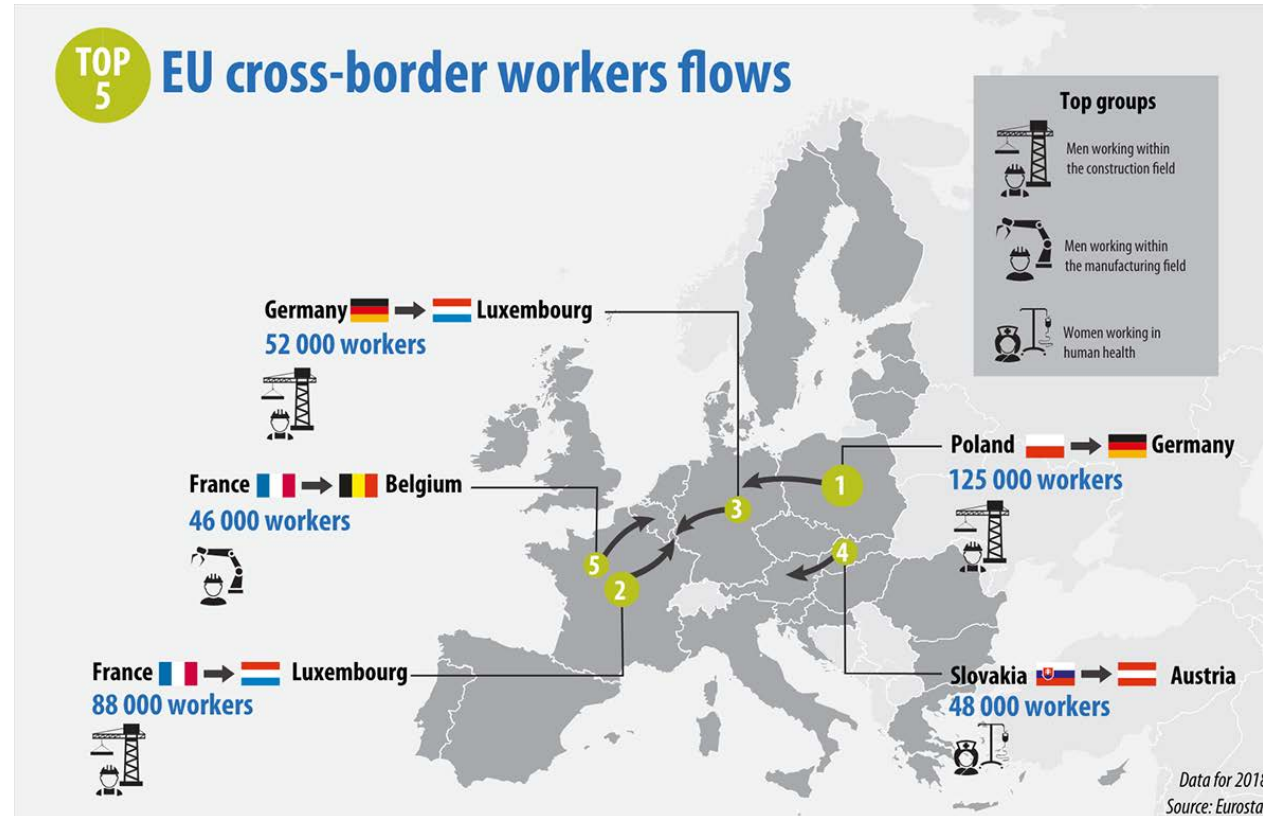


Nationality



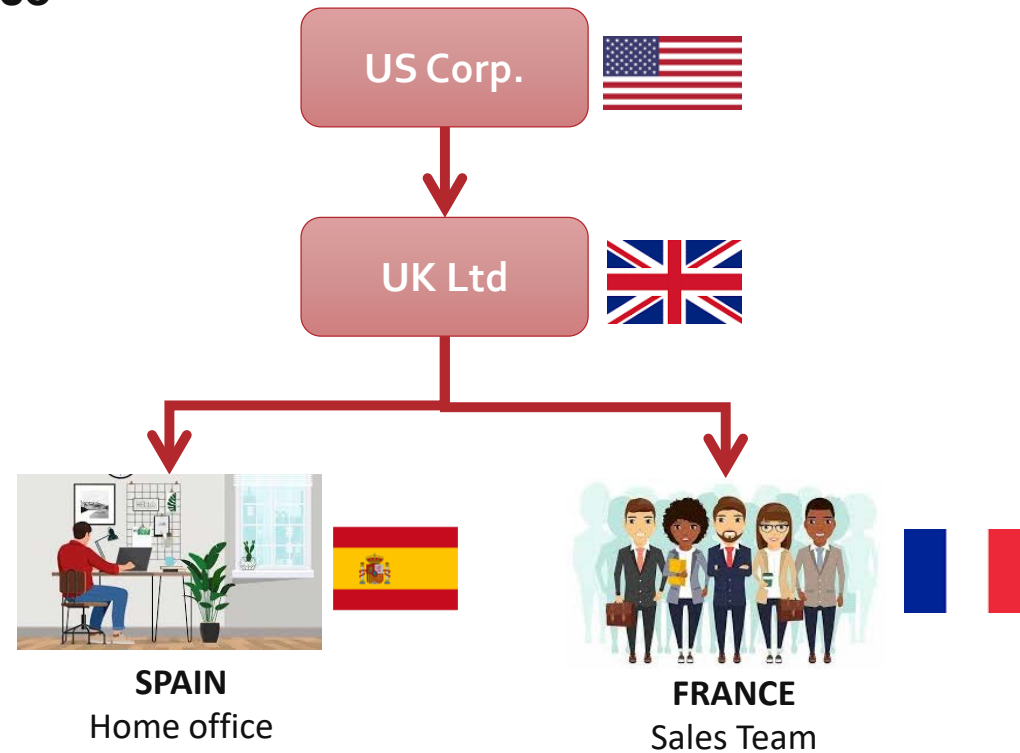
**Mutual
agreement**

Cross-border Workers



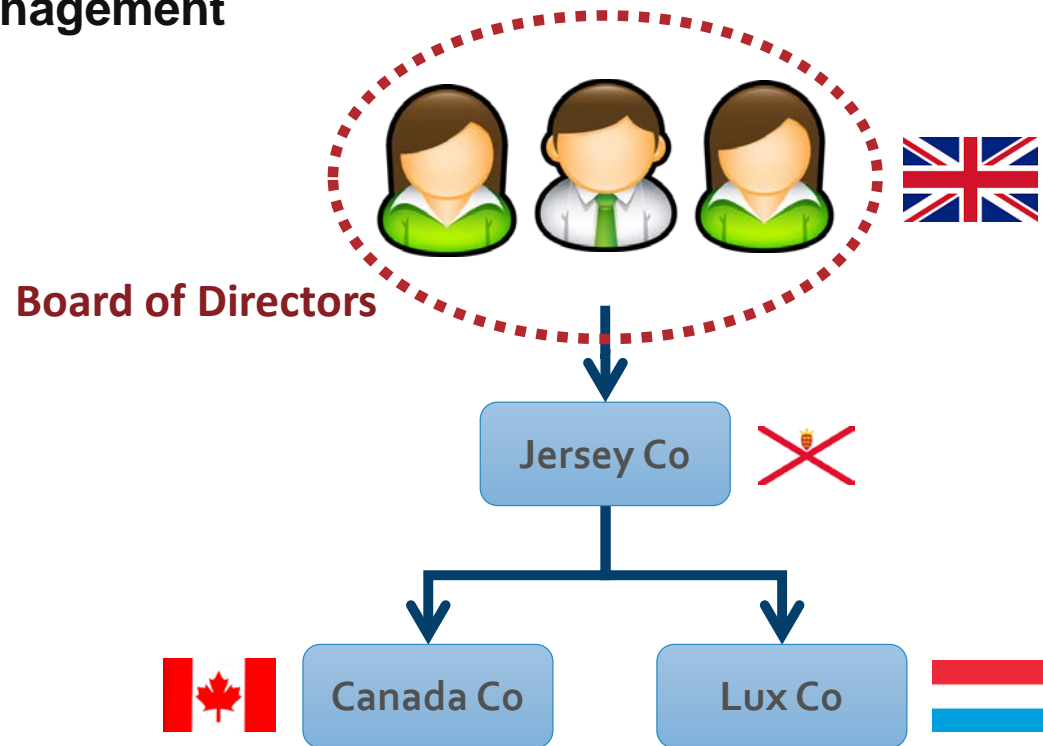
Examples

PE - Agent & Home office



Examples

Place of Effective Management



Examples

Residence VS Permanent Establishment (Agent)



OECD Secretariat Analysis

Area of Concern	Specific Issues	Guidance based on the Commentary of the OECD
1. Permanent Establishment (PE)	Home office	The exceptional and temporary change of the location where employees exercise their employment because of the COVID-19 crisis, such as working from home, should not create new PEs for the employer. Also, a home office needs to be "at the disposal" of the employer before it could constitute a PE, which would be a minority of cases
	Agency PE	Temporary conclusion of contracts in the home of employees or agents because of the COVID-19 crisis should not create PEs for the businesses
	Construction site	A construction site PE would not be regarded as ceasing to exist when work is temporarily interrupted

OECD Secretariat Analysis

Area of Concern	Specific Issues	Guidance based on the Commentary of the OECD
2. Residence of a company	Place of effective management	An extraordinary and temporary change in location of the chief executive officers and other senior executives due to the COVID-19 crisis should not trigger a change in residency
3. Income paid by employers to cross border workers during COVID-19 crisis	Article 15	Where a government has stepped in to subsidize the keeping of an employee on a company's payroll during the COVID-19 crisis, the income should be attributable to the place where the employment used to be exercised. Other employment income would normally be taxed where employment is performed. OECD is working with countries to mitigate the compliance and administrative costs for employees and employers
4. Residence status of individuals	Tie breaker rule	Unlikely that a person would acquire residence in the country where the person is temporarily because of extraordinary circumstances. But even if s/he does, if a tax treaty is applicable, the person would not be a resident of that country for purposes of the tax treaty

Country-Specific Guidance or Administrative Positions - U.S. Guidance

Foreign Business Activity in the U.S.

- In an FAQ webpage, the IRS offered relief to some foreign businesses that have activities in the United States. In determining whether a foreign corporation or nonresident alien is engaged in a U.S. trade or business or has a U.S. permanent establishment, certain business activities in the United States will not be counted for up to 60 consecutive calendar days. However, this relief is available only if those activities would not have been performed in the United States but for COVID-19 travel disruption.
- The date when the 60-day period starts is chosen by the foreign corporation or nonresident alien (or a partnership in which either is a partner), but it must start between Feb. 1 and April 1, 2020.
- The IRS stressed the need to retain contemporaneous documentation to establish a right to this relief.

Country-Specific Guidance or Administrative Positions - U.S. Guidance

U.S. Persons Doing Business in Foreign Countries

- The IRS has provided relief to U.S. persons that temporarily did business in foreign countries due to “COVID-19 Emergency Travel Disruptions.” (Rev. Proc. 2020-30)
- U.S. persons will not have an obligation to file (1) Form 8858, including an obligation to file a Form 8858 by attaching the Form 8858 to a Form 5471, with respect to a controlled foreign corporation, or (2) Form 8865 with respect to a controlled foreign partnership.

Country-Specific Guidance or Administrative Positions - Canada

The CRA Guidance on international income tax issues raised by the COVID-19 crisis page is now live on Canada.ca.

- English:
 - <https://www.canada.ca/en/revenue-agency/campaigns/covid-19-update/guidance-international-income-tax-issues.html>
- French:
 - <https://www.canada.ca/fr/agence-revenu/campagnes/mise-a-jour-covid-19/directives-problemes-fiscalite-internationale.html>

Consequences of Determination of PE

In principle, crisis should not result in negative impact:

- Administrative policies suggest no impact of “temporary” presence due to COVID
- PE does not in itself mean that significant profits of the non-resident are taxable
 - Certain activities are exempt under treaties (but expanded PE definition)
 - Depends on analysis of functions, risks and assets of the PE
- MAP relief from double taxation is available under tax treaties

Consequences of Determination of PE

But in practice:

- What is “temporary”? How long with effects of COVID last on MNE operations?
- Admin policies are not law: will tax auditors seek to leverage in the future?
- Analysis of functions, risks and assets involved at the PE level usually not simple
- MAP: time/resources, complex if multiple jurisdictions, no penalty protection

Think about mitigating PE risk?

- Resolution, minutes, correspondence on temporary and exceptional nature of the arrangements?
“preparatory or auxiliary” nature of activities?
- Documenting contractual rights and obligations; lack of authority to bind, etc.?
- Other

Q&A

Thank You!

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