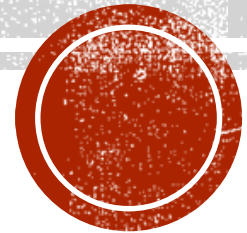


# HOW DO WE RE-THINK THE TAX RESIDENCE FOR CORPORATIONS IN THE DIGITAL AGE?

Session 5: International corporate taxation challenges

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# ROADMAP

- I. The rise of telework and the increasing mobility of individuals
- II. Foreseeable impact of mobility of individuals in the application of corporate tax residence rules
  - Residence rules based on decision-making as both domestic and treaty rules
  - Tax opportunities arising from mobility
- III. Proposed amendments to domestic and treaty residence rules
- IV. Reflection on the future of corporate tax residency



# I. RISE OF TELEWORK

The pandemic has made us all call into question the actual need to carry out work in person → cost-benefit analysis between

## On-site work

Overall (historically assumed) benefits

- Knowledge exchanges
- Better coordination
- Teambuilding



## Remote work

Benefits for businesses

- Replication of in-person work via videocalls?
- Reduction of business expenses (real estate investment, office rentals, utility bills)
- Higher productivity rates

Benefits for individuals

- Greater work-life balance
- Reduction of commuting time and other time inefficiencies
- Flexibility to relocate outside large cities

Benefits for society

- Reduction of traffic and greenhouse emissions
- Counteract rural depopulation



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- EU average of regular remote workers from 8,2% (2018) to 12,3% (2021)
- 40,7 million remote workers expected by 2025 only in the US (> 2,5x pre-Covid)

BUT...

- Not an option for all
- Mostly high-income / highly educated portion of society




In particular...  
Direction and management = occupation that best lends itself to remote work (71%)



# II. FORESEEABLE IMPACT OF MOBILITY OF INDIVIDUALS IN CORPORATE TAX RESIDENCE

Impact is intuitively expected in corporate tax residence rules based on corporate governance. These rules play a double role:

|   | As domestic rules to grant tax residence status   | As treaty tie-breaker rules  |
|---|---|--|
| Content   | Drafted, interpreted and applied heterogeneously across jurisdictions (e.g. <i>POEM</i> , <i>CMC</i> ). Some common approaches:<br>1) Definition of the relevant level of management.<br>Strategic direction / day-to-day / shop-floor management<br>2) Identification of persons behind (fact-based approach).<br>E.g. Board of directors (strategic) Executive committee (day-to-day)<br>3) Localization of decision-making (fact-based approach) | General tendencies: <ul style="list-style-type: none"><li>• Interpretation according to the fiscal culture of each jurisdiction despite homogeneous wording (MCs)</li><li>• Greater emphasis on strategic decisions and board meetings (Comm OECDMC 2000-2008)</li></ul> |
| Volume<br><br>Global impact | 77,2% of jurisdictions follow them (2nd most followed)<br>83,6% combine it with formal tests<br>14,8% solely use this test<br>1,6% combine it with formal + location of economic activity tests   | 65% of treaties follow them<br>86% solely use this rule<br>14% envisage MAP in case of no agreement<br>Proportion expected to drop ↓ 4% as MLI enters into force but POEM still relevant   |

# II. FORESEEABLE IMPACT OF MOBILITY OF INDIVIDUALS IN CORPORATE TAX RESIDENCE

For directors



For entities



Flexibility to travel and perform their functions remotely

Opportunities to:

- Secure tax residence in foreign territory (fiscal competition PITs)
- Avoid tax residence and achieve stateless status (nomad life)

Flexibility to displace their directors and/or arrange relevant on-site or virtual meetings in desired location(s)

Opportunities to:

- Secure POEM + tax residence in desired territory
  - by relocating their directors (#1)
  - by arranging *ad hoc* meetings (*fly-in fly-out management*) (#2)
- Risk of double residence → POEM would ordinarily prevail in treaty scenarios
- Split and ideally avoid POEM (+ achieve stateless status)
  - by arranging meetings in different territories on a rotational basis (#3)
  - by scattering directors among territories and requesting them to hold virtual meetings (#4)

Risk of unintended multiple POEMs & tax residency → No guarantee of double taxation correction





# III. PROPOSED AMENDMENTS TO DOMESTIC CORPORATE TAX RESIDENCE RULES

Consistency-wise... corporate tax residence based on corporate governance should only be kept by jurisdictions which regard their CITs as means to control accumulation of power of directors...

| If yes: two alternatives                      |   |   | If not: repeal them + new tests   |
|---|---|---|---|
| Proposals                                     | A) Day to day management  | B) Residence directors  | a) Place of incorporation or legal seat.<br>b) Residence of the majority of the entity's shareholders.<br>c) Location of economic activity. |
|   | Keep test based on decision-making but placing focus on lower-tiers of management: <ul style="list-style-type: none"><li>• More difficult/expensive to shuttle executives rather than directors</li></ul> | Adopt test based on residence of majority of directors: <ul style="list-style-type: none"><li>• More resistant to opportunistic relocations</li><li>• Risk of dual resident / tax stateless directors</li></ul> |   |
| Tax strategies                                | Tax risks   |   |   |
| #1 Permanent relocation of decision makers    | ↓ (>\$)   | =   |   |
| #2 Fly-in-fly-out management                  | ↓ (>\$)   | X   |   |
| #3 Rotational meetings                        | ↓ (>\$)   | X   |   |
| #4 Geographical dispersion + virtual meetings | ↓ (>\$)   | X   |   |

# III. PROPOSED AMENDMENTS TO TREATY CORPORATE TAX RESIDENCE RULES

Tie-breaker rule envisaged in tax treaties to solve dual residence:

Pre OEDCDMC17

## POEM

Increasingly manipulable and uncertain as a result of the rise of mobility and virtual meetings

OEDCDMC17

## MAP + ambiguous factors

Not satisfactory solution:

- a) No-rule: does not provide accurate guidelines to guide the negotiation
- b) No guaranteed solution → denial of treaty benefits (abuse is assumed)

Way forward?

## MAP + explicit and precise factors

MAP with reference to factors in order of prevalence:

- a) Economic nexus (measurement of relevant links)
- b) Place of effective management (autonomous concept)
- c) Tax residence of selected individuals linked to entity (e.g. employees, shareholders, directors)



# IV. REFLECTION OF THE FUTURE OF CORPORATE TAX RESIDENCY

Question we should be raising is not how corporate tax residence could be saved but whether corporate tax residence is something worth saving in the first place.

- Entity is a legal fiction and so is corporate tax residency...
- Can (and should) residency be extrapolated from individuals to entities for tax purposes?
  - Probably not. *"The myth of corporate tax residence"* (D. Elkins). CCCTB and Pillar 1.
  - Yes ↓
- Has corporate tax residence rules been defined conveniently so far? Probably not ↓
  - Inheritance from private international law
  - No clear tax policy goals behind them and lack of alignment with CIT's own goals
  - Instrumental to detach taxable profits from territories where economic activities take place
  - Latest challenges posed by globalization and digitalization
- Can (and should) corporate tax residence rules be redefined? If so, how?
  - Why do we want to tax corporate income in the first place?
  - BEPS mantra (backed by 141 BEPS signatories): tax corporate income wherever they perform economic activities → Benefit rationale → Most coherent residence rule: location of economic activity test



# THANKS FOR YOUR ATTENTION

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