

COVID 19: Impact on economy and international tax

Abstract

The Covid-19 pandemic seemed like a historic turning point like World Wars I and II and the Great Depression¹. It has spread with great speed, infecting millions of people and bringing economic activity to a near standstill as countries had to impose restrictions/ lockdowns to prevent the spread of the virus. With multiple waves, the virus is continuing to disrupt economic activity and negatively impacting businesses in some countries. Most businesses had to run business contingency planning to ensure their operations continue. Though it has affected various sectors, however, the economic impact differs across different sectors. Some sectors are experiencing limited effects while, in contrast, others are experiencing significant adverse effects, including sustained losses. It can be expected that financial markets will continue to be volatile, and some sectors will likely recoup faster than others. While there are some signs of recovery in some countries, the pandemic's impact is to stay, and it will take some time for businesses to revive completely.



From the policy perspective, the crucial issue in the aftermath of the 2020 crisis will be how countries can raise finance and revenue, incentivise industrial development and achieve further economic growth. The tax has a crucial role in public policy as a source of revenue collection, which will be taken into account for reviving the economy. A lot of policy questions lies ahead of the government.

On the other hand, as a short-term measure to help individuals/ businesses deal with the impact of the Covid-19, countries are using tax systems to ease the impacts of the crisis². In the international tax context, a lot of issues did arise during the pandemic times, some of which are to stay in coming times too.

In light of the above background, the paper provides a brief background on some of the issues that have arisen because of Covid-19. Thereafter, it discusses some of the OECD guidelines (in the taxation area) issued from time to time to address the open questions. It then explores some of these issues in greater detail and briefly discusses the impact of Covid-19 on technology in the tax arena. It further discusses about the impact of Covid-19 on the Indian economy and some of the circulars issued by the Indian government to handle the international tax challenges. The paper also briefly presents the concept of autonomous organization and how algorithm-based decision-making and the concept of smart working (the practice of which seems to rise in post covid too) stating that these will impact the residential status of company/ individuals in coming times.

Keywords: Covid-19, International taxation, Transfer pricing, Residential status, Permanent establishment, Place of effective management, Tax and technology

¹ Reuven Avi-Yonah, 'COVID-19 and Fiscal Policies: COVID-19 and US Tax Policy: What Needs to Change?', (2020), 48, Intertax, Issue 8, pp. 790-793, <https://kluwerlawonline.com/journalarticle/Intertax/48.8/TAXI2020077>

² Raphael J Heffron & Jack Sheehan, Rethinking international taxation and energy policy post COVID-19 and the financial crisis for developing countries, *Journal of Energy & Natural Resources Law*, 38:4, 465-473 (2020), DOI: 10.1080/02646811.2020.1796315

Section I: Background

The economic consequence of the pandemic varies widely across economies, industries, and businesses around the globe. Countries have taken a wide range of diverse measures to safeguard its economy from the impact of Covid-19 (Covid). It seems that monetary policy alone may not address these challenges³. Hence, both fiscal stimulus and monetary stimulus are required to corroborate based on the economy's capacity to respond to this situation⁴ and achievement of stable policies.

In terms of taxation, the tax systems per se have not been significantly modified by the pandemic. Some earlier tax measures focused on mitigating the most immediate consequences by reducing liquidity constraints for some businesses and households. Tax authorities across the globe offered some or other form of tax relaxation measures, for ex: tax deferrals, extension in deadlines for tax returns, reduction in advance payments, suspended debt enforcements measures, enhanced tax refunds, postponing the collection of taxes in some cases, tax amnesty policy, relaxation of certain existing restrictions such as expanding the ability to carry back losses etc.

If we were to talk about some of the important issues from international taxation, some of the prominent ones would be transfer pricing issues, residency issues for individuals and companies, permanent establishment issues for companies because of cross border movement of workers etc. The OECD has also issued some guidance covering these areas (discussed in Section II below).

Pertinent to mention, pandemic did change the mindset of the people in terms of digitalization and digital transformation. The lockdowns and restrictions have forced tax administrations and businesses to adapt to technological solutions. On the global facade, digitalisation has increased the use of digital services tied with pressure on public finances to accelerate efforts to reach a consensus-based solution on the taxation of the digitalising economy⁵.

For brevity, the table below highlights some of the ongoing challenges and the new challenges that may arise because of the pandemic from business and international taxation point of view:

On-going challenges	New long-term challenges
Decline in revenues/ profits for some sectors (though some sectors are picking up); Liquidity and cost-management ; Recalibration of supply chains and value chains ; Issues related to tax residence of individual and companies (including smart working) ; Permanent Establishment (PE) issues ; Issues pursuant to global restructuring, other transfer pricing issues etc.	Impact on capital structure ; Issue of the residency of individuals and companies because of the changes in operating and working models ; Agile working environments and product/ service offerings to respond to changes in the business environment, changes in value propositions and/or operating models ; Renegotiation of commercial arrangements (including pricing and any potential compensation for the renegotiation itself) ; PE issues and other transfer pricing challenges etc.

³ Recovery from the COVID-19 crisis, What role will tax policy play? Deloitte (https://www2.deloitte.com/global/en/pages/tax/covid-19/tax-policy-supporting-recovery-covid19-crisis.html?nc=1&id=cy:2sm:3fb:4TAX.COVID19::6abt:20200903120000::3641366121:5&utm_source=fb&utm_campaign=TAX.COVID19&utm_content=abt&utm_medium=social&linkId=98479519 last accessed on 17 May 2021)

⁴ European Commission, Spring 2020 Economic Forecast: A deep and uneven recession, an uncertain recovery (Press Release 2020), available at https://ec.europa.eu/commission/presscorner/detail/en/ip_20_799 last accessed on 17 May 2021)

⁵ <https://www.oecd.org/tax/beps/brochure-addressing-the-tax-challenges-arising-from-the-digitalisation-of-the-economy-october-2020.pdf> last accessed on 17 May 2021

Section II: OECD analysis and guidelines issued from time to time

Earlier in the year 2020 (19 May 2020), the Organisation of economic cooperation and development (OECD) issued a report providing guidance on how tax policy (in different stages) can help support economies from this crisis, briefly covered underneath⁶:

First phase	Second phase	Third phase	Fourth phase
<p>Strong containment measures, need to strengthen the healthcare sector</p> <p>Here, the focus was on providing income support to households, strengthening patient care, and reducing pressure on health systems.</p>	<p>Gradual, partial and intermittent relaxation of containment measures</p> <p>Here, the focus was on efforts to reduce the scale of the health crisis.</p>	<p>Recovery phase, during which some economies may need support to exit the crisis</p> <p>Here, the focus was on targeting incentives at the investment that reduces future risks and strengthens resilience.</p>	<p>Restoring public finance</p> <p>Here, the focus was on ways of raising revenue to restore fiscal sustainability and to fund public investment to strengthen health infrastructure and welfare capacity.</p>

Further on 18 December 2020, OECD issued guidance on the transfer pricing implications of the Covid pandemic. The guidance mainly discussed four aspects, briefly covered underneath⁷:

<p>Comparability analysis</p> <p>It states that publicly available information regarding the effect of Covid on businesses may be useful (e.g., analysis of changes in volumes/capacity utilization, the extent to which governments contributions have been received, macroeconomic information like country-specific GDP etc.). Budgeted financial information⁸ may be used to approximate the effects of Covid on revenues, costs and margins and to support the setting of arm's length prices. It emphasized using reasonable commercial judgment supplemented by contemporaneous information to overcome information deficiencies, where feasible, allowing for an ex-post testing approach, using more than one transfer pricing method, and identifying separate testing periods.</p>	<p>Allocation of losses COVID-19-related costs</p> <p>A reasonable approach should ensure consistency in pre and post-Covid situation (for example, simple or low-risk functions are not expected to generate losses for a long time).</p> <p>In relation to specific costs, a reasonable approach is to be followed for risk assumption and how third parties would treat such costs. (for ex. accurately delineation of the controlled transaction would be required to determine which entity has the responsibility for performing activities related to the relevant costs and assumes risks related to those activities).</p>
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⁶ OECD Centre for Tax Policy and Administration, Tax and Fiscal Policy in Response to the Coronavirus Crisis: Strengthening Confidence and Resilience (OECD 2020), available at https://read.oecd-ilibrary.org/view/?ref=128_128575-o6rakt0aa&title=Tax-and-Fiscal-Policy-in-Response-to-the-Coronavirus-Crisis last accessed on 17 May 2021

⁷ OECD, Guidance on the transfer pricing implications of the COVID-19 pandemic, OECD Policy Responses to Coronavirus (COVID-19) para. 4 (OECD Publishing 2020) [hereinafter OECD Guidance on COVID-19].

⁸ Financial data of comparable companies are published atleast 12 months after closing of the year

<p>Governments Assistance programs</p> <p>Any form of government assistance programs (e.g., subsidies, tax deductions, investment allowances) should be evaluated to determine the potential impact on controlled transactions. The same may affect the comparability analysis (e.g., in terms of duration and relation between the assistance provided and the pandemic-related costs). Further, government assistance to an associated party should not change the allocation of risk in a controlled transaction.</p>	<p>Advance pricing agreements</p> <p>Existing APAs and their terms should be respected, maintained and upheld, unless a condition leading to the cancellation or revision of the APA (e.g., breach of critical assumptions) has arisen. It does notes that tax administrations may respond differently towards taxpayer’s failure to fulfil critical assumptions (i.e., revision, cancellation or revocation).</p>
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Earlier this year, on 21 January 2021, OECD further released another guidance analysing the impact of the Covid crisis on the interpretation of international tax treaty provisions (Secretariat analysis of tax treaties and the impact of the COVID-19 crisis)⁹, briefly discussed underneath¹⁰:

<p>Creation of a permanent establishment</p>	<p>It is stated that exceptional/ temporary change of the location of the place of exercise of employment, such as working from home, should not create new PEs for the business/ employers (this would not satisfy the permanence and disposal test in most cases).</p> <p>Similarly, the temporary conclusion of contracts in the home of employees or agents should not create agency PEs for businesses. Further, ‘an employee’s or agent’s activity in a State is unlikely to be regarded as habitual in most of such cases’.</p> <p>The guideline was very clear in stating that ‘individuals (employees/ agents) who stay at home to work remotely are typically doing so due to government directives; it is force majeure, not an enterprise’s requirement’.</p> <p>Further, construction site PE should not be regarded as ceasing to exist when work is temporarily interrupted because of Covid. The Commentary on Article 5(3) of the OECD Model Convention (OECD MC) explains that a site should not be regarded as ceasing to exist when work is temporarily discontinued i.e., the duration of such an interruption of activities should however be included in determining the duration of a site and hence shall affect the question of determination of the PE.</p>
<p>Changes in residence</p>	<p>The guidance clarifies that an entity's place of residence under the tie-breaker provisions included in double tax treaties is unlikely to be impacted by the fact that the individuals participating in the management and decision-making processes of the entity cannot travel due to a public health measure imposed or recommended by at least one of the governments of the jurisdictions involved. It regards that a temporary change in location of board members or other senior executives should</p>

⁹ OECD Secretariat analysis of tax treaties and the impact of the COVID-19 crisis (2020); <https://www.oecd.org/coronavirus/policy-responses/oecd-secretariat-analysis-of-tax-treaties-and-the-impact-of-the-covid-19-crisis-947dcb01/> last accessed on 17 May 2021

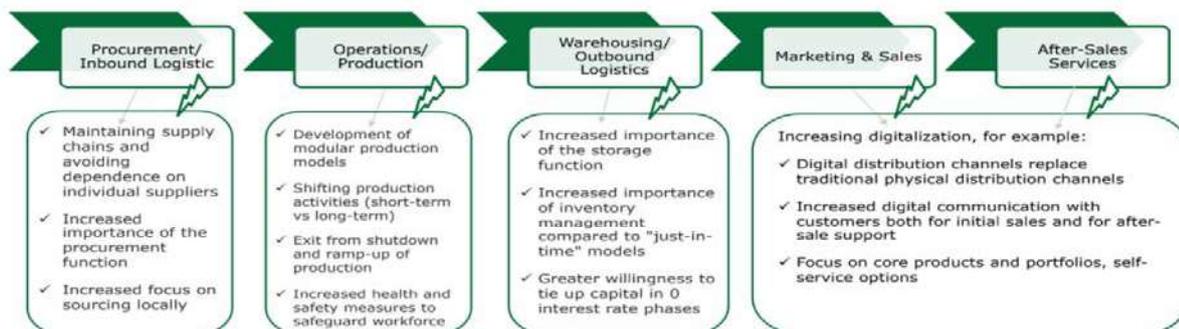
	constitute an extraordinary and temporary situation.
Income from employment	<ul style="list-style-type: none"> • In the case, where employees being resident in one jurisdiction and who formerly exercised employment in another jurisdiction, receives Covid related subsidies from the government; the same should be attributable to the work jurisdiction under Article 15 of OECD MC; • Where employees are stranded because of Covid related public health measures of one of the governments involved and remaining in a jurisdiction; it would be reasonable for a jurisdiction to disregard the additional days spent in that jurisdiction under such exceptional circumstances to calculate the 183-day test under Article 15(2)(a) of the OECD MC; and • Where employees are teleworking from abroad, (i.e., working remotely from one jurisdiction for an employer resident in the other jurisdiction); those situations may have an impact on where employment income is taxed, i.e., new taxing rights over the employee's income may arise in other jurisdictions, and those new taxing rights may change existing taxing rights. <p>Considering that payroll taxes are often withheld at source, countries may need to consider taking administrative relief measures to mitigate potential compliance and administrative costs for the employer and the employees.</p>

The guidelines issued by OECD are to be considered temporary, as it intends to address the exceptional circumstances arising from the Covid pandemic only. To note that a significant takeaway of most of the guidelines from the OECD, (especially in case of Transfer pricing (TP)), is the element of ‘but for Covid’, i.e., to regard covid as an exceptional event and therefore to regard business as usual, as if Covid had not occurred for the above purposes. Further, these are just guidelines and countries are not bound to adopt them.

Section III-A deeper deluge into the prominent international tax issues

a. Transfer Pricing issues

These unforeseen challenges have resulted in businesses re-negotiating/ seeking to negotiate their contracts/ re-structuring the operations to obtain better terms and conditions to survive the pandemic. There was a potential impact of this on long-term equilibrium and market dynamics on the industrywide value chain/ supply chain (diagram below illustrates this), especially because of the increased reliance on technology and remote working.



Source: WU transfer pricing workshop, TP Toolkit for dealing with Covid 19 impact (Deloitte 2020)

For businesses dealing with related parties in multiple countries, this raises unique issues because the international transfer pricing rules require associated entities to set prices at ‘arm’s length’.¹¹ The steps that some of the multinationals (MNEs) followed, can be bulleted as under:

- Identification of the challenges to the key principles underlying Arm’s length price (ALP) from Covid
- Identification of TP challenges for specific intra-group transactions with the value chain/ supply chain from Covid
- Identify potential steps plans to continue to ensure compliance with the ALP
- Use of economic/ non-economic measures to handle the TP audit challenges of the future

Some of the prominent issues are analyzed below:

i. Benchmarking analysis (comparability analysis, Function, Assets and Risk (FAR) analysis, Development enhancement maintenance procurement and exploitation (DEMPE), substance etc.)

Benchmarking strategies were revised considering the comparable sets similar to the tested party (based on functional/ economic/ factual characteristics and the impact of the pandemic on them). Business strategies were also considered when determining the comparability of controlled and uncontrolled transactions and enterprises¹².

The functional analysis of an MNEs and its different affiliates is key for a proper transfer pricing model within the group, as this requires identification of entrepreneurial group companies versus group companies with a more routine function. For intangible property and the critical drivers for an appropriate allocation of the group's IP profit, the functions regarding DEMPE of IP are important¹³. Where, there was a change in qualitative FAR, it was required to be analyzed, whether the change is material and considered a significant departure from the past and whether it will likely continue post-recovery. This also entailed analyzing the need for change in Functional profile (also DEMPE) because of the change in employee work/ changes in characterization (if required).

Further, a lot of challenges arose in terms of the search for the right comparable for the year 2020. Such solutions relied upon were:

- Revisiting search strategy criteria
- Adjustment of comparable companies’ data (for ex.: use previous year data as 2018/2019 and make adjustment for 2020, non-econometric adjustments to comparable data/ predictive modelling)/ adjustment using simplistic approaches (linear regression between GDP or other macro variable and comparable sales/ costs/ operating profits)
- Selection of loss-making companies or companies with a particular pattern of sales or capacity utilization decline
- Amendment of the period of analysis by focusing on the 2020 financial data of listed companies or on data concerning previous recession years (for ex. apply recession period (2008/2009) and apply results to 2020)¹⁴, considering term test i.e., looking at both, tested party and comparable

¹¹ In Australia, see Div. 815 of the Income Tax Assessment Act 1997 (Cth.) (ITAA 1997) (Cross-border transfer pricing), which states (in sec. 815-5) that its object: “... is to ensure the following amounts are appropriately brought to tax in Australia, consistent with the arm’s length principle: profits which would have accrued to an Australian entity if it had been dealing at arm’s length, but, by reason of non-arm’s length conditions operating between the entity and its foreign associated entities, have not so accrued ...”.

¹² At paragraph 1.114, the OECD Guidelines also stress the importance of business strategy when evaluating comparability, stating that: Business strategies must also be examined in delineating the transaction and in determining comparability for transfer pricing purposes.

¹³ <https://news.bloomberglaw.com/coronavirus/insight-49?context=article-relatedthe> last accessed on 17 May 2021

¹⁴ Matteo Cataldi and Antonietta Alfano, The Impact of COVID-19 on Transfer Pricing: Issues Arising during the Economic Downturn and Possible Solutions (2020) 27 International Transfer Pricing Journal, No. 4

companies over a three-year period, and undertaking post-facto adjustments once the results of comparable companies for 2020 were in the public domain

Such solutions were also subject to local rules and reliant on the OECD's Covid-19 guidance. In all, it is vital that transfer pricing benchmarking analysis are aligned to this new reality. At the moment, different data and data sources should be used to find sufficient/ reliable comparable data to determine reasonable ALP rates.

- ii. **Documentation aspects:** The deadline for TP filings and documentation were extended by many countries. However, it should be ensured that TP documentation appropriately captures the impact of Covid on selected industry and its sub-sectors, including impact on key business drivers, supply disruption, demand shrinkages, the time span of impact, etc. There should be an alignment of disclosure in the Master File on the impact of Covid on the MNE group with other public disclosures/ filings of the company.
- iii. **Intercompany loans and guarantees**¹⁵: The borrower's credit rating must be considered for Covid impact in all relevant areas (financial data/ country and sector information, etc.).

In the case of intragroup borrowings, the restructuring of any loan agreement could also be demonstrated to be at ALP by considering changes in domestic tax and regulatory framework apart from taking into consideration, the quantum of loan funding/ intercompany debt terms/ credit rating of the borrower. Further, interest rates on new inter-company debt loans in debt market instability due to Covid has significant implications when evaluating new intercompany loans. It is important to consider the moratorium, interest rate reduction and other benefits granted because of the Covid.

Appropriate documentation should be maintained to ensure that tax authorities do not impute notional guarantee commission to the said guarantee because of Covid.

* Force majeure is a common clause in any legal contract, which relieves the parties to the contract from liability or an obligation due to an event beyond their control. The question that arises then is, can an ongoing pandemic be considered an event leading to invoking the force majeure clause. Arguments exist on both sides; however, it would also vary depending on the specific terms of a contract. The fact patterns of comparable companies and the actions of the enterprise relative to its external stakeholders in its ecosystem (suppliers, customers, lenders), are also necessary to take into account while considering the invocation of the force majeure clause.

iv. **Balancing uncertainty with tax certainty**

Advance Pricing Agreements (APAs): In certain situations, it may not be beneficial for the taxpayers to be bound by the terms of the APAs terms which were entered before (especially where circumstances warrant and there is change in critical assumption). In that case, revision may be warranted if the taxpayer's business environment is considered abnormal based on the specific facts and circumstances of its case and the impact of the uncertainty on the transaction under consideration. (similar viewpoints were confirmed by OECD, discussed in Section II earlier). Where taxpayers are in the process of negotiating new APAs, they should discuss the economic impact of the current crisis and related uncertainty.

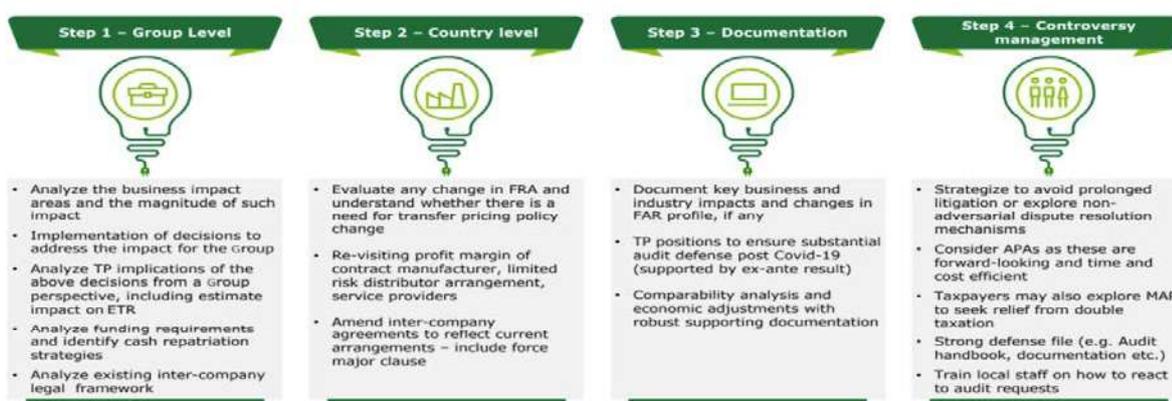
¹⁵ Vispi T. Patel et al, The Impact of COVID-19 on the Transfer Pricing of Intercompany Financial Transactions such as Loans, Borrowings and Guarantees – An Indian Perspective (2020) 27 International Transfer Pricing Journal, No. 6

Safe harbours

Taxpayers should evaluate whether or not to opt for safe harbours, at least for the year 2020 and 2021.

Overall, the impact of the pandemic, steps taken by the management to mitigate the adverse impact, negotiations/renegotiation (with third parties as well as affiliates), business plans and strategies, government policies and interventions are some of the key factors which will jointly determine the TP impact of the pandemic on the taxpayer.

Further, tax administrations should minimize disputes where taxpayers are making good faith efforts to determine ALP in the context of the information deficiencies associated with the Covid. In some case, where practical approaches regarding the performance of comparability analyses in not consistent, it may be possible that tax authorities may insist on ex-ante approach. The below diagram briefly represents the way forward for businesses:



Source: WU transfer pricing workshop, TP Toolkit for dealing with Covid 19 impact (Deloitte 2020)

b. Permanent establishment issues

Where the remote working location of the employee is in the same jurisdiction as his/her employer, such arrangement will not trigger any international tax implications¹⁶. However, where the employee's location of temporary presence or quarantine is in a different country, the employee's business activities may trigger PE implications on the company and potential tax implications¹⁷. (OECD guidelines in relation to PE issues were discussed earlier in Section II). Many countries signed the agreement for a temporary period to take due consideration for this in Covid situation.

An employee's home office may qualify as a PE in some jurisdictions if the use thereof is not intermittent or incidental and provided the foreign enterprise requests with the employee to use the home office. However, there are varied interpretations on what is an appropriate time in terms of permanence. OECD considers six months to be a requisite time period unless the nature of the business requires less time.

In terms of Agency PE, Construction PE issues reference can be placed on OECD guidelines (discussed earlier in Section II). However, for Construction PE determination, it is questionable whether the understanding of 'temporary interruption' (i.e., inclusion of temporary interruption period while calculating the threshold for Construction PE) can apply to the current pandemic situation, as this was unpredictable and would be more of a force majeure situation.

¹⁶ Transfer Pricing Considerations for Remote Workforces, Bloomberglaw (2020) <https://news.bloomberglaw.com/coronavirus/insight-49?context=article-related> last accessed on 17 May 2021

¹⁷ ibid

Further, MNEs should continue to maintain a record of the facts and circumstances supporting each cross-border working arrangements resulting from public health measures to prevent the spread of the Covid, including travel disruptions, quarantines, and border closures, initiated by at least one of the governments of the jurisdictions involved, review and document ‘ordinary place of management’ and where contracts were concluded ‘habitually’ under ordinary circumstances, assess the degree of permanency for the home office arrangements of your employees, review your cross-border working arrangements for employees.

b. Residential status and taxation of the individual

Several challenges arose in determining individual residency. For ex., a person is temporarily away from his home and gets stranded in the host country because of the Covid crisis and attains domestic law residence there (discussed in Section V, considering the clarification issued by Indian government in this regard). Many said that tax treaty would come to rescue in most of such situations, but it is doubtful as some countries have narrow tax treaty network and not all countries provide for unilateral tax credit/ relief.

Not much has been discussed about the social security contribution¹⁸ issues. Tax law and social contribution law are usually separated; however, both involve a lot of interaction in practice. The difference is just that social security contributions is used to dedicatedly finance social security payouts and is not allocated to the general budget. Taxes on cross-border employment income are often allocated to both the resident State and the source state (article 15(1) of the OECD Model (2017)). A 183-day-rule exception is often present in treaties (article 15(2)), with the effect that tax is only payable in the resident state. However, social contributions are usually levied only by one state. Thus, social contribution may be another challenge when the residential status of the individual will change because of Covid.

c. Residency issues of companies

Even when the domestic law of certain countries may consider a company to be a resident as a result of the working arrangements of certain employees, the treaty tie-breaker rule would ensure that the residence status of an entity is tied to its ‘usual’ or ‘ordinary’ place of effective management¹⁹. Most double tax treaties provide for a tie-breaker clause in their Art. 4 (3), which provides that a company being a resident of both contracting states (under domestic law) is deemed a resident only of the state its place of effective management is situated²⁰. The OECD Commentary 2010²¹ defines the place of effective management as ‘the place where key management and commercial decisions that are necessary for the conduct of the entity’s business as a whole are in substance made’. Pertinent to mention, that the wording of OECD MC 2017 is different as it states that competent authorities of the Contracting States shall endeavour to determine by mutual agreement the Contracting State of which such person shall be deemed to be a resident for the purposes of the Convention, having regard to its place of effective management, the place where it is incorporated or otherwise constituted and any other relevant factors²².

¹⁸ Katia Cejje, European Union/OECD/Sweden/Denmark - New Problems Caused by the COVID-19 Pandemic – Income Taxes and Social Security Contributions (An Overview) (2021) 61 European Taxation, 2021 No. 5

¹⁹ <https://www.dlapiper.com/en/us/insights/publications/2021/01/oecd-published-guidance-on-the-tax-impact-of-cross-border-working-arrangements/> last accessed on 17 May 2021

²⁰ The following criteria will among others be taken into consideration in order to determine where the POEM is situated: the place where the board of directors or equivalent body holds its meetings; the place where the senior day-to-day management is carried on; the place where the senior executives carry on their activities’

²¹ OECD MC Commentary (2010), Commentary on Article 4

²² OECD MC Commentary (2017), Article 4

The POEM concept still appears to be significant because many countries have not yet decided to amend Article 4 of tax treaties in line with the OECD MC text updated in 2017. Further, even OECD MC 2017 have not completely overlooked the POEM concept for determination of residential status of companies.

Several questions arose during the Covid times in terms of residency of the company, in terms of whether extraordinary and temporary change in location of the chief executive officers and other senior executives due to the Covid should not trigger a change in company residency. In case of Covid it was clarified by OECD that such temporary change may not impact the residence of companies. (discussed earlier in Section II)

Future challenges:

Organisations' are moving away from hierarchical, linear management models and are implementing an approach based on decentralization and dispersion decision-making processes²³. In addition, decision-making processes undergo 'deterritorialization', i.e., even collective decisions no longer require the physical presence of all decision-makers in one place/ room, accordingly this increases the possibility of more people participating in decision-making (people are more moving toward the concept of smart working). In relation to new business models based (using) to a large extent on broadly understood digital technologies, decentralization can adopt various forms. Let's take example of Autonomous Organization (DAO), 'DAO is a computer program that operates on a peer-to-peer network incorporating governance and decision-making rules. DAOs can be programmed to operate autonomously without human involvement, or the code can provide for direct, real-time control of the DAO and the funds controlled by it. DAOs were made possible by the development of a public blockchain which provides a decentralized virtual machine to execute peer-to-peer contracts using its native cryptocurrency. This holacracy concept is also an example of decentralized management and organizational governance that challenges rigid management structures'.²⁴

Another phenomenon that is possible by the development of computer networks is the creation of virtual organizations. Virtual organization partners can be selected dynamically regardless of their location, and each brings their key competencies to the organization.²⁵ Immaterial of the management model (i.e. hierarchical or de-hierarchical), its performance will be affected by artificial intelligence (AI) development based on machine learning. Lipniewicz mentioned 'The role of algorithms in company management processes can also be seen from the perspective of the managed units. What is of interest here is the question of the applicability of algorithms for making strategic managerial decisions. Under such a system, algorithms will have ability to make a strategic managerial decision'²⁶.

The question does arise: With increasing reliance on technology and move more towards technological advancement in the post Covid scenario too, how companies' residential status will be determined as in these situations (as discussed above) it will be very difficult to determine the factors (like POEM etc.) that can aid in determination of the residential status of the company.

Another concept that is picking up in this age of hybrid business is the concept of digital nomad, which shall bring separate challenges in terms of Article 15 of the tax treaty and other residency related issues (however, this is not discussed in this paper).

²³ Rafal Lipniewicz, 'Place of Effective Management in the Digital Economy', (2020), 48, Intertax, Issue 6, pp. 602-615, <https://kluwerlawonline.com/JournalArticle/Intertax/48.6/TAXI2020055>

²⁴ D. Harrison, Decentralized Autonomous Organizations, Allen & Overy LLP (11 July 2016) <https://www.allenoverly.com/en-gb/global/news-and-insights/publications/decentralized-autonomous-organizations> last accessed on 17 May 2021

²⁵ U. Słupska, Proces kreowania organizacji wirtualnej we współczesnym świecie biznesu 141–151 (2016), <http://cejsh.icm.edu.pl/cejsh/element/bwmeta1.element.desklight-6b699b32-52c7-478c-bed4-6c2a3ccf3450/c/slupska.pdf> last accessed on 17 May 2021

²⁶ Lipniewicz (n23)

However, it appears that the topic of residence of individuals/ companies, taxation of employment income, PE issues because of cross border movement of employees need to be visited together to consider the aftermath effects of Covid in terms of changing working models and increasing digitalisation.

Section IV: Covid and tax technology

Although the government had historically used technology to improve compliance and increase tax revenues, Covidacted as a catalyst to fast-track many of these efforts. Many governments have promoted the digitalization of tax procedures, encouraging people to use electronic means of communication with the tax administration or receive official notifications. On-site assistance was cancelled or reduced significantly during the emergency period²⁷. Some of these measures taken by some countries include:

E-invoicing: An e-invoice refers to an invoice that is electronically generated and authenticated by the government before it becomes a valid document that the customer can use to claim a tax set-off. Thus, this becomes a tool that customers can use to record, and tax administrators can review.

Paperless customs: The electronic transmission of the customs documents replaced earlier requirement of carrying paper copies of these documents. **Faceless assessments and appeals:** The dispute resolution process is also going digital and there has been introduction of e-assessments and e-appeals in many situations. These shall aid in more efficient use of available resources and reduction in the arbitrary exercise of discretion at times in concluding assessments and appeals.

On the other hand, even MNEs are looking for more digital means of doing business. Many companies were trying to automate the tax functions to the extent possible in pre-covid situation too (some companies were already building/ implementing solutions for transfer pricing compliance, VAT etc., for example SieDoc 2.0, Siemen’s documentation tool that enables it to automate of TP documentation process); however, the urge to move towards tax automation shall increase in the post-covid situation.

Section V: Impact of Covid 19 on the Indian economy and international tax arena

Many developing countries have already adopted tax policies mainly targeted towards lessening the economic fallout and productivity losses caused to manage the impact of the crises.²⁸

As per IMF for India, ‘The economic impact of COVID-19 has been substantial and broad-based. GDP contracted sharply in 2020 Q2 (-24.4 per cent year-on-year) due to the unprecedented lockdowns to control the spread of COVID-19. The contraction moderated to -7.5 per cent year-on-year in 2020 Q3, and growth returned to positive territory in 2020Q4, at 0.4 per cent. The national statistical office released the second advance estimate for FY2020/21 GDP growth to be -8%, in line with the January WEO projection’²⁹.

To boost businesses and sustain the economy, the Indian government, alongside the Reserve bank of India (RBI), introduced a lot of fiscal and monetary measures. Also, various short-term sources of credit have been made available to small and medium-sized enterprises by the government. Further, RBI also directed banks to give a moratorium on all outstanding loans to provide some relief to businesses. There were significant rate cuts made to interest rates to encourage businesses to make more investments³⁰.

²⁷ See, for example, the cases of Uruguay (A. Laura Riccardi Sacchi, National tax measures adopted in response to COVID- 19 crisis: Uruguay (2021) OJC. Special issue 2020 – Covid 19, § II.3) and Portugal (J.F. Pinto Nogueira, Tax reactions to the SARS-CoV-2/COVID-19 pandemic in Portugal (2021) OJC. Special issue 2020 – Covid 19, § IV.7)

²⁸ Heffron et al (n2)

²⁹ <https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19#I> last accessed on 17 May 2021

³⁰ ibid

If we were to talk about taxation, from time to time, circulars were issued by the Indian government to handle the crises impact by reduction of rates, deferrals, other amnesty schemes etc. In terms of international tax, the determination of the residential status of the individual came into controversy.

The Central board of direct taxes (CBDT) came out with clarification on 8th May 2020 vide Circular No. 11/2020³¹ and provided relief to such persons becoming accidental and unintentional residents. The accompanying press release dated 9th May 2020 provided further assurance from the Government that relief for financial year (FY) 2020-21 would be given in due course of time. The circular applies to individuals who came on a visit to India on or before 22nd March 2020 and have continued to be in India in different scenarios. This circular applies only for the determination of residency for FY 2019-2020.

In many situations, by the time flights were restarted, criteria of 182 days were already met, thereby resulting in a situation in which a non-resident who were stranded in India because of the lockdown became a tax resident for FY 2020-21. Accordingly, people made various representations to the Government for clarity. After multiple representations to the Government, a Special leave petition (SLP) was filed before the Supreme Court. While hearing the SLP filed by a Non-resident Indian (NRI) who gained involuntary residency in India, the Court ruled that the CBDT is the appropriate body to grant relief and directed it to issue circular within three weeks.

Circular No. 2/2021 was issued on 3rd March 2021³², which doesn't grant any relief or concession, as was expected, and is mere summarization of existing provisions, discussed briefly below³³:

No short stay in India	The circular specified that short term stay anyways does not result in residency in India. This shows that it has not considered the situation where the flights are not opened, and individuals are stranded in India and could not leave the country and return to their country of usual residence. In such situation, they might have already exceeded/ or exceed the threshold period for being non-resident in India and hence became/ may become residents.
Possibility of dual non-residency	The circular states that granting relief for the forced period of stay in India may result in a situation where a person may not become a tax resident in any country in F.Y. 2020-21 even after staying for more than 182 days or more in India, resulting in double non-taxation and end up not paying tax in any country. For ex.: Mr. A came for a temporary stay in India; however, due to the Covid, he had to stay for more than 182 days. Considering the Covid, if India would have decided not to consider the time period when the pandemic hit the country or when flights were non-functional, Mr. A was deemed to be a non-resident of India. Further, the Mr. A may also be considered a non-resident in his original country if the minimum period of stay in the relevant year, required in the other country for becoming resident is not satisfied ³⁴ . Pertinent to mention that it may happen that if such person becomes resident in India, whatever payments such persons would make that may also fall in taxation purview and may be deemed to accrue and arise in India and be chargeable to tax in India.
Tie-breaker rule	The circular explains that the tie-breaker test under tax treaties will come to

³¹ https://www.incometaxindia.gov.in/communications/circular/circular_no_11_2020.pdf last accessed on 17 May 2021

³² <https://www.incometaxindia.gov.in/news/residency-circular-02-of-2021.pdf> last accessed on 17 May 2021

³³ T.P Ostwal | Kush Vatsaraj, COVID IMPACT AND TAX RESIDENTIAL STATUS: THE CONUNDRUM CONTINUES, BCAS Journal (April 2021)

³⁴ <https://taxguru.in/income-tax/cbd-t-clarifies-residential-status-issues-new-nr-form.html> last accessed on 17 May 2021

<p>under the tax treaties</p>	<p>the rescue of dual-residents. These seems contradictory as circular also stated that if someone becomes a resident of India by virtue of their period of stay in India, they will not be able to access the tie-breaker test of the tax treaty because they may not qualify as residents of the country of their usual or normal tax residency.</p> <p>Also, India does not have a tax treaty with all countries. Hence, in situations where person is a resident of a country with which India does not have a tax treaty this possibility will not be available.</p>
<p>Employment income</p>	<p>The circular reiterates the current position that the employment-related income will only be subject to tax in India if his stay exceeds 183 days in India or if a PE of the foreign employer bears the salary.</p> <p>For ex: Mr A is an employee of a US company but has come temporarily to India. However, Mr A got stranded in India. In such scenario, the income arising from employment will not be taxable in India unless Mr A has stayed in India for more than 182 days or if the salary is borne by the Permanent establishment of the US company in India³⁵.</p>
<p>Availability of the credit</p>	<p>The circular states that in case of double taxation, credit of foreign taxes would be available in India as per Rule 128. However, where if the foreign tax liability and the effective tax rate is lower than the Indian tax rate, there may arise concerns in terms of final tax payouts. Apart from this, the elimination of double taxation through tax credit is not relevant for Indian emigrants living and working abroad in lower tax or zero-tax rate countries such as the Gulf countries like Qatar, United Arab Emirates etc. In such a scenario, individuals would have to pay tax in India, which they would not have to in normal situation.</p>

CBDT has very clearly highlighted that double taxation is significantly less likely to arrive even if no general relaxation in determining the residency status is provided for the FY 2020-21. Further, for the double-taxation situation, a new Form-NR has been specified where the person can declare that he/she is double taxed during the pandemic and declare the reasons and details for the same. This form is to be submitted electronically to the Principal Chief Commissioner of Income-tax (International Taxation)³⁶.

However, CBDT didn't clarified the impact on the place of effective management and PE. Thus, the clarification about residency conspicuously leaves out the related PE aspect (in this case, residency and PE are two sides of the same coin, so to speak), and this lacuna leading to possible assertion of PE by the Revenue authorities runs counter to the Covid related guidance of the OECD that advocates the exclusion of the period during which the individual was forced to stay outside his or her normal place of work, thereby creating an unintentional PE during that interval.

The clarification made by the CBDT in the circular was already known before and hence it did not bring any new guidance/ relief. The second petition filed against the circular before the Supreme Court (by the same NRI who had filed the original SLP) does argues that the Government is obligated to provide relief based on its earlier promise³⁷.

³⁵ ibid

³⁶ <https://blogs.compliancecalendar.in/clarification-in-respect-of-residency-under-income-tax-act-1961-8835> last accessed on 17 May 2021

³⁷ Reliance was placed on the judgement of Ram Pravesh Singh vs. State of Bihar (some of the grounds taken were 'legitimate expectation', circular being unconstitutional because it violates the principle of equality before law under Article 14 of constitution, violation of Article 19 because it interferes with the freedom to practice a trade or profession and places undue restrictions on the same. Lastly, it argues that the Constitution guarantees protection to life and personal liberty and the lockdown was a force majeure situation, where the appellant was forced to remain in India in order to protect his life and liberty)

Section VI: Conclusion and what lies ahead

The Covidpandemic came as a severe and sudden blow to the global economy, with many companies unprepared from a business continuity planning perspective. Accordingly, while we speak about agility and dynamism, the same may need to be stoutly embedded in business models for the future.

On 10 June 2020, José Ángel Gurría, the OECD Secretary-General, said that ‘how governments act today will shape the post-COVID world many years to come’³⁸. While thinking for the future and aftermath of crisis, especially for developing countries, it seems that countries will need to create favourable situation for sustainable and resilient economic growth, and consequently for this they would also need a clear and strategic tax policies. Further, no doubt that multilateral collaboration and coordination is necessary to increase the effectiveness of countries’ responses at various stages of the path to recovery and strengthen the global economy’s resilience to future shocks³⁹.

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“The world progresses, year by year, century by century, as the members of the younger generations find out what was wrong among the things that their elders said.”

Linus Pauling

³⁸ J.A. Gurría (@A_Gurria), Twitter (10 June 2020, 19:44 GMT), available at https://twitter.com/A_Gurria/status/1270781348098322433

³⁹ Kurt Van Dender, Pierce O’Reilly, Sarah Perret, ‘COVID-19 and Fiscal Policies: Tax and Fiscal Policy in Response to the Coronavirus Crisis: Strengthening Confidence and Resilience’, (2020), 48, Intertax, Issue 8, pp. 736-742, <https://kluwerlawonline.com/journalarticle/Intertax/48.8/TAXI2020069>