INSIDE VIEW

Cross-border Teleworking and Permanent Establishment Risks

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If there is something we learned from the COVID pandemic, it is that many jobs that were previously considered as requiring a fixed location can be (and are) performed remotely in the long term. Employees and employers are adjusting to this new reality and tax might be a critical factor in long-term solutions.

Background

With today's modern technological solutions (internet, smart devices, conferencing platforms, cloud-based collaboration, file sharing, and so on), the possibility of employees not only working in their employer's office has been becoming more common, even before the global pandemic. As a result of recurring waves of COVID-19 and the lockdowns and travel restrictions, teleworking has, in many sectors, become standard practice. The corresponding rules (tax, social security, labor law) for these arrangements were not designed with such extraordinary circumstances in mind.

The OECD realized early that companies rightly might be concerned that employees dislocated to jurisdictions other than the one in which they regularly work could create a "permanent establishment" (PE) in those jurisdictions, triggering new filing requirements and tax obligations for those businesses in various additional countries.

The OECD issued guidance back in April 2020, updated in January 2021, stating that a place must have a certain degree of permanency and be at the disposal of an enterprise for it to be considered a fixed place of business through which the business of that enterprise is wholly or partly carried on. It also implies that a temporary change due to extraordinary circumstances (such as the pandemic) should 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.

New Normal?

But what happens if an individual (for example, an expat realizing the benefits of remote working from their home country near to their family) continues to work from home after the cessation of the public health measures imposed or recommended by the government?

By its own definition, the OECD guidance is relevant only to circumstances arising during the COVID-19 pandemic when public health measures are in effect and maintains that each jurisdiction may adopt its own guidance to provide tax certainty to its taxpayers.

The Hungarian tax authority has now confirmed that even in the case of long-term or permanent cross-border home office scenarios, if and when the pandemic is already over, working from home does not necessarily trigger a permanent establishment for the employer. An important distinction is whether the company requires home working or whether it only offers the possibility to work from home while maintaining office space for its employees in another country. "Voluntary" home office by the employee should not be considered a PE for the employer and, therefore, should not trigger additional tax and compliance burdens.

The Hungarian tax authority also stressed, in accordance with the OECD guidance, that the issue of whether a PE exists is a test based on all the relevant facts and circumstances on a case-by-case basis.

Hungary has an extensive network of double taxation treaties with more than 80 countries based on the OECD Model Convention. The Hungarian tax office also established that, despite the changes to the Model Convention in 2017, there are no significant differences between the rules applicable to treaty and non-treaty states from a Hungarian PE point of view. As of January 2021, two new elements have been added to the concept of establishment in the Hungarian Corporate Income Tax of International Trade provisions, with the purpose to approximate the concepts of establishment in the Model Convention (the existing conventions) and the Hungarian CIT rules (for non-treaty states).

Summary

The Hungarian tax authority confirmed a rather promising approach in its latest non-binding ruling regarding the interpretation of PE implications, or the lack thereof, of cross-border home office setups. This might allow employees and employers to find mutually beneficial long-term home office arrangements, based on the employee's request, without the additional headache of PE risks in Hungary.

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