

# COVID-19 FORCED TAX RESIDENCY

## Part I – Foreign Companies

May 8, 2020

The mandatory confinement and international travel restrictions imposed by the Colombian Government to prevent the spread of Covid-19 in our Country may carry unintended tax consequences in Colombia for both foreign companies and non-tax-resident national and alien individuals.



Because of the above mentioned measures, non-tax-resident aliens and nationals may be currently stranded in Colombia with no short-term expectation to return to their usual countries of residence, overstaying in Colombia longer than what they originally expected and having to continue to work from Colombia, a situation that may trigger risks arising from statutory domestic rules and from Double Tax Treaty (“DTT”) provisions on fiscal residency, permanent establishments and place of effective management. This could potentially impact the right to tax between Colombia and other countries, and result on filing requirements and tax obligations in the Country.

In the field of DTTs, the OECD has issued guidance to deal with these issues amongst treaty countries, and has encouraged tax administrations to domestically issue guidance to deal with these issues. Despite the above and the fact that Colombia was recently formally admitted as the 37th member of the OECD, to this date the Colombian Tax Administration (DIAN) has not issued any guidance on these matters.

This bulletin is **Part I** of a two-part delivery, focusing on the potential issues for foreign companies. In the upcoming **Part II**, we will deal with the potential issues for non-tax-resident individuals.

The “*OECD Secretariat Analysis of Tax Treaties and the Impact of the COVID-19 Crisis*” can be consulted on this [link](#).

## 1. Permanent Establishments

In its domestic tax framework Colombia has a definition of fixed place of business and dependent agent permanent establishment (“PE”), it does neither have a services PE nor a construction site PE definition. A Colombian PE of a foreign company is subject to corporate income taxation in Colombia on all domestic and foreign source income attributable to the PE. During the current situation the question is whether under Colombian tax rules and applicable DTT provisions, either (i) a worker of a foreign company stranded in Colombia because of the Covid-19 measures, preventing her to travel back to her country of residence, or the place from where said employee is working from; or (ii) an inactive construction site in Colombia, can constitute a PE in Colombia for the foreign company.

In our view, the place in Colombia from which a currently stranded employee is partly carrying business on behalf of the foreign company, should not be construed as a fixed place of business. A **fixed place of business** requires *permanency* and needs to be at the *disposal* of the foreign company; in our view it should be clear that under the current situation neither the *permanency* or *disposition* thresholds are present. Unfortunately, because of the lack of guidance by the Colombian Tax Service (“DIAN”) on this issue and the scarce doctrine

of the DIAN on PEs, there is room for the Administration to adopt a different position.

In the case of a temporarily stranded person that is a **dependent agent** of a foreign company, the domestic rule clearly requires that the exercise from Colombia by that person of the authority to conclude binding contracts for the foreign company is *habitual*, and in our view under the current circumstances one can only conclude that such exercise is *temporary* and not *habitual*, and therefore a PE should not be construed in the context of the current circumstances. Moreover,

it is clear that in the case at hand that person is only discharging her duties or exercising her authority from Colombia due to *force majeure* reasons; nonetheless, the application of *force majeure* in this case would be unprecedented.

In the context of tax treaty countries, the above-cited OECD guidance is clear and the answer should be the same in both cases. Nonetheless, it is advisable to be alert to the specific facts and circumstances of each case to try to mitigate any risks.

On the other hand, the PE definition in all DTTs concluded by Colombia comprises a **construction site PE**. However, unlike the OECD Model, which suggests that a construction site PE shall only be triggered when the related project/activities last more than 12 months, all of Colombia's currently in force DTTs provide a **6-month threshold** (that is the case of the DTTs with Spain, Switzerland, Chile, Canada, Mexico, Portugal, South Korea, India, Czech Republic and the UK); some of the DTTs not yet in force include a 183-day threshold (France, Italy and Japan) and the DTT with the United Arab Emirates sets an even shorter 90-day threshold.

According to OECD Guidelines on the application and interpretation of tax treaties

in the context of Covid-19, current inactivity in construction sites, as any other temporary interruption, shall not preclude the creation of a PE. Hence, the term of the interruption shall be regarded as part of the life of the site when determining if it constitutes a PE.

Although the Colombian Government recently authorized construction companies to resume their activities as of April 27, foreign companies carrying out construction or installation activities or projects in a construction site in Colombia, who were not expecting to trigger a Construction PE in the country based on a projected duration of their activities of less than 6 months, shall reassess their situation, bearing in mind that the 5 weeks of inactivity will most likely be regarded as part of the life of the site.



## 2. Place of Effective Management

Foreign companies that according to the Colombian tax framework are effectively managed from Colombia are deemed as Colombian companies for tax purposes, thus subject to corporate income taxation in Colombia on their worldwide revenue.

During the current situation the question is whether under Colombian tax rules the execution of her duties by a chief executive officer or other senior executives of a foreign company, stranded in Colombia because of the Covid-19 measures preventing them to travel back to their country of residence, can trigger the statutory threshold for said foreign company to be deemed as having its place of effective management (“POEM”) in Colombia.

The Colombian threshold for deemed POEM is rather subjective and, in addition to the place where the duties are *usually* and *ordinarily* being discharged by a chief executive officer or other senior executives, it requires an examination of the specific facts circumstances of each situation at hand. Under the current events, the temporary forced location of chief executive officers and other senior executives discharging their duties from Colombia, is clearly *extraordinary* and *temporary* as opposed to *usual* and *ordinary* and, together with the unprecedented circumstances of the current situation, should lead to a clear-cut conclusion that the relevant foreign company should not be deemed to have its POEM in Colombia. Moreover, under the current circumstances it is also clear that a chief executive officer or other senior executives of a foreign company would only be discharging their duties from Colombia due to *force majeure* reasons; nonetheless,

the application of *force majeure* in this case would also be unprecedented.

Nonetheless, to this date DIAN has not issued any guidance addressing this topic and the impact of Covid-19, and for this reason it is advisable to be alert to the specific facts and circumstances of each case to try to mitigate any risks.

In the context of tax treaty countries, the above-cited OECD guidance is clear and the answer should be the same, but the OECD also advises a careful examination of the facts and circumstances of each case to assess the presence of the *usual* and *ordinary* elements of POEM under each treaty framework.

For questions about these topics, please contact your trusted partner at Lewin & Wills, or:

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