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Permanent Establishment in the Time of Covid-19: a Concept to Revise?

Supervisor
Chiar.mo Prof. Claudio Di Gregorio

Graduand
Silvia Casonato
841573

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In the life of Nations
the error of not knowing
how to grasp the fleeting moment
is usually irreparable.

Luigi Einaudi

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To my parents. Without your endless efforts, this would never exist.

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Permanent Establishment in the Time of Covid-19: a Concept to Revise?

Abstract

The advent of the pandemic from Sars CoV-2 (COVID-19) in the global scenario has produced profound and diversified effects not only from the health point of view.

Restrictions on the free movement of persons, trade and business management, the adoption of urgent fiscal policy measures by States, represent a clear example of the impact of COVID-19 at global level.

In this regard, on 21 January 2021, the OECD issued specific "Guidance" aimed at overcoming the concerns of certain Tax Administrations, warning that the recommendations adopted therein should be interpreted as provisional.

This work aims, in particular, at deepening the effect of the pandemic on the legal concept of "Permanent Establishment", as it was conceived and accepted in the international tax treaties until the publication of the OECD Guidance and at verifying whether, in the light of the experience already gained, such a concept deserves a revision.

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INRODUCTION

The concept of “Permanent Establishment”, as a fixed place of business or agency that gives rise to a tax liability in a certain jurisdiction, is rather ancient in international taxation and its field of application has attracted over time authoritative scholars and tax administrations in different countries.

Even without going back too far, as some suggest (Kobesky, 2011) [1], to the Treaty of the 19th century (1889) between the Austro - Hungarian Empire and the Kingdom of Prussia, the basis of the concept is quite fully elaborated in the framework of the League of Nations at least one hundred years ago (Geneva, 1923)[2], deepening the theme of the right to tax on profits earned by a business enterprise or a commercial establishment[3].

That is because the taxation of business profits derived from cross-border activities, and in particular through a Permanent Establishment, is one of the core issues in international tax law.

It depends on the application of two (alternative) fundamental principles of international taxation: “source principle” and “residence principle”. The final choice implies the correct detection of the source of wealth, the country entitled to tax, the tax base (whole or part), the emerging moment of taxation and why. It is not so easy as it could seem, especially because once decided if a Permanent Establishment actually exists, it should be decided how much wealth (e. g. income) to attribute to it (Avi-Yonah, 2019)[4].

The issues faced by experts and the solutions they proposed, resulting from the overlap of “source jurisdiction” and “residence jurisdiction” led the League of Nations to develop, in 1927, its first tax treaty model to prevent double taxation, and this was the foundation

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[1] KOBETSKY M., *International Taxation of Permanent Establishments: Principles and Policy*, Cambridge, 2011, p. 109 observes that the Treaty should be marked as the first “international agreement” aimed at avoiding double taxation, whilst other agreements (i.e. the one between Prussia and Saxony in 1869) were rather “domestic”. See, on the contrary, SAVITSKIY A., *The First Tax Treaties: In Search of Origins*, in *Intertax*, Volume 49, Issue 6/7 (2021) pp. 569 – 585.

[2] LEAGUE OF NATIONS, Financial Committee, *Experts' Report on Double Taxation: Document E.F.S.73.F.19*; Geneva, April 5, 1923, *Excerpt from the University of Sidney Library, https://adc.library.usyd.edu.au/view?docId=split/law/xml-main-texts/brulegi-source-bibl-1.xml;chunk.id=item-1;toc.depth=1;toc.id=item-1;database=;collection=;brand=default.*

[3] See *Experts' Report* already quoted, para. II., pp. 11 - 12

[4] AVI-YONAH R.S., *Advanced Introduction to International Tax Law*, Northampton, MA, U.S.A., 2019, pp. 25 – 26.

of the OECD Model Tax Convention 2010, of the UN Model Convention 2012 and of the modern tax treaties[5].

The internationally agreed and so laboriously achieved notion of Permanent Establishment was largely revised, further to the BEPS Action Plan, launched by the OECD in 2013, aimed at countering the perverse effects of the globalization, in terms of "double non-taxation" risk.

In fact, multi-national enterprises (here in after MNEs) now represent a large proportion of the global GDP. Also, intra-firm trade represents a growing proportion of overall trade. Globalization has led to a shift from country-specific operating models to global models based on the management of integrated supply chains that centralize different functions at regional or global level.

In addition, the growing importance of the service component of the economy and digital products that can often be provided via the Internet made it much easier for companies to localize many manufacturing activities in geographic areas distant from the physical location of their customers (OECD, 2013)[6].

These developments have opened up opportunities for MNEs to greatly minimize their tax burden.

With special reference to the concept of Permanent Establishment, the BEPS Action 7 proposes several changes to its definition in the OECD Model Tax Convention to counter BEPS (OECD/G20, 2018), as follows:

• changes to ensure that where the activities - that an intermediary exercises in a jurisdiction - are intended to result in the regular conclusion of contracts to be performed by a foreign enterprise, that enterprise will be considered to have a taxable presence in that jurisdiction, unless the intermediary is performing these activities in the course of an independent business;

• changes to restrict the application of a number of exceptions to the definition of Permanent Establishment to activities that are preparatory or auxiliary nature and will ensure that it is not possible to take advantage of these exceptions by the fragmentation of a cohesive operating business into several small operations;

[5] See OECD Model Tax Convention, art. 5 – Permanent Establishment and UN Model Convention, art. 5 – Permanent Establishment.

[6] So, textually, in OECD, *Action Plan on Base Erosion and Profit Shifting*, Paris – Cedex, 2013, pp. 7 – 8.

• changes to address situations where the exception applicable to construction sites is circumvented through the splitting-up contracts between closely related enterprises[7].

The changes to the definition of permanent Establishment were integrated in the 2017 OECD Model Tax Convention and in Part IV of the Multilateral Instruments (MLI Articles 12 through 15).

The advent of the pandemic from Sars CoV-2 has produced profound and diversified effects in this legal scenario. Restrictions on the free movement of persons, trade and business management, the adoption of urgent fiscal policy measures by States, represent a clear example of the impact of COVID-19 at global level.

In this regard, the OECD (2021) issued specific "Guidance" aimed at overcoming the concerns of certain tax administrations, warning that the recommendations adopted therein should be interpreted as provisional[8].

United Nations, on their side, published a Report (UN, 2021) concerning gaps in the definition of Permanent Establishment (Art. 5 of the UN Model Convention) related to provision relying on time threshold as well as to the situation of working from home or remote working (the so-called "*smart working*").

On the other hand, a number of tax authorities have issued guidance on whether changes in work practices prompted by the COVID-19 pandemic can result in the creation of a Permanent Establishment. Countries (Australia, Austria, Canada, Germany, Greece, Ireland, New Zealand, U.K. and U.S.A.) have welcomed a certain flexibility provided by the guidance in these unprecedented times and issued their own directions[9].

In this context, the question arises whether the concept of Permanent Establishment, as it developed up to the advent of the pandemic, is nowadays susceptible to a broaden review, taking into account exceptional events such as a pandemic or a war (IMF, 2022)[10].

The present work has been aimed at responding to this question.

Stemming from the historical and conceptual background of the definition of Permanent Establishment, already formalized in the Model Tax Conventions adopted so far by a number of States, it examined the initiatives carried out by the OECD, G20 and UN, further to the BEPS Action Plan, and verified the evolution of the definition of Permanent

[7] See the text of the OECD/G20 Base Erosion and Profit Shifting Project, *Additional Guidance on the Attribution of Profits to Permanent Establishments, BEPS Action 7*, Paris – Cedex, 2018, pp. 9 – 17.
[8] OECD, *Tackling Coronavirus (COVID-19): Contributing to a Global Effort, Updated guidance on tax treaties and the impact of the COVID-19 Pandemic*, Paris-Cedex, 2021.
[9] See OECD, *Tackling…*, pp. 4 – 5.
[10] See, in this regard, the issues proposed by IMF, *Fiscal Monitor* (*Fiscal Policy from Pandemic to War*), Washington D.C., U.S.A., 2022, pp. 1 – 23.

Establishment in the Italian Income Tax Code context, as well as in the case law developments.

In this regard, the concept of “Hidden Permanent Establishment”, of case-law elaboration, has been deepened as well.

CHAPTER 1

THE TRADITIONAL CONCEPT OF PERMANENT ESTABLISHMENT AND ITS EVOLUTION

1.1. Historical and Conceptual background.

As already seen, the concept of "Permanent Establishment" (hereinafter PE) is one of the most relevant in the international taxation and in the Model Tax Conventions (OECD MTC - UN MDTC, 2017)[11].

Basically, its relevance resides in the need to determine the allocation of profits for tax purposes between different jurisdictions, when an entity carries on a business in more than one State (its residence country).

This usually happens when an enterprise avails itself of at least a headquarters and of one branch.

Very often the term "Permanent Establishment" is referred to a foreign branch, even though it was correctly argued (Oats, 2021) that the aforementioned expression has a much wider meaning[12].

Actually, international tax treaties acknowledge a PE on the basis of certain requirements which make it possible to attribute to one jurisdiction rather than another the right to tax the profits it earned, no matter where the enterprise's headquarters is located.

So, once a PE has been set up, it can be subject to direct and/or indirect taxation (Tanzi, 2011; Avi-Yonah, 2019)[13] in the State where the income (profit) is produced ("source – principle") rather than in the State where the enterprise headquarter is established and where the requests to implement all the connected instrumental and accounting obligations can be ordinarily made ("residence principle").

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[11] See the Articles 5 and 7 of the OECD Model Convention with respect to taxes on income and on capital, as they read on 21 November 2017, and the Article 5 of the UN Model Double Taxation Convention between Developed and Developing Countries, 2017.
[12] OATS L., *Principles of International Taxation*, London, 2021, p. 189.
[13] TANZI V, *Tax Systems in the OECD: Recent Evolution, Competition, and Convergence*, excerpt from The Elgar Guide to Tax Systems edited by ALBI E., MARTINEZ J.M., MA, USA, 2011, pp. 37-39; AVI-YONAH R.S., *Advanced Introduction to International Tax Law*, Northampton, MA, U.S.A., 2019, p. 26.

Consequently, the companies which decide to generate income in a country other than their residence-country are requested to verify whether their activity is structured in such a way as to constitute a PE in that State.

The concept of PE, German origin, first appeared in the Prussian Industrial Code (1845), although taxation was not its main purpose (Henderson, 1958)[14].

It was around the second half of the 19th century, that the Franco-Prussian Treaty (1869) defined the conditions for taxation of the so called "*stehendes Gewerbe*" ("standing operation"). The standing operation required two important components that would later become the key-elements of the modern definition of PE:

1) the place of business in a foreign State;
2) the intention, on the enterprise's side, to develop a long-term business in a specific location.

At this early stage, the countries drew their attention only to the material aspect of the PE; later on, it also arose the need to find a definition for the case of someone directly involved in the operations (agent), following the idea that taxation could be also applied on the basis of a personal nexus.

A general version of the PE concept may be found in 1909 German Double Taxation Act, focused on the "*business activity test*", aimed at preventing double taxation between German States. According to the "*test*", a PE exists if a foreign "*fixed place of business*" is used to conduct an economic activity.

The first practical developments of the scholars' theories and Governments' debate about the concept of PE were due to the creation of the League of Nations (Geneva,1919) and particularly to the institution of the Financial Committee, deputized to establish minimum standardized rules in the field of international trade and to facilitate a fair competition between the countries which won the war.

In this framework, international taxation represented the place where fundamental principles (i.e. the right to tax) could be drafted, in order to govern the commercial

[14] According to HENDERSON W.O., *The State and the Industrial Revolution in Prussia: 1740-1870,* Liverpool, 1958, the Code was mainly oriented to the development of textile industry, the promotion of the German customs union (*Zollverein*) and the ban of strike.

relations between countries, to avoid the practice of double taxation and, even worse, that of "double non – taxation" (Kobesky, 2011; Skaar, 2020; Oats, 2021)[15].
A further "Committee of Experts" was entrusted to study and report the main factors of double taxation and to draft a "Convention Statement", as a guide about the right of taxation (Avi-Yonah, 2019)[16].

The experts' contribution was the starting point for a series of model conventions published between 1923 and 1927.

In 1927, the first draft of the Model Convention against double taxation was published, providing, in the Article 5, the first definition of PE:

«Income from any industrial, commercial or agricultural undertaking and from any other or professions shall be taxable in the State in which the persons controlling the undertaking engaged in the trade or profession possess permanent establishments» (UN, 2001)[17].

Further to the dissolution of the League of Nations, in 1946, the efforts to combat double taxation were initially carried out by the OEEC (European Organization for Economic Development) in 1948 and later by the OECD (Organization for Economic Cooperation and Development).
Since its establishment, in 1961, the OECD promoted the study of the former Model Conventions and finally published, in 1963, its own Model, under the name "Draft Double Taxation Convention on Income and Capital"[18].
The Model Convention and its Commentary have undergone a series of amendments and clarifications (Walker, 2013)[19], the latest one dated 21 November 2017.

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[15] KOBESKY M., *International Taxation of Permanent Establishments Principles and Policy*, Cambridge, 2011, pp. 111 – 12; SKAAR A.A., *Permanent Establishment: Erosion of a Tax Treaty Principle*, Amsterdam, 2020, pp. 121 – 123; OATS L., *Principles of International Taxation,* London, 2021, p. 191.

[16] AVI-YONAH R.S., *Advanced Introduction …*, p. 4, keenly noted that the composition of the Committee, comprising four eminent economists - Luigi Einaudi - Italy, Gijsbert Bruins - Netherlands, Edwin Seligman - U.S.A. and Josiah Stamp - U.K. - was not chosen randomly. In fact, Italy and the Netherlands had traditionally supported source-based taxation, while the United Kingdom, historically the largest exporter of capital, considered that the source-countries should cede jurisdiction to resident-countries and U.S.A. had recently become the world's largest exporter of capital, strongly supporting the residence-principle in tax matters.

[17] See UN Model Double Taxation Convention between Developed and Developing Countries, 2001, New York, *Introduction*, para. A. and Commentary, pp. 68 – 92.

[18] Up to date, more than 3000 tax treaties in force around the world are based on the OECD Model, which is regularly updated.

[19] WALKER B., *The evolution of the Agency Permanent Establishment Concept*, Sidney, 2013, in *https://www.business.unsw.edu.au › Documents › 40-Walker-ATTA2018*.

1.2. The OECD Model of Permanent Establishment.

The definition of "Permanent Establishment" as it is found, respectively, in the two most widespread Models Convention (OECD and UN) aimed at preventing double taxation and based fundamentally on the concept of the "fixed place of business" where all or part of an economic activity takes place (business or enterprise) is still widely accepted in international treaties, although subject to constant revisions, amendments, clarifications and exceptions in the interpretative field[20].

However, the advent of the Digital Economy and Internet have made extremely difficult, in fact, to allocate a taxable income to one or another of the Contracting States and therefore necessary to deepen (Hoffart, 2007; OECD, 2011; IBFD, 2013) [21] the concept developed in the 20th century, as it will be reported in the following paragraphs.

1.3. The Material Permanent Establishment. The Basic Rule: Place of Business.

Paragraph 1 of Article 5 of the OECD Model Tax Convention reads as follows:

«For the purposes of this Convention, the term "permanent establishment" means a fixed place of business through which the business of an enterprise is wholly or partly carried on» (OECD, 2017)[22].

The first part of the above-mentioned Article quotes the basic requirement to declare a PE as such or not, that's the so-called "basic rule": the fixed place of business. It appears, as necessary, the physical presence, which has to be fixed.

The "fixed" connotation has to satisfy three fundamental conditions (OECD, 2019)[23]:

1. the existence of place of business: in that sense, it refers to structures, buildings or lands or sometimes to machinery or equipment that cannot be moved elsewhere; the presence of a distinct place, by the company, in a specific geographic location is characterized by a certain degree of permanence in that area. Therefore, the

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[20] See the Art. 5 (1), both in OECD MTC and UN MDTC.

[21] See HOFFART J., *Permanent Establishment in the Digital Age: Improving and Stimulating Debate Through an Access to Markets Proxy Approach*, in *NW Journal of Technology and Intellectual Property, Vol. 6, Art. 6, Issue 1,* Fall 2007, p. 107; OECD, *Interpretation and application of article 5 (Permanent establishment) of the OECD Model Tax Convention*, 2011, pp. 18 – 20; IBFD, *Taxation of Business Profits in 21st Century*, Amsterdam, 2013, pp. 189 – 192.

[22] OECD, *Model Tax Convention on Income and on Capital: Condensed Version 2017*, OECD Publishing, Paris, in https://doi.org/10.1787/mtc_cond-2017-en.

[23] OECD, *Commentary on Article 5: Concerning the Definition of Permanent Establishment*, in *Model Tax Convention on Income and on Capital 2017 (Full Version)*, 2019, OECD Publishing, Paris, para. 6, *https://doi.org/10.1787/5cd2b87b-en.*

Commentary aims at focusing on the meaning of the concept of fixed and to clarify any doubts regarding the duration of presence. More specifically, it is possible to refer to availability, spatial fixity and temporal permanence of the place of business. Availability implies that the foreign company has the actual possibility to exercise the control on the PE, which has not to be understood in a strictly legal sense, but analyzing the actual availability of the premises. In other words: the mere fact that an enterprise has a certain amount of space at its disposal which is used for business activities is sufficient to constitute a place of business. No formal legal right to use that place is therefore required. Thus, for instance, a permanent establishment could exist where an enterprise illegally occupied a certain location where it carried on its business [24].

The OECD considers that a place of business, as fixed, must be linked to a specific geographical area.

For the duration of the presence of a PE, the OECD doesn't refer to any temporal measure in terms of permanence in a geographical place, but underlines that the business activity has to be conducted in a regular and constant frequency (OECD, 2019)[25].

2. The way in which an enterprise carries on the business. In most cases, the business is conducted totally o partially by people who are dependent by the enterprise, that could be the legal representative or the personnel. The last category could include the personnel of the enterprise or dependent agents; they act habitually and in continuously way on behalf of the company and they have the legal authority to conclude contracts. The business can also be conducted through "*subcontractors*" who act independently or by the collaboration with the employees of the enterprise. However, in both cases the conditions announced in the first paragraph have to be satisfied, so that the *subcontractors* with the employees or not, conduct the business activity in a fixed place linked to a specific geographical area.
3. In the end, the PE can be existed also when the business activity can be carried on by automatic machines and where the operations of the personnel concern the steps of set-up, installation and maintenance of the machines (OECD, 2019)[26].

[24] *See* OECD, *Commentary*, 2019, C-5 (11).
[25] OECD, *Commentary*, 2019, C-5 (28).
[26] OECD, *Commentary,* 2019, C-5 (39).

1.3.1. The positive list.

Paragraph 2 of Article 5 of the Convention reads as follows:

The term "permanent establishment" includes especially:

a) a place of management;

b) a branch;

c) an office;

d) a factory;

e) a workshop, and

f) a mine, an oil or gas well, a quarry or any other place of extraction of natural resources.

This paragraph contains a list, to not to consider as exhausted, of example of places of business, to be classified as PE, in compliance with the requirements set out in paragraph 1.

Paragraph 3 of Art. 5 reads as follows:

«*A building site or construction or installation project constitutes a permanent establishment only if it lasts more than twelve months*»,

indicating the minimum time threshold for a construction site or installation to be classified as PE. This time threshold is, to all intents and purposes, binding even when within the same mentioned articles there is an office or workshop classifiable as PE within the meaning of paragraph 2, that are strictly essential to the performance of the activity under construction. It follows that profits attributable only to activities performed through an office or workshop are to be considered profits of the PE (OECD, 2019)[27].

1.3.2. The negative list. The preparatory or auxiliary activities.

A fixed place of business, in which a foreign enterprise conducts all or part of its business, is not always a necessary condition for the foreign enterprise to have a PE.

In fact, in the Art. 5, paragraph 4, of the Convention, a number of specific exceptions listed as follows form the definition of PE:

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[27] OECD, *Commentary*, 2019, C-5 (51), renumbered and amended on 21 November 2017.

«Notwithstanding the preceding provisions of this Article, the term 'permanent establishment' shall be deemed not to include:

a) the use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;

b) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of storage, display or delivery;

c) the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise;

d) the maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or of collecting information, for the enterprise;

e) the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity;

f) the maintenance of a fixed place of business solely for any combination of activities mentioned in subparagraphs a) to e),

provided that such activity or, in the case of subparagraph f), the overall activity of the fixed place of business, is of a preparatory or auxiliary character».

Compared to the previous paragraph, paragraph 4 contains an important exception to PE; namely, that if the activities carried on are of an "*auxiliary*" or "*preparatory*" nature for the core business, even in the presence of a permanent post, the latter one is not classifiable as a PE.

That's why the Commentary suggests a definition for an activity listed as preparatory or auxiliary, i.e. a support activity or set of activities those precede and ensure the proper performance of the general activity of the enterprise.

A preparatory activity, usually of short duration, may be the training of employees carried out at a given location before they can start work at the various sites in a foreign location (OECD, 2019)[28].

If a company with one or more subsidiaries in a certain country has a so-called "*management office*", the management activity, even if carried only in part, cannot be considered as auxiliary or preparatory activity (Peroni et al, 2021)[29].

[28] OECD, *Commentary*, 2019, Article 5, para. 4 (60), renumbered and amended on 21 November 2017.

[29] PERONI R. J., BROWN K. B., FLEMING J. C., *Taxation of International Transactions: Materials, Text, and Problems,* St. Paul, MN, U.S.A., 2021, p. 876.

The criterion is that the management activity constitutes an essential part of the core business of the enterprise and so they can't be summarized as preparatory (OECD Commentary, 2019)[30].

1.4. The Anti-Fragmentation Rule.

Paragraph 4.1 introduces the "*Anti-Fragmentation rule*", a particular innovation to the 2017 version of the Model Tax Convention.
It reads as follows:

«Paragraph 4 shall not apply to a fixed place of business that is used or maintained by an enterprise if the same enterprise or a closely related enterprise carries on business activities at the same place or at another place in the same Contracting State
and

a) that place or other place constitutes a permanent establishment for the enterprise or the closely related enterprise under the provisions of this Article, or
b) the overall activity resulting from the combination of the activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, is not of a preparatory or auxiliary character, provided that the business activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, constitute complementary functions that are part of a cohesive business operation».

According to the clause, where one or more interrelated companies, in a State, carry on several activities, a PE exists if the different activities are related to complementary functions of the same economic activity, unless the activities, taken together, are of a preparatory or auxiliary nature.

The issue of the preparatory or auxiliary activities, therefore, becomes of fundamental importance in the adoption by companies of their tax policy choices, given that in the light of the "new" Article 5 of the Convention, the identification of "*auxiliary or preparatory*" activities contributes to delineating the boundary line, fixed by the Article

[30] OECD, *Commentary*, 2019, C-5 (71), renumbered and amended on 21 November 2017.

7 (para.1[31]) of the Convention, between the taxing power over business income by the State of residence and that of the State of source (Oats, 2021; Garbarino, 2022)[32].

In fact, while paragraph 4 of the aforementioned Article 5 emphasizes how, for the purposes of exemption (i.e. the operation of the so-called "*negative list*"), economic activities must be preparatory or auxiliary, the new paragraph 4.1 was introduced to neutralize the distorting effects of the use of the so-called "*fragmentation of activities*". In the OECD's view, it is necessary to prevent illegitimate and abusive use of the negative list; in fact, a multinational group could easily conceal its structure and, therefore, it proves necessary to extend the *Anti-Fragmentation rule* in order to assess not only the individual company, but also the entire group as a whole (OECD, 2019)[33].

1.5. The Personal Permanent Establishment.

As far as "personal nexus" is concerned, Academia debate (Feuerstein, 2011)[34] concluded that: "*If the PE threshold only consisted of the basic rule on PEs, i.e. a fixed place of business made of bricks and mortar, a foreign enterprise could simply avoid a PE in the other State by engaging salesmen or other representatives who would then perform the business activities which would otherwise need to be undertaken by the foreign enterprise itself through a fixed place of business*".

According to the Article 5, there are two circumstances in which a foreign company may be subject to the permanent establishment tax regime:

- the "*physical presence*" Permanent Establishment [Art. 5(1)] when the activity of the foreign company is carried on in that State by facilities managed by the enterprise itself;
- the "*Agency*" Permanent Establishment [Art. 5(5)]. The enterprise's services are rendered by a particular type of agent, who is a tax resident in that State and acts on behalf of the foreign company.

[31] The text of Art. 7, para.1 reads as follows: «*Profits of an enterprise of a Contracting State shall be taxable only in that State, unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as a foresaid, the profits that are attributable to the permanent establishment in accordance with the provisions of paragraph 2 may be taxed in that other State*».

[32] OATS L., *Principles of International Taxation…*, quoted above, pp. 205 – 207; GARBARINO C., *Taxation of bilateral investments: tax treaties after BEPS*, Northampton, MA, 2019, p. 19.

[33] OECD, *Commentary*, 2019, C-5 (79).

[34] FEUERSTEIN D., *The Agency Permanent Establishment*, in *International and EU Tax Law,* Vienna, 2011, p. 105.

Thus, although there is no requirement of a fixed place of business or the presence of other premises and/or employees, the "*Agency PE clause*" has been added to the Article 5 as a deeming rule.

1.5.1. The dependent agent.

Even in the absence of a fixed place of business, the Article 5(5) gives to the PE an exclusively "*personal*" connotation: *«Notwithstanding the provisions of paragraphs 1 and 2 but subject to the provisions of paragraph 6, where a person is acting in a Contracting State on behalf of an enterprise and, in doing so, habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, and these contracts are*

a) in the name of the enterprise, or

b) for the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use, or

c) for the provision of services by that enterprise, that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities which that person undertakes for the enterprise, unless the activities of such person are limited to those mentioned in paragraph 4 which, if exercised through a fixed place of business (other than a fixed place of business to which paragraph 4.1 would apply), would not make this fixed place of business a permanent establishment under the provisions of that paragraph».

People likely to be elected as personal PE are those "*candidates*", whether employees or not of the company, who act in the name of and on behalf of the company; furthermore, it's not necessary that those people are "*source-country resident*".

The addition of this paragraph, i.e. the fact that one can speak of a personal PE when there is a subject (person or entity), as defined above, is to ensure that the host company is taxed for the profits it generates as a PE (OECD Commentary, 2019)[35].

That's why the Article 5(5) lists two conditions (OECD, 2019)[36]:

[35] OECD, *Commentary*, 2019, C-5 (82).
[36] OECD, *Commentary*, 2019, C-5 (84).

1) people who have the authority to conclude contracts in the name and on behalf of the company. The ability to conclude contracts depends on the relevant laws of that country and on the fact that even in the absence of negotiating activity, the other party may conclude the contract without the acceptance of the terms. In accordance with the relevant law, a contract is concluded in a State, but it is signed in another State. It's the case when a company concludes the contract, by the operating figure, accepting the third part's offer (OECD, 2019)[37].

2) people having an active position for the drafting of the contract, which is then concluded without substantial changes by the company.

   The fact that a person is authorized to negotiate all elements and parts of a contract in a such way that it will produce some commitments towards the company and the third party, this will implicate the existence of a PE for the enterprise. Usually, the typical leading role of the agent is associated with the conviction attempts towards the third party to stipulate a contract with the enterprise[38].

The 2017 version of paragraph 5 - people that «*habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts*»[39] - supposes that these activities are continuously and habitually performed. The Commentary quotes as example a person who normally receives and solicits orders regarding the transfer of goods from the company's warehouse upon company's authorization (OECD Commentary, 2019)[40].

Sub-paragraphs (a), (b) and (c) circumscribe a certain number of contracts concluded by a person in the name and on behalf of the company which generate obligations between the company and a third party (OECD, 2019)[41].

These contracts may have as their object «*the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use, or"* [5(5, b)], *"for the provision of services by that enterprise* [5(5, c)] » (OECD, 2019)[42].

[37] OECD, *Commentary*, 2019, C-5 (87).
[38] OECD, *Commentary*, 2019, C-5 (88).
[39] OECD, *Commentary*, 2019, C-5 (89).
[40] OECD, *Commentary*, 2019, C-5 (89).
[41] OECD, *Commentary*, 2019, C-5 (91, 94).
[42]OECD, *Commentary*, 2019, C-5 (92). See *infra* subparagraph 1.6.1.

Anyway, as it was observed in slop of the old version of the OECD MTC (Pleijsier, 2001; Walker, 2013) [43], these contracts regulate transactions strictly related to the core business of the company.

1.5.2 The independent agent.

The Art. 5, paragraph 6 reads as follows: *«5 (6) Paragraph 5 shall not apply where the person acting in a Contracting State on behalf of an enterprise of the other Contracting State carries on business in the first mentioned State as an independent agent and acts for the enterprise in the ordinary course of that business. Where, however, a person acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, that person shall not be considered to be an independent agent within the meaning of this paragraph with respect to any such enterprise».*

So, based on the Article 5(5) a personal PE is a "*dependent agent*" who habitually concludes contracts in the name and on behalf of an enterprise. By contrast, it should be inferred that there is no personal PE when "*independent agents*" carry on the business. The independence depends on the combination of some factors, e.g. the extent of the agent's duties and responsibilities and the agent's "*radius of action*" in relation to the directions issued by the company.

Another factor to be considered is whether or not the agent is obliged to follow a strict and detailed list of instructions given to him by the company (OECD, 2019)[44].

A further criterion to be taken into account is the number of companies represented by the agent. Actually, this latest criterion is not fully functional for the analysis of the agent's independence; it seems to be preferable to opt for an analysis that takes into account all the factors listed above, as a whole.

On the other hand, a dependence may be identified where a person acts in the normal course of business for a multiplicity of companies, without any of them being predominant, if those companies act in fact with a view to exercising control over the agent. However, it is essential to understand whether the activities carried on by the agent

[43] In this regard, before the amendments included in the OECD MTC 2017, see the comments of PLEIJSIER A., *The Agency Permanent Establishment, Practical Applications. Part Two*, in *Intertax*, Volume 29, Issue 6/7 (2001) pp. 218 – 232; WALKER B., *The evolution of the Agency Permanent Establishment Concept*, Sidney, 2013, pp. 8-15.

[44] OECD, *Commentary*, 2019, C-5 (104 –105).

constitute an autonomous business whose risks and benefits fall directly on the same agent (OECD, 2019)[45].

Finally, the subparagraph 8 reads as follows: *«5 (8) For the purposes of this Article, a person or enterprise is closely related to an enterprise if, based on all the relevant facts and circumstances, one has control of the other or both are under the control of the same persons or enterprises. In any case, a person or enterprise shall be considered to be closely related to an enterprise if one possesses directly or indirectly more than 50 per cent of the beneficial interest in the other (or, in the case of a company, more than 50 per cent of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company) or if another person or enterprise possesses directly or indirectly more than 50 per cent of the beneficial interest (or, in the case of a company, more than 50 per cent of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company) in the person and the enterprise or in the two enterprises».*

The first part of the paragraph defines what "*closely related*" person means by a subjective point of view. For closely related person it refers to the situations in which, on the basis of a special agreement, that person or enterprise carries on similar powers to those deriving from a condition of control, i.e. as if they owned more than 50% of shares (OECD, 2019)[46].

The second part, instead, refers to an object legal test, defining the "*closely related person*" based on actual circumstances (OECD, 2019)[47]:

a) direct or indirect ownership, by a person of more than 50% of the shareholding or, in the case of a company, of more than 50% of the total voting rights and share capital;
b) direct or indirect ownership, by a third party of more than 50% of the shareholding of the person or company or, in the case of a company, of more than 50% of the total voting rights and share capital (Vann, 2006; Walker, 2013)[48].

[45] OECD, *Commentary*, 2019, C-5 (109).
[46] OECD, *Commentary*, 2019, C-5 (120).
[47] OECD, *Commentary*, 2019, C-5 (121).
[48] VANN R., *Tax Treaties: The Secret Agent's Secrets, British Tax Review*, no. 3 (2006), p. 548, denounces some ambiguity in the formula formerly used by paragraph 8 of art. 5; in the same sense WALKER B. *The evolution of the Agency…*, already quoted, p. 15.

1.5.2.1. The commissionaire arrangements.

There is another point of discussion which is worth mentioning briefly here, even though it will be deepened in the next Chapter, dedicated to the PE in the BEPS Project scenario: it is the position of the so-called "*commissionaire arrangements*".
Action 7 of BEPS Plan contains important changes to the definition of PE, in order to prevent tax avoidance risks; the commissionaire arrangement is one of the possible ways, along with other strategies, to avoid the constitution of a PE.
A foreign company that uses a commissionaire arrangement does not constitute a permanent establishment as such, thereby circumventing the application of the Art. 5 of the OECD Model Tax Convention.

In a typical commissionaire arrangement, an agent concludes the contract on its name, but on behalf of its principal, usually a foreign enterprise, which has the ownership of the goods and signs the contract (OECD, 2015)[49]. Neither obligations nor enforceable rights arise between the final consumer and the business.
Thus, through such agreements, a foreign company is able to sell its products in another country, without technically owning a PE there, to which those sales should be attributed for tax purposes: i.e. without being substantially taxable in that country on the profits, which are generated by the sales, made there.
On the other hand, since the person making the sale is not the actual owner of the goods, that person is likewise not taxable on the profits arising from that sale and may be taxed only on the remuneration he/she receives for the services rendered (usually, a commission). The more significant share of profits is attributed to its principal.

According to the new version of the OECD Convention, a commission contract may contain the prerequisites for a PE if the object of the contract is the transfer of ownership of property owned by the principal or the provision of services.
However, commission contracts may give rise to doubts as to whether one is dealing with a PE or not, because the interpretation of a personal PE in *Common Law* or *Civil Law* countries is different.

[49] OECD, *Preventing the Artificial Avoidance of Permanent Establishment Status, Action 7 - 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, 2015, p. 9, OECD, Paris - Cedex, in *https://doi.org/10.1787/9789264241220-en.*

In *Civil Law* countries, an agent may act under a mandate with or without representation. In the first case, the agent acts in the name and on behalf of the principal; in the second case, it acts in its own name by binding itself to the contract. Underlying this, there is a further contract, concluded between the agent and the principal, setting out the rights and duties existing between the respective counterparties (Barbier, 2016; Oats L., 2021)[50].
In *Common Law* countries, there is no distinction between a mandate with or without representation, and the substantial difference lies in whether or not the agent acts in the name and on behalf of the principal.

1.6. The Permanent Establishment Risk.

The internationalization process, i.e. the relocation of a company's production and/or service activities, can take place in different ways that take into account both environmental (of the foreign country) and internal variables attributable to the company's characteristics.
The choice of entry strategy is therefore a very delicate phase, influenced, among others, by fiscal factors. Since the representative office does not allow commercial activities to be carried on, but only promotion, advertising, networking and data collection of the foreign market, the choice of the permanent establishment is, therefore, a natural alternative.

An enterprise that establishes a PE in a foreign country splits a portion of its activities, which are treated, not only "*de facto*", as part of the economic citizenship of that country. Integrated business models normally involve substantial tax obligations, which eliminate tax savings.

In most countries, the main effects of the establishment of a PE are tax registration, tax filing, the expectation of paying income taxes in that country, and other administrative duties, especially because over time the PE definition have included along with a 'place of business' and an 'agent' (dependent or independent) also the notion of "*Service PE*"

[50] BARBIER C., *The Permanent Establishment in a post BEPS world*, Tilburg, 2016, pp. 57-58, in *http://arno.uvt.nl› show*; OATS L., *Principles of International Taxation,* London, 2021, p. 211.

(UN, 2017)[51] and that of global "*Professional Employer Organizations - PEO*" (Steiner S., Wimpissinger C., 2012)[52].

As has already described, the PE concept requires that a recognizable activity be carried on in a Sate before the tax authority (of that country) can attract the company's business income to taxation. To sum up, the key elements are the following ones: (i) the existence of a place of business, (ii) the place must be fixed and at a disposal of the enterprise, (iii) a dependent agent who normally conducts wholly or partly the business and (iiii) a considerable set of activities (i.e. not 'auxiliary or preparatory' activities) conducted in that fixed place.

The awareness of these distinctive characteristics is essential in order not to incur in the so-called "*Permanent establishment risk*", that is «*the risk that the presence of an enterprise in a foreign country has inadvertently created a 'permanent establishment' in that country. Meaning the enterprise may inadvertently be liable for corporate income tax and any attendant penalties*» (Donnelly, 2022)[53].
That's why companies should constantly and actively monitor the presence of potential permanent establishments risks in order to avoid unexpected claims concerning the below areas.

1.6.1. Associated tax and tax registration liabilities.

In addition to the tax burden, there are other reasons why PE risk is a serious problem for companies engaged in the process of internationalization. The creation of a PE leads to the following tax-related obligations of the company in a foreign country: the payment of income - tax form profits generated by the PE, the payment of taxes from salaries of employees of the PE and, in many countries, the payment of indirect taxes such as Value Added Tax (VAT) or Goods & Services Tax (GST) on gross sales.

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[51] According to Art. 5 (3, b) of the UN Model Double Taxation Convention 2017, "*Service PE*" is "*the furnishing of services, including consultancy services, by an enterprise through employees or other personnel engaged by the enterprise for such purpose*".
[52] STEINER S., WIMPISSINGER C., *Services and the Service PE under Treaty Law from an Austrian Perspective*, in *Intertax,* Volume 40, Issue 10 (2012) pp. 566 – 572, *https://doi.org/10.54648/taxi2012056*.
[53] DONNELLY D., *What is Permanent Establishment and Why Does it matter*? in *https://nhglobalpartners.com/what-is-permanent-establishment/*

1.6.2. Associated employer liabilities.

In the case of a personal PE, the principal is liable if he or she fails to fulfil obligations such as: registering an employee ID; withholding income and salary tax; paying social security contributions; and respecting employee rights (minimum wage, equal employment opportunities).

If a company is investigated for PE, there is also a risk that the company will be found to have breached their obligations as an employer. This is because liability as an employer in a country is broadly analogous to corporate tax liability in a country: that is, it is a factual matter about the activities of the business which determine liability, not any official legal status of the business.

To illustrate this point, consider a case managed from the UK employment appeal tribunal which considers employer liability in the UK with respect to a US employee, who had been seconded to the UK.

If a business is found to have become a local employer, as well as a Permanent establishment, they may be liable for:

- ✓ a failure to register an employer ID;
- ✓ a failure to withhold employee income and payroll tax;
- ✓ a failure to make necessary social contributions to employees such as, health insurance, pension, unemployment insurance, and worker's compensation contributions;
- ✓ breaching employee rights, such as minimum wage and equal employment opportunity rights. (Donnelly, 2021; *Case* Smith v Pimlico Plumbers, 2022)[54].

In line with failures to pay corporate income tax and indirect taxes, these employer failures could lead to back payments, interest and penalties.

[54] See DONNELLY D., *What is Permanent Establishment…*, 2021, already quoted, and the case *Smith v Pimlico Plumbers Ltd – Court of Appeal Decision on Workers and unpaid leave, UK, 2022, with notes of* WRENCH S., *16 February 2022* in *https://esphr.co.uk/news/smith-v-pimlico-plumbers-court-of-appeal-decision-on-workers-and-unpaid-leave/.*

1.6.3. Increased audit attention.

A company that is temporarily audited by the tax authorities in a country will be more likely to be subject to similar audits in the future to verify the correct or non-fulfilment of tax obligations.
Any business that has been found wanting by the authorities will have an increased likelihood of being audited in the future. This includes tax audit and any compliance audit from employment regulators (Donnelly, 2021)[55].

1.6.4. Reputational damage.

In the case of the company is found to be in breach of its tax obligations, it will suffer damage to its image, not only with the tax authorities, but also with its consumer group.
A failure to pay taxes, and other associated compliance failures, thus, can significantly hurt the reputation of an enterprise in a country, both with regulators and (when published), the public.

1.6.5. Inefficient tax planning.

A failure to recognize and fund a corporate tax liability in advance usually indicates ineffective tax planning in general.
It is crucial that any business expanding overseas carefully considers how to manage its international tax liabilities. This might include thinking about the use of subsidiaries, joint ventures, holding companies and foreign investment trusts in order to best manage the tax aptitude.

1.6.6. Covid-19 and the Permanent Establishment Risks.

The impact of the pandemic from COVID-19 and its effects on the very concept of "Permanent Establishment" represent the "core issue" of the present work. The last Chapter and the Conclusion are dedicated to them.

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[55] See again DONNELLY D., *What is PE…*, 2021.

However, it seems appropriate to anticipate some considerations with particular reference to the specific risks which can stem from the "Permanent Establishment" scheme, caused by the health prevention measures taken at global level on the WHO initiative, including a so-called "lockdown" to impede the diffusion of virus, an extensive vaccination campaign to the people and special certificates to prove that they have been subject[56].

These unprecedented measures imposed or recommended by governments, including travel restrictions and curtailment of business operations have been into effect in most jurisdictions in various forms and stages during most of 2020, due to the COVID-19 pandemic, and this situation continued in many countries to the end of 2022.

The OECD Updated Guidance (OECD 2021)[57], aimed at providing more certainty to taxpayers during this exceptional period, recommending to the countries a "case by case" approach, with regard to the PE contained in the Model Tax Convention, didn't avoid the PE risk related to specific aspects of the situation caused by the pandemic ("*ex multis*", Barone et al, 2020)[58].

Among the various aspects of the "Permanent Establishment" scheme that can be inferred from the OECD Model Tax Convention, what appears to be of greater relevance as far as the effects on "PE Risk" concern individuals, understood as "workers" or other similar qualifications[59].

In fact, due to the aforementioned restrictions, many cross-border workers were unable to physically perform their duties in the country where (or in favor of which) they were actually working.

In this regard, the Article 15 of the OECD MTC comes up establishing that "*salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is*

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[56] Referring, in particular, to the adoption, at EU level, of the so-called "Green Pass" ("White card" in the United States of America), which reported the number and the type of vaccinations administered, in order to allow cross-border travel.

[57] See OECD, *Tackling Coronavirus (COVID-19): Contributing to a Global Effort, Updated guidance on tax treaties and the impact of the COVID-19 Pandemic*, Paris-Cedex, 2021.

[58] BARONE et al, *COVID-19 – Comments on Permanent Establishment Risks*, 2020, in *https://blog.pwc-tls.it/en/2020/04/15/covid-19-comments-on-permanent-establishments-risks/.*

[59] Particularly interesting, in this regard, is the case of the researchers of a US University blocked in China by COVID-19, but subsidized by the University for their research and therefore beneficial owners of "payments", pursuant to Art. 20 of the OECD Model. In fact, payments were actually received in that country (China) in which they carried out their research and therefore relevant pursuant to the Art. 21 of the same OECD Model, where the duration of the stay, although compulsory, exceeded the threshold of one year. On this point, please refer to Chapter 4.

exercised in the other Contracting State" that seems to correspond precisely to the unforeseeable and occurred circumstances.

Generally, the OECD focuses on the possible consequences, for employees and employers, which would have with reference to the application of the Art. 15 of the Conventions, should the contingent situation change the existence of the requirements established by the same Art. 15.

In its "Guidance" related to the COVID-19 pandemic, OECD suggested that the tax authorities adopt, at that stage, a substantially more flexible line, in order to allow the suspension or the reimbursement of the withholdings wrongly applied. According to the OECD, exceptional circumstances require an exceptional level of coordination between countries to mitigate enforcement and related administrative costs for both employees and employers, associated with the involuntary and temporary change of the place where (and in favor or on behalf of whom) the working activity it is ordinarily carried on.

The main possible scenarios could basically be two (Barone, 2020)[60]:

1) a person is temporarily away from home (perhaps on vacation, perhaps to work for a few weeks) and remains stuck in the host country due to the COVID-19 crisis. If the country's internal regulations provide that residence status can be acquired on the basis of physical permanence in the country for a certain number of days, then, there could be significant tax implications;
2) a person works in a country (the "current country of origin") and has acquired residency status there, but temporarily returns to his "previous country of origin" due to the COVID-19 situation. These people may never have lost their status as residents in their previous country of origin under national law, or they could regain their residence status upon their return.

In both scenarios, the OECD recommended that Countries evaluate the tax residence on the basis of international treaties, in order to avoid possible cases of "*double residence*" due to temporary location, determined by the application of individual national regulations.

Indeed, the OECD emphasized that an individual can only be resident in one country at a time and that the rules are laid down in the Article 4 of the OECD MTC.

However, in the second case, applying the same rules of the treaty, there would be a more uncertain result because the link between the person and the previous country of origin is

[60] BARONE et al, *COVID-19 – Comments…*, p. 6.

stronger and the fact that the person moved to the previous country of origin during the COVID-19 crisis may risk reversing the balance towards the previous country of origin.
In this case, the "*habitual residence test*" would not be able to satisfy the established requirement simply by determining in which of the two Contracting States the person spent more days during that period.
Therefore, according to the OECD "Guidance", since the COVID-19 crisis is a period of great changes and an exceptional circumstance, in the short term, tax administrations and competent authorities will have to consider, for the purposes of assessing residence, a period of time that is not influenced by exceptional events like that, but that is "*normal*" for the person.
Spite OECD suggestions and the caution shown by the concerned countries, it seems actually conceivable a "*PE risk*" in these exceptional cases, depending on single attitude of the States or of their Tax Administrations.

1.7. Redefining the traditional concept of Permanent Establishment.

The advent of the Internet in the early 1990s created the preconditions for the birth and gradual spread of a new phenomenon, i.e. Digital economy.
Between the 2000s and 2010s, the discovery of new communication and information technologies further contributed to the global propagation of the digital economy.
The continuing development of the dematerialized economy, based on transactions that originate and finalize in the network, raise major tax issues (i.e. "*harmful tax competition*") at international level which necessarily require coordinated supranational, multilateral or bilateral actions (Di Gregorio et al, 2005)[61].

The advent of the digitalization of the economy has enabled multinational companies to establish themselves as global enterprises from an early stage, since their digital presence in individual countries, rather than the creation of a subsidiary, is sufficient. Not only that, but the lowering of customs and currency barriers, the change of product type from "*material*" to "*digital*", and finally the shift to a predominantly service-based economy,

[61] With particular reference to the issue of the "*Harmful Tax Competion*" and to the countermeasures suggested by the OECD in its *"The OECD's Project on Harmful Tax Practices: the 2004 progress Report*", see "*ex multis"* DI GREGORIO C., MAINOLFI G., SCAZZERI G., *L'imposta sulle società nell'Unione Europea*, Milano, 2005, pp. 359 – 363.

has prompted companies to review their entry strategy into new countries, opting for countries with advantageous taxation.
In view of the advent of digitalization, and thus the disappearance of the physical presence of operators and the requisite fixed place of business, it is appropriate to review the appropriateness of the concept of Permanent establishment in the context of the digital economy (Gaiani et al, 2018)[62].

Four revisions to the PE concept have been proposed: Virtual Permanent Establishment approach (or the significant economic presence), the Base Erosion approach and Refundable withholding approach.

1. The Virtual Permanent Establishment approach. Following the publication of the OECD/G20 Base Erosion and Profit Shifting Project 2015 Final Report, some changes were suggested to the traditional definition of the PE concept. At the European level, it is the most discussed theory.
   To define the PE from the perspective of lasting economic permanence, two types of factors must be considered, qualitative and quantitative. Digital factors, i.e. digital platforms (databases, online market, etc.) belong to the first category, while revenue-based and user-based factors belong to the quantitative criteria, as they define numerical thresholds above which the digital presence of a company can be claimed. Examples of these thresholds could be: the minimum number of users of digital platforms, the percentage of sales realized from the provision of digital services and/or goods in the host country, etc. (Cockfield, 2004; Sestakova M, 2018)[63].

2. The Base Erosion approach (Doernberg, Hinnekens, 1999)[64]. This approach tried to reconcile the essential features of the classical definition of PE with the doubts of those countries adopting a new business model for the first time.

[62]GAIANI L., GUARNERIO G., TRABUCCHI A., TRETTEL S., *La fiscalità nell'economia digitale. Problematiche e scenari possibili,* in *https://www.fondazionenazionalecommercialisti.it/filemanager/active/01270/2018_05_23_La_fiscalit___ nell___economia_digitale._Problematiche_e_scenari_possibili_.pdf?fid=1270, 2018, p. 6.*
[63]COCKFIELD, A.J., *Reforming the Permanent Establishment Principle through a Quantitative Economic Presence Test*, in *Tax Notes International*, Vol. 33, No 7, pp. 643-54; SESTAKOVA M., *Redefining the "Permanent establishment" concept to make its measurement more relevant for a digital economy,* 2018, p. 5 available in *http://www.cutn.sk/Library/proceedings/km_2018/PDF_FILES/11_Sestakova-128-136-9s.pdf*
[64] DOERNBERG R., HINNEKENS L., *Electronic commerce and international taxation*, The Hague, 1999, Chapter 4 "Policy Proposals".

The Base Erosion approach's fundamental idea is that «*a country where the business transaction takes place is authorized to collect single rate withholding tax for every income gained from transactions that are potential to grind tax basis of the country*». In order to prevent a double taxation, others suggested that the single rate taxes imposed can "*be credited or deducted from the income tax amount that has been paid to the origin country of the non-resident company*" (Hendri et al, 2021)[65].
An obstacle to implementing this approach is the need for agreements between both countries, the origin one and the destination one, defining the rate and criteria for erosion.

3. The "Refundable withholding" approach. Compared to previous models, withholding tax approach (Pinto, 2003)[66] is one in which source countries are allowed to withhold a rate based on the profits from all e-commerce transactions. The value of the withheld rate is defined in a multilateral agreement.
   In addition, the value of the withheld tax could be refunded if the total gross sales of the foreign company were below a minimum threshold (Ndonga D., Riegler A., 2019)[67].

1.8. The relevance of the Permanent Establishment in the Digital Economy.

The Internet's spread and the progressive proliferation of e-commerce, especially during the period of the COVID-19 pandemic, has pressed international organizations, such as OECD and EU, to revisit the issue of taxation for MNEs that use technology and digitalization to shift profits to low-tax countries or to erode the tax base.
The concept of Permanent establishment, understood as a physical presence in the foreign country, has been directly affected by the strong development of the Internet and the volume of e-commerce business of the so-called digital companies, revealing considerable perplexity about its application.

[65] HENDRI, RAHAYU N., SETYOWATI M., *Redefining Permanent Establishment Concept of e-Commerce Cross-border Transaction: A Preliminary Study in Indonesia*, 2021, in *Journal of Internet and e-Business Studies*, Vol. 2021, p.10.
[66] PINTO D., *E-Commerce and Source-Based Income Taxation*, Amsterdam, 2003, pp. 47 – 66.
[67] NDONGA D., RIEGLER A., *Source-Based Taxation of E-commerce Income: A study of the Unresolved Issues,* in *Journal of Business Law,* 2019, 6, p. 470.

Although realized around the mid-2000, the works on the so-called "Digital Age" (Pinto, 2003, Hoffart, 2007)[68], nevertheless remain a superb theoretical support in the study of the effects of E-commerce on international taxation and, in particular, on the concept of Permanent Establishment as it has been drafted in the OECD MTC and in the consequent international tax treaties (Singh, 2014)[69].

The works point out that the developments of the traditional PE concept are biased towards giving importance primarily to the geographical location of buyers and sellers (of physical goods) and thus to the place where value is created rather than the place where wealth originates.
That misunderstanding stemmed from the fact that the PE concept, as it has been drafted in the Model Tax Conventions, is rather on a "delegation of access to markets" than on the creation of value. That's due to the fact that the early attempts of a physical presence made by a non-resident entity were seen as a way of approximating 'access' to a foreign market.
Their supporting idea refers to early UN documents in which the term "origin of wealth" is mentioned, identifying how the steps leading to the realization of a profit are an integral part of the creation of that profit; considering the PE concept under a different approach compared to the "value creation", they argue that the interpretation of PE as "delegation of market access" could already have been considered at the time of the UN definition of PE.

That idea represents a good supporting point towards the revision of the PE concept.
Just like the "creation of value" once presumed a tangible presence, access to markets required a physical presence too (a store, for example). While the "creation of value" can now be achieved by automated software functions bearing no relationship to geographic boundaries, the same can be said for businesses' market access efforts.
As emphasized by the OECD, the difficulty of defining the Permanent Establishment concept by its traditional characteristics emerges, given the diffusion of new business models in the Digital economy. It is now becoming more and more difficult to trace the so-called "*fixed place of business*" and to establish the link between the on-line economic

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[68] HOFFART B, *Permanent Establishment in the Digital Age: Improving and Stimulating Debate Through an Access to Markets Proxy Approach*, in NW. J. Tech & Intell. Prop., 2007, 6, pp. 106-121.
[69] SINGH, M.K., *Taxing E-Commerce* on the Basis of Permanent Establishment*: Critical Evaluation,* in *Intertax*, Vol. 42 Issue 5.

transaction with a particular geographical location (Della Rovere A., Viola I., 2019; Giovannini, 2022)[70].

By implementing these aggressive tax planning schemes, a company is able to avoid taxation both in the origin country and in the destination country, where its customers live and buy.

In the attempt to amend the Art. 5 of the OECD MTC including the term "digital permanent establishment" various solutions have been proposed, either in the form of a separate text or within the positive list in Art. 5(2). In both cases, one must proceed with extreme caution (Dulevski S., 2020)[71].

However, more intriguing in this regard is by far the Action 1 of the BEPS Project, entitled "*Tax Challenges Arising from Digitalization*".

Since the OECD MTC doesn't mention the criteria to classify the "*significant digital permanence*", reference should be made to Action 1 and specifically to the document "Addressing the Tax Challenges of the Digital Economy, Action 1 - 2015 Final Report" (OECD, 2015)[72].

According to the document, one may identify a significant digital presence if the combination of three fundamental elements is fulfilled: i) the amount of revenue decoupled from its place of origin, ii) the processing of data and end-user elements, iii) the value of revenue from activities such as, for example, the sale of data, the sale of a marketing and advertising package for a given customer base as well as the conclusion of commercial contracts.

The numerical value of the three above-mentioned criteria has been the subject of subsequent investigations by EU institutions. In particular, on 21 March 2018, the European Commission approved a package for fair taxation of the digital economy, consisting of two proposals of Directives and one Recommendation.

The short-term proposal delivered by the EU COM (2018) n. 148 final intends to corresponds to the requests of various European Member States to have a common

[70] DELLA ROVERE A., VIOLA I., *Prospettive della digital economy in ambito internazionale, europeo e nazionale*, in *Il Fisco*, 2019, 10, pp. 947-8; GIOVANNINI A., *Territorio invisibile e capacità contributiva nella Digital Economy*, in *Rivista di diritto tributario*, fascicolo n. 5/2022, pp. 497 - 528, in *https://www.rivistadirittotributario.it/2022/11/07/territorio-invisibile-e-capacita-contributiva-nella-digital-economy/.*

[71] DULEVSKI S., *Digital Permanent Establishment,* in Economic Archive, 2020,4, pp. 53-4.

[72] OECD, *Addressing the Tax Challenges of the Digital Economy, Action 1 - 2015 Final Report*, 2015, available in *https://read.oecd-ilibrary.org/taxation/addressing-the-tax-challenges-of-the-digital-economy-action-1-2015-final-report_9789264241046-en*.

internal, albeit provisional, rule for the taxing profits earned from digital activities, which were not considered by the tax point of view before [73].

The long-term proposal [(COM), 2018) n. 147 final][74], on its side, includes a reform about the profit taxation rules so that they include the concept of the significant digital presence. The innovative element is the introduction of a taxable nexus with a given geographical jurisdiction even though the company is not physically present there. The new rule aims at equalizing the tax contribution of on-line businesses with that of so-called "*brick-and-mortar*" companies.

A significant digital presence can be defined in a Member State if at least one of the following criteria is met:

- profit amount, derived from the sale of services and/or digital goods in the jurisdiction, exceeding 7 million euros in the tax period;
- number of digital users exceeding 10,000 euros in the tax period,
- number of contracts for the sale of goods or the provision of digital services concluded between users and the company must exceed 300,000 units.

[73] COM (2018) 148 final 2018/0073(CNS).

[74] See the proposal EU COM (2018) n. 147 final, dated 21 March 2018, laying down rules relating to the corporate taxation of a significant digital presence, update 7 March 2019, with comments of KOFLER G., *The Future of Digital Services Taxes*, in EC *Tax Review*, 2021-2, pp. 50 – 54. To date, a complete regulation concerning the taxation of significant digital presence has not been adopted yet at EU level.

CHAPTER 2

THE CONCEPT OF PERMANENT ESTABLISHMENT IN THE FRAMEWORK OF THE OECD ACTION PLAN ON BASE EROSION AND PROFIT SHIFTING (BEPS)

3.1. The revised interpretation and application of the Art. 5 (Permanent Establishment) of the OECD Model Tax Convention 2011 and 2012.

Since 1963, when the first "Model Convention with respect to Taxes on Income and Capital" was enacted, the PE concept (Article 5) has raised numerous questions regarding its application by scholars and practitioners. Between 2011 and 2012, the OECD published two documents with the aim of accepting suggestions for changes from the international community regarding the difficulties in interpreting the PE definition as it read in the Article 5 of the OECD MTC.

On 12 October 2011, the OECD released its first document in this regard: the "Discussion Draft" (OECD, 2011)[75]; the aim was to summarize not only the requests for changes, but also the clarifications on the interpretative aspects, as they were considered the most emblematic of the PE subsistence criteria.

A total of 43 submissions were collected from 12 October 2011 to 29 February 2012.

The OECD, in view of the work carried out by the subgroup of Working Party 1 on Tax Conventions and Related Matters of the Committee on Fiscal Affairs, examined the issues related to the interpretation and application of the Article 5 and accepted only some of them.

The result was the publication, on 9 October 2012, of a second draft discussion, the Revised Discussion Draft (OECD, 2012)[76]. In this regard, until 31 January 2013, only suggestions of a formal nature could be proposed with the aim of approving the final text of the Commentary in view of the updates planned for 2014 to the Model Convention. The main changes proposed by the OECD, based on the analysis of some 30 suggestions

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[75] OECD, *OECD Model Tax Convention: Interpretation and Application of Article 5 (Permanent Establishment)*, 12 October 2011.

[76] OECD, *OECD Model Tax Convention: Revised Proposals Concerning the Interpretation and Application of Article 5 (Permanent Establishment)*, 19 October 2012.

to the Revised Discussion Draft, will be analyzed below (Nouel, 2011; IBFD, 2012; Valente, Vinciguerra, 2013)[77]:

- Concept of *"at disposal of*"[78]. According to paragraphs 4 to 4.2. of the Convention[79] the presence of a material Permanent Establishment, (Article 5) implies an essential condition, i.e. the presence of a place of business "*at disposal of*" the person in the foreign Contracting State, for the conduct of the business activity.

  However, doubts and concerns have been expressed by the entrusted Committees about the uncertainty of the concept of 'at the disposal' which requires at a minimum, a non-exclusive list of criteria as to what constitutes *"at the disposal"*[80].

  In this regard, the proposed amendment to the Commentary's paragraph 4.2, concerns the need to demonstrate the existence of an «*effective power to use that location as well as the extent of the presence of the enterprise at that location and the activities that it performs there*».

  According to the OECD, what's important is not to confuse the concept of "*at disposal of"* with the concept of "*at direction of*"[81]; indeed, the civil liability arising out of a sub-supply or service agreement would not create the prerequisites for identifying a material permanent presence, since the criterion of a permanent physical presence is lacking in order to be able to define a material PE as such.

- Permanent establishment and income from real estate[82]. Income from immovable property or agricultural activities is governed by Article 6 of the OECD Model, which states in paragraph 1 that the income is taxable in the State where the property is situated. The Working Party did not raise any relevant concerns as to whether a farm may constitute a PE within the meaning of Article 5 of the OECD Model.

  Income from a farm or forestry business is taxed in the Contracting State where such property is situated; if the entrepreneur is resident for tax purposes in another

[77] NOUEL, L., *OECD, the New Article 7 of the OECD Model Tax Convention: The End of The Road?* in *Bulletin for International Taxation*, 2011, Vol. 65, No.1; IBFD, *Interpretation and Application of Article 5 (Permanent Establishment) of the OECD Model Tax Convention. Response from IBFD Research Staff*, Amsterdam, 2012; VALENTE P., VINCIGUERRA L., *Stabile Organizzazione occulta.* IPSOA, 2013, Wolters Kluwer, Milano, pp. 68-75.

[78] OECD, *Model Tax Convention: Revised Proposals Concerning the Interpretation and Application of Article 5 (Permanent Establishment)*, Paris – Cedex, 2012, pp. 5 – 8.

[79] The paragraphs mentioned in the text correspond to the para. 10 through 12 of the OECD MTC Commentary, before they have been renumbered in 2017. See, in this regard, the OECD 2019 Commentary, C-5 para. 10 – 12 which referred to the "HISTORY" of the changes.

[80] See OECD, *OECD MTC: Revised Proposals…*, p. 5.

[81] See OECD, *OECD MTC: Revised Proposals…*, p. 6. See also OECD, *Commentary*, 2019, Art. 5, from paragraph 4 (58) to paragraph 12.

[82] See OECD, *OECD MTC; Revised Proposals…*p. 8

Contracting State, the income will also be taxable in that State. To clarify the point questioned by some countries, the suggested new paragraph provides that «*determination of whether or not an enterprise of a Contracting State has a permanent establishment in the other Contracting State must be made independently of the determination of which provisions of the Convention apply to the profits derived by that enterprise*».

- Home office as PE. The Working Party proposed to add in the Commentary paragraphs 4.8 and 4.9 in the Art. 5, after the new paragraph 4.7.[83]. The proposed new paragraphs intended to clarify that an employee's home may be considered to be *"at the disposal"* of the business if it is used continuously and with a certain regularity to carry on the business activity. The home is covered by the PE definition if the company has expressly requested the employee to use it for work.

- Time requirement for the existence of a PE. On the issue of the duration of a PE, the OECD Model does not provide for a minimum time threshold to decree or exclude a PE.

  The Working Party itself found numerous difficulties, in this regard, in the case of repeated business activities of short duration.

  The proposed new paragraphs 6.1. and 6.2. stemmed from various examples to those described in paragraph 6 of the previous Discussion Draft; they are exceptions to the general practice between two Contracting States, which in cases where the commercial activity lasts for less than 6 months cannot be considered a PE.

  The example described in the proposed new paragraph 6.1. refers to a commercial activity that takes place for periods of less than 6 months, but for several consecutive years. Since this is the particular nature of the business, even for short but interconnected periods of the year, it can be declared to be a PE.

  The example in the next paragraph describes an activity carried out exclusively in one country by a person resident in a different country. It concerns a catering service provided by an entity, at a house owned by its parents, to a television crew engaged in the filming of a documentary. The presence of a PE can be declared as the commercial activity is the only one that is carried on in the country even though for a duration of less than 6 months.

[83] See OECD, *OECD Model Tax Convention: Revised Proposals…*, pp. 9-10.

However, for the OECD, the duration of the activity in the source-state will remain an open clause that depends on the nature of the business and cannot refer to a specific time parameter in order to be able to declare or not the presence of a PE[84].

- Presence of personnel in another country. The Revised Discussion Draft examines the circumstances in which the presence of personnel of an MNE in another State may constitute a PE. Paragraph 37 of the Commentary specifies that the placement of a part of personnel in a State different from the State of residence does not immediately constitute a material PE. The reasons for this clarification lie in the fact that the activity carried on by this group in another company, that is part of the principal, would coincide with the activity carried on by the other company.
- Meaning of *«to conclude contracts in the name of the enterprise»*. The OECD Model recognizes the case of the general contractor who delegates the performance of part or all of the commissioned work to one or more subcontractors, although he or she remains civilly liable.
  The proposed addition to the Commentary of paragraph 10.1. aims to clarify that if the case of a contractor arises, it is possible to refer of PE if the contractor has a fixed place of business at which the subcontractor can perform the work.
  The suggested amendment to paragraph 19 of the Commentary reiterates that the time spent by the subcontractors in carrying on the activities entrusted by the contractor enterprise should be considered as if it were the time spent by the contractor enterprise. The fixed place of business, i.e. the construction site, must be considered to be *"at the disposal of the general contractor"* for the entire period spent by the subcontractor or multiple subcontractors.

More in general, the Working Party has put on the table the main issues emerged from the interpretation and application of the OECD MTC version 1977 and its Commentary, also on the basis of the cases law coming from the States' Courts, presenting a number of proposals for amendments concerning Art. 5 (from paragraph 1 to 42.10. of the consolidated version of Commentary) for the update in 2014.

However, this approach would have been short-lived, due to the rise of a fundamental issue: that of the "Base Erosion Profit Shifting".

[84] See more in dept OECD, *OECD Model Tax Convention: Revised Proposals…*, pp. 12 – 15.

In other words, while States, scholars and practitioners were struggling to find the most suitable solutions to define a PE concept as shared and effective as possible, in order to facilitate the identification of the source of income and thus recognize the "*right to taxation*" according to the "*source principle*" so to overcome the issue of "*double taxation*", on the other hand, an increasingly need to remove the tax arrangements that produced and extended the areas of "double non-taxation" came up (Atanazov, 2017; Avi-Yonah, 2019; Herzfeld, 2020; Oats, 2021, Weisser, 2020)[85].

The BEPS Project was aimed at countering this phenomenon, with significant implications for the PE concept (Action 7) and it is now worth talking about.

2.2. The OECD BEPS Action Plan 2013.

Contrary to what some believe (Cobham, 2016)[86], the BEPS Project background is not only the result of the failure of the long debate, within the OECD, aimed at improving the various definitions contained in the Model Tax Convention.

Nor it is the consequence of the century-old dispute between the "*residence principle*" supported by the advanced economies, and the "*source principle*", advocated by the developing countries (Ashfaq Ahmed, 2020) [87], for the equal and just attribution of the taxable income to one or other Contracting State, which adequate their tax policy to the OECD MTC so far (Appendix)[88].

The instances that constitute the background of BEPS come from further away (Avi-Yona, Xu, 2017; Wright, Zucman, 2018)[89].

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[85] ATANAZOV A., *Permanent Establishment 2.0 - Is It Time for an Update?* Luxembourg, 2017, in *http://dx.doi.org/10.2139/ssrn.3017892*, pp. 8 – 16; AVI-YONAH R.S., *Advanced Introduction to International Tax Law*, Northampton, MA, U.S.A., 2019, pp. 67 – 73; HERZFELD M., *International Taxation in a Nutshell,* St. Paul, MN, U.S.A., pp. 85, 161; OATS L., *Principles of International Taxation*, London, 2021, p. 228, WEISSER A., *International Taxation of Cloud Computing: Permanent Establishment, Treaty Characterization, and Transfer Pricing,* Lausanne, 2020, pp. 39 – 83.

[86] In August 2016, the Tax Justice Network's Alex Cobham described the OECD's MLI as a failure due to the opt–outs and watering–down of individual BEPS Actions. In December 2016, Cobham highlighted one of the "key anti–BEPS Actions", full public *country–by–country–reporting* ("CbCr"), had been dropped due to lobbying by the U.S. multinationals.

[87] ASHFAQ AHMED M., *United Nations Model Tax Convention Article 5: The Predatory Ploy – A Neo-Marxist Mapping of the Permanent Establishment*, in *Manchester Journal of International Economic Law*, 2020, Volume 17, Issue 2: pp. 186-217.

[88] See, *infra*, the Appendix, Figures 1 through 4 which show the Development of Worldwide Tax Treaty Network from 1950 up to 2018.

[89] AVI-YONAH R.S., XU H., *Evaluating BEPS*, in *Erasmus Law Review*, Vol. 10, No. 1, 2017, *in https://ssrn.com/abstract=3026297*; WRIGHT T., ZUCMAN G., *The Exorbitant Tax Privilege*, Working Paper 24983, NBER, Cambridge, MA, U.S.A., 2018, in *http://www.nber.org/papers/w24983.*

The first factor is certainly the financial crisis that has characterized the US market since the beginning of the last century (Enron, 2001; Lehman Brothers, 2008), causing – because of globalization – a crisis on the market for goods and services, with the creation of "new poors" even in the advanced economies. This have led Governments to adopt "Austerity" policies (Alesina et al, 2019)[90] and to find urgent resource needs to cope with recession (Avi-Yonah, Xu, 2017) [91].

A second factor is the official entry, in the world economic scenario (WTO), of two political giants (China, 2001; Russia, 2012), that have extended, with other countries (so-called "BRICS") the percentage of presence on the global market (IMF, 2009) [92] and qualitatively enlarged the group of the MNEs (e.g. HBSC, Huawei, Gazprom) able to use the same technical expedients of tax planning already used by their Western counterparts (e.g. Apple, Microsoft), to minimize their tax burden (Appendix)[93].

The third factor is the spread of e-Commerce and Digital economy, which has made outdated concepts and rules so laboriously elaborated, modified and finally agreed on "*transfer pricing*", "*treaty shopping*" and, of course, of "permanent establishment", easily avoided by MNEs, so much so as to cause an annual loss of revenue on the so-called "*active income*", jointly estimated by the OECD and the G20 in 100 - 240 billion dollars (OECD, 2015; Bundgaard, Kjærsgaard, 2020)[94].

These factors are expressly mentioned in the Action Plan of 2013 ("Introduction" and "Background"), starting from the globalization that – according to the OECD document – has determined, along with the free movement of capital and labor also "*the shift of*

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[90]ALESINA A, FAVERO C., GIAVAZZI F., *Austerity: When It Works and When It Doesn't*, Princeton, NJ, U.S.A., 2019, pp. 28- 42.

[91] See AVI-YONAH R.S., XU H., *Evaluating BEPS*, already quoted, p. 1.

[92] According to the IMF, *BRICs Drive Global Economic Recovery*, published on July 22, 2009 *(https://www.imf.org/en/News/Articles/2015/09/28/04/53/sorea072209a),* at that time, the so-called "BRICS" countries (Brazil, Russia, India, China, officially including South Africa since 2010), with 40 percent of the world's population spread out over three continents, already account for 25 percent of global GDP, even though China detained the largest part of the BRICS GDP and the biggest presence in the world trade.

[93] See, *infra*, Appendix, Figures 5 and 6, respectively reflecting the Revenue Effects of the OECD/G20 Inclusive Framework Agreement, Pillars 1 and 2 (*Percent of current global income tax*) and the Disaggregation of Total Profit of Multinational Corporations in Trillions of US Dollars, based on IMF, *Fiscal Monitor – Coordinating Taxation Across Borders*, Washington D.C., April 2022, pp. 25 – 46.

[94]OECD, *Addressing the Tax Challenges of the Digital Economy, Action 1 - 2015 Final Report*, 2015, available in *https://read.oecd-ilibrary.org/taxation/addressing-the-tax-challenges-of-the-digital-economy-action-1-2015-final-report_9789264241046-en.* See also: OECD/G20, *International collaboration to end tax avoidance*, in *https://www.oecd.org/tax/beps/* and BUNDGAARD J., KJÆRSGAARD F., *Taxable Presence and Highly Digitalized Business Models, Tax Notes International*, 2020, 97(9), 977-1006, in *https://corit-advisory.com/wp-content/uploads/2020/04/Taxable-Presence-and-Highly-Digitalized-Business-Models.pdf.*

manufacturing bases from high-cost to low-cost locations" and a profound impact on the "*countries' corporate income tax regimes*"[95].

The same phenomenon has also favored the growth of MNEs, both in number and in organizational strategies. The OECD, in fact, while acknowledging that "*Multi-national Enterprises (MNEs) represent a large proportion of global GDP*" and "*a growing proportion of overall trade*", also highlights that "*Globalization has resulted in a shift from country-specific operating models to global models based on matrix management organizations and integrated supply chains*" and that "*These developments have opened up opportunities for MNEs to greatly minimize their tax burden*" [96].

All that – according to the OECD – "*has led to a tense situation in which citizens have become more sensitive to tax fairness issues. It has become a critical issue for all parties*"[97].

Finally, the third factor of concern – the spread of Digital Economy – brought the OECD to take note that "*The digital economy is characterized by an unparalleled reliance on intangible assets, the massive use of data (notably personal data), the widespread adoption of multi-sided business models capturing value from externalities generated by free products, and the difficulty of determining the jurisdiction in which value creation occurs. This raises fundamental questions as to how enterprises in the digital economy add value and make their profits, and how the digital economy relates to the concepts of source and residence or the characterization of income for tax purposes*"[98].

In this regard, it has observed (Cooper, 2014)[99] that the BEPS Action Plan focuses on the fact that many of Tax Regimes are directed at the tax position of residents and it proposes inserting new clauses on the OECD MTC which would preserve any regime (whether

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[95] See *OECD Action Plan on BEPS*, 2013, p. 7. BRAUNER Y., *Treaties in the Aftermath of BEPS,* in *Brooklyn Journal of International Law*, 2016, Vol. 41, Issue 3, pp. 982 – 985 considered the hypothesis that the International Tax Regime resulted by the OECD MTC is going to a disintegration and that's because of the general criticism of the OECD and its dominance over the international tax regime sharpened as some of the developing countries that are not members of the OECD began emerging and establishing both economic and political dominance. Furthermore, and most notably, the countries of Brazil, Russia, India, China and the Republic of South Africa ("BRICS"), led by India and China, gained strong positions in the global market and began demanding a corresponding voice in the policymaking process.

[96] OECD, *ibidem*, p. 8.

[97] OECD, *ibidem*, p. 8.

[98] OECD, *ibidem*, p. 10. See, more in depth the OECD/ G20 *Base Erosion and Profit Shifting Project Addressing the Tax Challenges of the Digital Economy, Action 1 2015 Final Report.*

[99] COOPER G.S., *Preventing Tax Treaty Abuse*, in *United Nations Papers on Selected Topics* in '*Protecting Tax Base of Developing Countries*', 2014, p. 50 in *https://www.un.org/esa/ffd/wp-content/uploads/2014/09/20140923_Paper_PreventingTaxTreatyAbuse.pdf*.

viewed as an anti-abuse measure or not) directed at the taxation of residents, with a few exceptions[100].

On this basis and taking into account the G20 request to develop an action plan to address BEPS issues in a coordinated and comprehensive manner the Action Plan:

(i) identifies actions needed to address BEPS;

(ii) sets deadlines to implement these actions;

(iii) identifies the resources needed and the methodology to implement these actions with the purpose to effectively prevent double non-taxation, as well as cases of no or low taxation associated with practices that artificially segregate taxable income from the activities that generate it (Russo, 2017)[101].

The list of Actions, thus, reads as follows:

- Action 1 _ *Address the tax challenges of the digital economy*;
- Action 2 _ *Neutralize the effects of hybrid mismatch arrangements*;
- Action 3 _ *Strengthen CFC rules*;
- Action 4 _ *Limit base erosion via interest deductions and other financial payments*;
- Action 5_*Counter harmful tax practices more effectively, taking into account transparency and substance*;
- Action 6 _*Prevent treaty abuse* (The definition of permanent establishment (PE) must be updated to prevent abuses);
- Action 7_*Prevent the artificial avoidance of PE status*;
- Action 8_*Intangibles*;
- Action 9_*Risks and capital*;
- Action 10_*Other high-risk transactions*;
- Action 11_*Establish methodologies to collect and analyze data on BEPS and the actions to address it*;
- Action 12_*Require taxpayers to disclose their aggressive tax planning arrangements*;
- Action 13_*Re-examine transfer pricing documentation*;
- Action 14_*Make dispute resolution mechanism more effective*;

[100] See, for instance, US Model Convention, above n. 24, art 1(4) and (5) quoted by COOPER G.S., *Preventing Tax Treaty Abuse…*, footnotes 3 and 32 and further details referred to the Articles 5 (Permanent Establishment), 7 (Business Profit) and 22 (Limitation on Benefits) of the 2016 U.S. Model Income Tax Convention in HERZFELD M., *International Taxation in a Nutshell*, St. Paul, MN, U.S.A., 2020, pp. 161 – 166.

[101] OECD, *Action Plan…*, p. 11; RUSSO R., *The BEPS Project: A new era in international taxation?* in *Nomos & Khaos*, 2017, *Nomisma Economic & Strategic Outlook*.

- Action 15_*Develop a multilateral instrument*[102].

Although the Plan includes 15 separate actions, they should be read in a comprehensive approach.

This is evident from the listing of some of them (e.g.: *ACTIONS 8, 9, 10: Assure that transfer pricing outcomes are in line with value creation*)[103]. But it becomes more and more clear when the interpreter deepens their contents.

With particular reference to the PEs, the OECD Plan is not limited to Action 7, in which title and purpose are expressly devoted to countering the artificial use of their "*status*".

The title of Action 7 should be read in pair with that of Action 6 which, in indicating its scope of preventing the abuse of treaties for avoidance purposes, immediately makes it clear the real object and goal of the program it intends to implement, e.g. "*The definition of permanent establishment (PE) must be updated to prevent abuses*"[104].

There is even more: the Action Plan is not fully understood if it is not examined in pair with the Inclusive Framework on BEPS, launched in 2016 in agreement with the G20, to combat evasion and avoidance practiced by MNEs through BEPS tools (Christian, 2016; Appendix)[105], and with the Multilateral Convention to implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting, which lists nowadays 100 countries[106].

It is in this context that the so-called "Two Pillars Approach" has been elaborated:

- Pillar One, related to Action 1 (*Addressing the fiscal challenges of the digital economy*). It applies to large multinationals that will redistribute certain amounts (A and B) of taxable income to market jurisdictions, resulting in a change in the effective tax rate and

[102] OECD, *ibidem*, pp. 14 – 26. For a preliminary evaluation on the BEPS Project, with particular reference to the Environment that Strongly Motivates BEPS Behavior-Systemic Issues and Developments Occurring over Past Decades and to its Future, see KADET J., *Taxation of trans-pacific transactions (T-536). Overview of the practice of International Taxation*, Washington D.C., U.S.A., 2017, pp. 165 – 184.
[103] OECD, *ibidem*, p. 20.
[104] OECD, *ibidem*, p. 19.
[105] CHRISTIANS A., *BEPS and the New International Tax Order,* 2016, Brigham Young University Law Review, in *https://digitalcommons.law.byu.edu/lawreview/vol2016/iss6/4.* The OECD/G20 Inclusive Framework on BEPS counts nowadays more than 140 countries: see *OECD/G20 Inclusive Framework on BEPS Progress report July 2020 – September 2021*, p. 28; see also, *infra*, Appendix, Table 2, reproducing the list of Members of the OECD/G20 Inclusive Framework on BEPS, updated November 2021.
[106] See, for the updated text, *https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf.* See also, *infra*, for details concerning Signatories and Parties, Appendix, Table 3. With particular reference to Art. 13 of the MLI _ *Artificial Avoidance of Permanent Establishment Status through the Specific Activity Exemptions*, see, more in depth, ALMEIDA L., TOLEDANO P., *Understanding how the various definitions of Permanent Establishment can limit the taxation ability of resource - rich source countries*, in *Columbia Law Review*, March 2018, pp. 7 – 12.

cash tax obligations, and an impact on current transfer pricing arrangements (IMF, 2022)[107];

- Pillar Two, related to Action 13. (*Re-examine transfer pricing documentation*). It aims to ensure that income is taxed at an appropriate rate and has a number of complicated mechanisms to ensure this tax is paid (Bunn, 2020; Brokelind, 2021)[108].

Bearing in mind this "comprehensive approach" it turns out easier to frame the BEPS Action 7, concerning the attempt to prevent the artificial avoidance of PE status (Jimenez, 2014, Schmitz-Filho, 2019)[109].

2.3. The OECD BEPS Action 7 and the changes to the definition of Permanent Establishment.

Within the framework of the BEPS Action Plan, the name of Action 7 – *Prevent the Artificial Avoidance of PE status* – intends to express much more than, at a first glance, one can stem from the formula "*PE status*" (it's a typical case of the Latin Brocard: "*minus dixit lex quam voluit*").

In fact, it is true that the Action 7 section refers to the use of "*commissionaire arrangements*"[110] and to "*specific activity exemptions*".

But the next content highlights as a "*major issue*" that of the "*transfer pricing*" and the "*enforcement of the arm's length principle*", making it immediately clear that Action 7 is not aimed at actually discussing of "Permanent Establishment" (Art. 5 OECD MTC) and of "Transfer Pricing" (Art. 9 OECD MTC, BEPS Actions 8, 9, 10).

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[107] See, more in depth, IMF, *Fiscal Monitor – Coordinating Taxation Across Borders*, Washington D.C., April 2022, whose figures are reproduced in the Appendix of this work, *infra*, Figure 1 and 2.

[108] See OECD/G20 *Base Erosion and Profit Shifting Project Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalization of the Economy*, October 2021, pp. 13 – 16; BUNN D., *Reports on Pillar One and Pillar Two Blueprints*, Washington D.C., 2020, in *https://files.taxfoundation.org/20201211093047/Tax-Foundation-Response-to-OECD-Public-Consultation-Document.Reports-on-the-Pillar-One-and-Pillar-Two-Blueprints.pdf*; BROKELIND C., *An Overview of Legal Issues Arising from the Implementation in the European Union of the OECD Pillar One and Pillar Two Blueprint*, in *Bulletin for International Taxation,* 2021, Vol. 75, Issue 5, pp. 212 – 219.

[109] JIMENEZ A. M., *Preventing the Artificial Avoidance of PE Status*, Càdiz, 2014, pp. 4 – 77, in *https://www.un.org>20140923_Paper_PE_Status*; SCHMITZ-FILHO R.S., *Towards a Broader Concept of Permanent Establishment: a Study in Light of the Digitalization of the Economy and the BEPS Era*, Lisbon, 2019, in *https://www.semanticscholar.org/paper/Towards-a-broader-concept-of-permanent-%3A-a-study-in-Filho-Sergio/1eeeda4add71147a435a599c7045b0bb2fed81d1.*

[110] See, supra, Chapter 1, subpara. 1.5.2.1.

The object of Action 7, as well as that of Action 6 – which, as mentioned, should be examined in pair with Action 7 – is to modify the OECD MTC in order not to lend itself to interpretations aimed at increasing the field of the "Base Erosion and Profit Shifting", improperly using this or that definition offered by the Model itself.

This is because the evolution of the economic scenario related to the globalization has induced a change in the MNEs' business conduct, since such entities avail themselves of procedures and interpretations that have facilitated the discovery of new tools for tax avoidance. In other words: international tax rules should prevent a situation where the evolution of business reflects only the intention of shifting the tax burden from a country to another, on the basis of what is the most preferable tax regime.

To achieve this goal, the Action 7 "*Prevent the Artificial Avoidance of PE Status*" aims at revising the definition and the scope of PE status, as provided in the Article 5 of the OECD Model Tax Convention.

The issue has been pointed out again in the OECD Final Reports concerning Action 7, released in 2015, based on two discussion drafts containing comments and observations addressed to all stakeholders to amend the existing treaty rules on Permanent establishments[111].

In the 15 May 2015 Report specific "artificial tools" were identified in the PE definition, as provided by Art. 5 of the OECD MTC:

1. *Artificial avoidance of PE status through commissionaire arrangements and other similar strategies*. According to the Report, changes were needed to the wording of Art. 5(5) and 5(6) of the OECD Model in order to address commissionaire structures and similar arrangements. As a matter of policy, where the activities that an intermediary carries on in a country are intended to result in the regular conclusion of contracts to be performed by a foreign enterprise, that enterprise should be considered to have a sufficient "*taxable nexus*" in that country unless the intermediary is performing these activities in the course of an independent business. The discussion draft put forward four alternative options (Options A, B, C and D) for changes to Art. 5(5) and 5(6) that were intended to reflect that policy without

[111] OECD, *Public discussion draft – BEPS Action 7: Preventing the Artificial Avoidance of Permanent Establishment status*, *13 October 2014 - 9 January 2015*, Paris-Cedex, 2015; OECD, *Revised discussion draft – BEPS Action 7: Preventing the Artificial Avoidance of Permanent Establishment status, 15 May 2015 - 12 July 2015*, Paris-Cedex, 15 May 2015.

allowing the types of avoidance strategies that have taken place under the current wording of the Article.

The Working Party concluded that Option B was the preferable one[112] and that the concept of "*associated enterprises*" used in 5 Art. 5(6) should be replaced by a narrower concept, as well as Art. 5(6) should not automatically exclude an unrelated agent acting exclusively for one enterprise. In the end, a proposal was made for replacing Art. 5(5) and Art. 5(6) of the OECD Model and the Commentary (Eisenbeiss, 2016)[113].

2. *Artificial avoidance of PE status through the specific activity exemptions.* Some aspects of Art. 5(4) of the OECD Model Tax Convention, according to which a permanent establishment is deemed not to exist where a place of business is used solely for activities that are listed in that paragraph, give rise to BEPS concerns.

   First, some consider that the fact that some parts of Art. 5(4) do not expressly refer to preparatory or auxiliary activities does not seem to conform with what they consider to be the original purpose of the paragraph, *i.e.* to cover only preparatory or auxiliary activities.

   Second, concerns have been expressed with respect to the application of paragraph 4 where activities are fragmented between related parties.

   Such situations could be addressed by a rule that would take into account not only the activities carried on by the same enterprise at different places but also the activities carried on by associated enterprises at different places or at the same place[114].

3. *Splitting-up of contracts.* BEPS concerns related to the splitting-up of contracts in order to circumvent the restrictions imposed by paragraph 3 of Article 5 could be addressed either by an "automatic" rule that would take account of any activities

[112] The "Option B" reads as follows: "*Add a reference to contracts for the provision of property or services by the enterprise; replace "conclude contracts" by "concludes contracts, or negotiates the material elements of contracts"; strengthen the requirement of "independence"*. See OECD, *Public Discussion Draft BEPS ACTION 7: Preventing the artificial avoidance of Pe status*, 31 October 2014 – 9 January 2015, Paris-Cedex, 31 October 2014, p. 13.

[113] See OECD, *Revised discussion draft BEPS ACTION 7: Preventing the artificial avoidance of PE status 15 May 2015 – 12 June 2015*, Paris-Cedex, 15 May 2015, pp. 4 – 5. EISENBEISS J., *BEPS Action 7: Evaluation of the Agency Permanent Establishment*, 2016, in *Intertax*, Volume 44, Issue 6/7, pp. 481 – 502, with particular reference to Agency PE, observes that marking the threshold for source-state taxing rights, the PE has been at the center of an entrenched debate since the concept's emergence in the nineteenth century. Thus, working on the Agency PE, the OECD soon found itself caught between a rock and a hard place. With strong national interest for a high threshold on the one side and the increasing need to rebalance taxing rights due to globalization and the emergence of modern business models on the other side. Moreover, with the Agency PE in the spotlight, attention will inevitably be directed to the attribution of profits, an issue neglected in the BEPS Project.

[114] See OECD *Public Discussion Draft BEPS ACTION 7…,* Paris-Cedex, 15 May 2015, p. 7.

performed by associated enterprises or by the addition of a new example to the Commentary on the general anti-abuse rule (*i.e.* the "Principal Purposes Test" rule) proposed as a result of the work on Action 6.

The splitting of contracts to abuse the exception in Article 5(3), i.e. PE from construction, PE from installation project, etc., was later discussed in paragraph 18 of the OECD Commentary referred to Article 5.

In this regard, the time threshold of 12 months has created many interpretative complaints (OECD, 2015; Annex)[115].

Three years after the publication of the aforementioned Report and the edition of the current version of the OECD Tax Convention Model (OECD, 2017)[116], the Organization published its "*Additional Guidance on Attribution of Profits to Permanent Establishments, BEPS Action 7*", reaffirming its strategic intent: to bring to the "Permanent Establishment" concept, as already defined in the Model Tax Convention, the amendments deemed necessary to determine the correct tax base of the profits produced in a given country by a foreign MNE, through a PE, to whom the right to tax this tax base should be attributed and for which part[117].

In fact, according to the OECD, the definition of Permanent establishment (PE) included in tax treaties "*is crucial in determining whether a non-resident enterprise must pay income tax in another State*". This is because the PE definition has been systematically used over time in certain common tax avoidance strategies.

In particular, the Guidance stressed the fact that "*Depending on the circumstances, activities previously considered to be merely preparatory or auxiliary in nature may nowadays correspond to core business activities. In order to ensure that profits derived from core activities performed in a country can be taxed in that country, Article 5(4) is modified to ensure that each of the exceptions included therein is restricted to activities that are otherwise of a 'preparatory or auxiliary' character. (...) BEPS concerns related to Art. 5(4) also arise from what is typically referred to as the 'fragmentation of activities'*

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[115] See OECD *Revised discussion draft BEPS ACTION 7: Preventing the artificial avoidance of PE status 15 May 2015 – 12 June 2015*, Paris-Cedex, 15 May 2015, pp. 4 – 6 and, *infra,* the Annex, Table 4, reflecting Construction Permanent Establishment Threshold in over 1800 Tax Treaties concluded between April 1997 and January 2013.

[116] The changes are now included in the OECD Model Tax Convention on Income and on Capital - Full version (as it read on 21 November 2017) - published, together with the Commentary, in 2019.

[117] See OECD, *Additional Guidance on Attribution of Profits to Permanent Establishments, BEPS Action 7*, Paris-Cedex, March 2018, p. 7.

The anti-fragmentation rule [contained in the new version of the OECD MTC] will address these BEPS concerns”[118].

To prevent this kind of risk, the Art. 5 (4.1.) applies in two cases:

- first, it applies where the non-resident enterprise or a closely related enterprise already has a PE in the source-country, and the activities in question constitute complementary functions that are part of a cohesive business operation.

  The profits attributed to the PEs and subject to source taxation are the profits derived from the combined activities constituting complementary functions that are part of a cohesive business operation considering the profits each one of them would have derived if they were a separate and independent enterprise performing its corresponding activities, taking into account in particular the potential effect on those profits of the level of integration of these activities;
- secondly, it applies in a case where there is no pre-existing PE but the combination of activities in the source country by the non-resident enterprise and closely related non-resident enterprises results in a cohesive business operation that is not merely preparatory or auxiliary in nature.

  The profits attributable to each PE so arising are those that would have been derived from the profits made by each activity of the cohesive business operation as carried on by the PE if it were a separate and independent enterprise performing the corresponding activities, taking into account, in particular, the potential effect on those profits of the level of integration of these activities[119].

As far as the issue of “Splitting-up of contracts” is concern, the Guidance recalls the amendments brought to the Art. 5(5) and observes that “*Once it is determined that a PE exists under Article 5(5), one of the effects of paragraph 5 will typically be that the rights and obligations resulting from the contracts to which Article 5(5) refers will be properly allocated to the Permanent establishment*”[120].

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[118] See OECD, *Additional Guidance…*, p. 9, related to the ‘Attribution of profits to permanent establishments resulting from changes to Article 5(4) and the Commentary’, which reads as follows: “*The anti-fragmentation rule recommended in the Report on Action 7 (at p. 39) is contained in the new paragraph 4.1 of Article 5. It prevents paragraph 4 from providing an exception from PE status for activities that might be viewed in isolation as preparatory or auxiliary in nature but that constitute part of a larger set of business activities conducted in the source country by the enterprise (whether alone or with a closely related enterprise) if the combined activities “constitute complementary functions that are part of a cohesive business operation*”.

[119] See again OECD, *Additional Guidance…*, p. 9.

[120] See more in depth, also for the exceptions acknowledged and examples supporting to this conclusion, OECD, *Additional Guidance…*, pp. 13 – 16, related to ‘Attribution of profits to permanent establishments resulting from changes to the Article 5(5) and 5(6) and the Commentary’.

The fact is that the OECD seems to focus its action against elusive phenomena and exceptions to the PE concept, as it is inferable from the text of the Art. 5 of the Model Tax Convention and in its Commentary.
However, as it has been acutely observed (Garbarino, 2019)[121], the Art. 5 of the Model Tax Convention is only concerned to offer the notion of the “Permanent Establishment”, specifying the ordinary scope of its business, but does not care to establish – not even through the refinement of such a concept – to whom should be attributed the profits of that business and which of the Contracting States has the right to proceed to taxation.
The criteria for the allocation of profits – and of the consequent income tax – are instead defined in the Art. 7 of the Model, which explicitly mentions “Permanent Establishment” in para. 3.
In fact, the “Guidance” contains numerous references to the Art. 7 of the Model[122] trying to deepen the criteria of allocation of profits (and therefore those of 'right to tax') to one or the other contracting State, depending on whether one follows the fundamental principles of “source-country” or “residence-country”.
In other words, focusing the attention on the sphere of definition (Art. 5) rather than on that of the allocation of profits could represent not only an error of perspective, but also one of the main weaknesses of the BEPS project (Avi-Yonah, 2019) [123], which reflects the “*state of the art*” of the fundamental principles of the International Tax Law (residence-principle, source-principle, benefits principle, single-tax principle).
Other scholars (Barbier, 2016)[124] point out the already mentioned need to consider Action 7 like the other facet of a strategy that, along with the Action 6, is aimed at combating the

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[121]GARBARINO C., *Doing Business through a Permanent Establishment (PE)* in *Taxation of Bilateral Investments – Tax Treaties after BEPS*, Northampton, MA, 2019, pp. 7 – 9 quoting the case ‘Spain, Tribunal Economico Administrativo Central, 03852/2004, 23 November 2006’, which supports the principle “*until an enterprise of one State has a PE in another State, it should not properly be regarded as participating in the economic life of that other State to such an extent that the other State should have taxing rights on its profits’, adding that the right to tax of the State where the PE is situated does not extend to profits that an enterprise may derive from that State but that are not attributable to the PE*; See also, in the same sense, GARBARINO C., *Permanent Establishment and the BEPS Project (Action 7): perspectives in evolution, in Intertax,* 2019, vol. 47 (4), pp. 365-370.
[122] See OECD, *Additional Guidance…*, pp. 7, 11 – 15, 18, 21.
[123] According to AVI-YONAH R.S., *Advanced Introduction to International Tax Law*, Northampton, MA, U.S.A., 2019, pp. 74 – 75, the main criticality of the BEPS Project is the fact that the traditional international taxation is still bound to the old principles (residence principle, source-principle, single tax principle) in order to avoid the double taxation issue rather than double “non-taxation” issue that seems to be instead, at the present, the major issue.
[124] BARBIER C., *The Permanent Establishment in a post BEPS world*, Tilburg, 2016, in *http://arno.uvt.nl› show*, pp. 57, 60-61.

development of Base Erosion Profit Shifting caused by actual "double non-taxation" policies resulting from the tax treaties.
In coherence with Action 6, which addresses the inappropriate granting of treaty benefits, the measures adopted in Action 7 should result in a re-establishing taxation in cross-border situations, where income has been untaxed or taxed at very low rates due to the unintentional treaty benefits MNEs made use of.
The amendments of paragraph 4 – 6 of the Art. 5, which include preparatory and auxiliary character of activities, rather than the anti-fragmentation rule or the provisions concerning the PE agency and commissionaire arrangements should be read as the attempt to favor an economic approach to the OECD MTC.
So, according to this interpretation, the most important aspect of the BEPS Action 7 is the provision on the artificial avoidance of the PE agency, even though MNEs might neutralize its impact by changing their structures or increasing the use of Limited Risk Distributors (LRDs)[125]. The use of an LRD will not lead to the recognition of a permanent establishment because in contrary to other commissionaire structures, the LRD will be the owner of the goods before the sales take place.
In practice, the results of broadening the PE-concept are expected to lead to a rise in the number of permanent establishments recognized. For companies this might lead to an increase in administrative burdens and more uncertainty about future tax positions, as economic reality is harder to control than contracts. As there might be room for interpretation on the exact level of involvement of the agent in the conclusion of contracts with customers, no guarantee exists that tax authorities of two states will come to the same result. Governments might therefore re-assess the business activities performed in a country and will recognize a PE more easily than before.
In the end, others (de Wilde, 2018)[126], considering the issue of digitalization, suggest that the tax policy responses in the area of direct taxation that are currently on the table at both the OECD and EU levels don't take into account enough that the digital economy cannot be seen in isolation from the rest of the economy; it is the overall economy that is becoming increasingly digitalized. In this regard, initiatives as BEPS Action 7 seem to

[125] A Limited Risk Distributor is a buy-sell distributor, which distributes products in its own name and for its own account for a principal company under an arrangement in which most risks are borne by the principal and only limited risks are borne by the LRD.
[126] DE WILDE M.F., *Comparing Tax Policy Responses for the Digitalizing Economy: Fold or All-in*, in *Intertax,* Volume 46, Issue 6/7 (2018) pp. 466 – 475.

bring little to the table other than market distortions, inequities, arbitrary taxation, tax cascading, legal uncertainties, and red tape.
The real question, therefore, seems to be whether the time has come to explore the opportunity to proceed to a genuine and comprehensive reform in the corporate taxation (de Wilde, 2021)[127].

2.4. The Anti-Abuse Rule for Permanent Establishments Situated in Third States (BEPS Action 6 referred to art. 29(8) of the OECD Model).

As mentioned above, the strategy for combating BEPS contained in Action 7 should be assessed along with Action 6, which is labelled "*Prevent treaty abuse*" and better indicated under the formula "*Develop model treaty provisions and recommendations regarding the design of domestic rules to prevent the granting of treaty benefits in inappropriate circumstances*".
However, it is in the clarification of the Action that the role of the PE emerges.
It reads, in fact: "*The definition of permanent establishment (PE) must be updated to prevent abuses*" [part in bold in the text]. "*In many countries, the interpretation of the treaty rules on agency-PE*" – the explanation follows – "*allows contracts for the sale of goods belonging to a foreign enterprise to be negotiated and concluded in a country by the sales force of a local subsidiary of that foreign enterprise without the profits from these sales being taxable to the same extent as they would be if the sales were made by distributor. In many cases, this has led enterprises to replace arrangements under which the local subsidiary traditionally acted as a distributor by* '*commissionaire arrangements*' *with a resulting shift of profits out of the country where the sales take place without a substantive change in the functions performed in that country. Similarly, MNEs may artificially 'fragment' their operations among multiple group entities to qualify for the exceptions to* '*PE status*' *for* '*preparatory and ancillary activities*'[128].
In Action 6, thus, the Plan anticipates themes (*"commissionaire arrangements*", "*agency-PE"* and "*ancillary - preparatory activities*") which are then developed in Action 7.
On the other hand, the question of using the PE definition as an instrument of abuse for elusive purposes returns to prominence in the OECD, both with regard to the Art. 10 of

[127] DE WILDE M.F., *Is There a Leak in the OECD's Global Minimum Tax Proposals (GLOBE, Pillar Two)?*, Rotterdam, 2021, in *https://kluwertaxblog.com/2021/03/01/is-there-a-leak-in-the-oecds-global-minimum-tax-proposals-globe-pillar-two/.*
[128] See OECD, *Action Plan on Base Erosion and Profit Shifting*, Paris-Cedex, 2013, p. 19.

the MLI[129] and with regard to Art. 29(8) of the Model Tax Convention (Lang, 2014; González - Barreda, 2018, Valderrama, 2020, Van West, 2020)[130].

The above issues are widely reflected in the voluminous Report, published by the OECD within the Inclusive Framework on BEPS (OECD/G20, 2022)[131], and dedicated to Action 6, whose conclusions reads as follows:

"*Treaty shopping is undesirable for several reasons, including:*

- *Treaty benefits negotiated between the parties to an agreement are economically extended to residents of a third jurisdiction in a way the parties did not intend. The principle of reciprocity is therefore breached and the balance of concessions that the parties make is altered;*
- *Income may escape taxation altogether or be subject to inadequate taxation in a way the parties did not intend; and*
- *The jurisdiction of residence of the ultimate income beneficiary has less incentive to enter into a tax agreement with the jurisdiction of source, because residents of the jurisdiction of residence can indirectly receive treaty benefits from the jurisdiction of source without the need for the jurisdiction of residence to provide reciprocal benefits*"[132].

The conclusions basically refer to the Art. 29(8) of the OECD Model Tax Convention that reads as follows (Entitlement to benefits)[133]:

"*8. a) Where:*

(i) an enterprise of a Contracting State derives income from the other Contracting State and the first-mentioned State treats such income as attributable to a Permanent Establishment of the enterprise situated in a third jurisdiction, and

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[129] Art. 10 MLI is entitled: "*Anti-abuse Rule for Permanent Establishments Situated in Third Jurisdictions*". MLI has been signed by 100 countries and entered into force in 74 countries, as of 10 November 2022, as it is shown, *infra*, Appendix, Table 3.

[130] LANG M., *BEPS Action 6: Introducing an Anti-abuse Rule in Tax Treaties*, in *Tax Notes International*, 2014, pp. 655 – 64; GONZÁLEZ – BARREDA, *A Historical Analysis of the BEPS Action Plan: Old Acquaintances, New Friends and the Need for a New Approach*, in *Intertax*, Volume 46, Issue 4 (2018) pp. 278 – 295; VALDERRAMA I. J. M., *BEPS Principal Purpose Test and Customary International Law*, in *Leiden Journal of International Law* (2020), 33, pp. 745–766; VAN WEST J. P., *The Anti-Abuse Rule for Permanent Establishments Situated in Third States. A legal Analysis of art. 29(8) of the OECD Model, 2020,* IBFD Amsterdam, pp. 97 – 109.

[131] OECD/G20, Inclusive Framework on BEPS, *Action 6: Prevention of Tax Treaty Abuse – Fourth Peer Review Report on Treaty Shopping*, Paris, 2022, pp. 1 – 317: see, in particular, Chapter 7_ *Background on the Action 6 Minimum Standard and Peer Review*.

[132] OECD/G20, Inclusive Framework on BEPS, *Action 6: Prevention…*, 2022, p. 29.

[133] LANG M., *BEPS Action 6: Introducing…*, p. 656, observe that the expression ''benefit under this Convention'' must refer to a benefit resulting from the treaty.

(ii) the profits attributable to that permanent establishment are exempt from tax in the first-mentioned State, the benefits of this Convention shall not apply to any item of income on which the tax in the third jurisdiction is less than the lower of [rate to be determined bilaterally] of the amount of that item of income and 60 per cent of the tax that would be imposed in the first-mentioned State on that item of income if that permanent establishment were situated in the first-mentioned State. In such a case any income to which the provisions of this paragraph apply shall remain taxable according to the domestic law of the other State, notwithstanding any other provisions of the Convention.

b) The preceding provisions of this paragraph shall not apply if the income derived from the other State emanates from, or is incidental to, the active conduct of a business carried on through the Permanent Establishment (other than the business of making, managing or simply holding investments for the enterprise's own account, unless these activities are banking, insurance or securities activities carried on by a bank, insurance enterprise or registered securities dealer, respectively)".

The minimum standard on treaty shopping requires jurisdictions to include two components in their tax agreements: an express statement on "non-taxation" (generally in the preamble) and one of three methods of addressing "treaty shopping": (i) Principal purpose test; (ii) Principal purpose test with either a simplified or detailed limitation on benefits provisions; and (iii) a detailed limitation-on-benefits (LOB) with anti-abuse measures to counteract conduit financing.

The minimum standard does not provide how these two components should be implemented (i.e. through the MLI or amending instruments). It recognizes, however, that these provisions need to be agreed bilaterally and that a jurisdiction will be required to implement the minimum standard when requested to do so by another member of the Inclusive Framework (OECD/G20, 2022)[134].

It thus appears in all its evidence that the numerous interventions made on the PE concept (Art. 5 (4-6); 7 (3); 29 (8), through BEPS Actions 6 and 7 are only the technical expedients for a counter-strategy aimed at countering its improper use to obtain in fact a result "*in a way the parties did not intend".*

[134] OECD/G20, Inclusive Framework on BEPS, *Action 6: Prevention…*, 2022, p. 30, paragraphs 94 - 95.

This counter-strategy is summarized in para. 9 of art. 28, added on 21 November 2017 by the Report entitled "The 2017 Update to the Model Tax Convention", adopted by the OECD Council on 21 November 2017, on the basis of another report Entitled "Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 - Final Report", endorsed by the G20 at the 2015 G20 Antalya Summit on 15-16 November 2015[135].

The paragraph reads as follows: "*Notwithstanding the other provisions of this Convention, a benefit under this Convention shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention*".

This is the formalization of the main method of addressing "*treaty shopping*": the "Principal Purpose Test" (Valderrama, 2020)[136].

In general, PPT comprises two elements, one subjective, the other objective.

The subjective component assigns the burden of proof to the tax administration. The corresponding model has the following formula: "*if it is reasonable to conclude, having regard to all relevant facts and circumstances that obtaining the benefit was one of the principal purposes of any arrangement or transaction that resulted Directly or indirectly in that benefit*".

The objective component instead attributes the burden of proof to the taxpayer, through the following formula: The objective component instead attributes the burden of proof to the taxpayer, through the following formula: "*if it is established* [by tax administration] *that granting that benefit in these circumstances would be in accordance to the object and purpose of the relevant Provisions of the Covered Tax Agreement*"[137] .

Through PPT, BEPS Action 6 aims at combating the possible aggressive tax planning of MNEs and the test dissemination is certainly a brake against the construction of a merely elusive corporate structures.

On the other hand, the contrast of such aggressive tax planning, supported by such a vast international consensus (OECD/G20) contributes to the development of fair and neutral

[135] See OECD MTC Commentary, 2019, History, para. 9, M-82 (p. 112).
[136] VALDERRAMA I. J. M., *BEPS Principal Purpose Test* ..., 2020, p. 746.
[137] See again, VALDERRAMA I. J. M., *BEPS Principal Purpose Test* ..., 2020, p. 746.

tax competition and to the pooling of more revenue for the States participating in both the OECD Model Tax Convention and MLI (Weber, 2017; Van West, 2020) [138].

2.5. The OECD MTC 2017 and Multilateral Instruments (MLI) Permanent Establishment definition as integrated by the results of the discussion.

As already seen, the OECD strategy to combat BEPS, as defined by Actions 6 and 7, intervenes on the PE concept in several articles of the MTC [Art. 5 (4-6); 7(3); 29 (8)] by transferring its content to the provisions of MLI Convention [Art. 7, 10, 13 and 14] (OECD MTC and Commentary, 2019; MLI Consolidated version 2022) [139].
Closing standard – also seen and commented on – is the anti-abuse one, contained in para. 9 of art. 28 of the MTC introduced on 21 November 2017, that introduces the so-called "Principal purpose test", whose mechanism has already been described[140].
In the view of the OECD-G20 Inclusive Framework, if implemented, these rules provide States with more flexibility to tackle tax evasion and avoidance including the possibility of denying a tax treaty benefit if it is clear that obtaining this benefit was one of the principal purposes of an arrangement or transaction (Almeida – Toledano, 2018)[141].
More in detail, as for the PE concept outlined in the Art. 5 of the OECD MTC, without prejudice to the "*summa divisio*" contained in para. 1 through 5 between "*material PE*" and "*personal PE*", here it is sufficient to add that para. 4, letter d) also includes the so-called "*brick and mortar*" sites, a term used to designate the physical presence of a company and, more strictly, the stores or physical spaces where customers can

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[138] WEBER D., *The Reasonableness Test of the Principal Purpose Test Rule in OECD BEPS Action 6 (Tax Treaty Abuse) versus the EU Principle of Legal Certainty and the EU Abuse of Law Case Law*, in *Erasmus Law Review,* No. 1, 2017, pp. 48 – 59; VAN WEST J. P., *The Anti-Abuse Rule for Permanent Establishments…*, 2020, pp. 256 – 58.
[139] See OECD Model Tax Convention on Income and on Capital - FULL VERSION – as it read on 21 November 2017 – and Commentary, Paris-Cedex, 2019, with particular reference to the "History" of single Articles and paragraphs 5 (4-6); 7(3); 29 (8-9) and Multilateral Convention to implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting (MLI), as it resulted by the Signatories and Parties status as of 10 November 2022, summarized, *infra*, in Appendix, Table 3. See, with particular reference to the PE concept, the content of the Art. 10, 13 e 14 of the Convention.
[140] The Art. 7(6) of MLI also includes the so-called *"Simplified Limitation on Benefits Provision"*, subjected to a Covered Tax Agreement only where all Contracting Jurisdictions have chosen to apply it. See what already mentioned in para. 2.4. of this work referred to the "minimum standard on treaty shopping".
[141] ALMEIDA L., TOLEDANO P., *Understanding how the various definitions of Permanent Establishment can limit the taxation ability of resource - rich source countries*, in *Columbia Law Review*, March 2018, p. 28.

visit in person to see, buy and test products or services, request assistance or return the purchased goods.

Over the years, online sales have become much more widespread and the retail world has undergone profound changes, giving rise to new sales models and new terminologies to identify them, such as the expression "*click and mortar*" used to specifically define companies that exploit both the online channel and the physical store (Steinfield et al, 2002)[142].

As far as the MLI is concerned, it should be preliminarily observed that the Art. 6 para. 1 requires the Contracting Parties to include in the preamble to the Covered Tax Agreement the following formula ("minimum standard on treaty shopping"): "*Intending to eliminate double taxation with respect to the taxes covered by this agreement without creating opportunities for non-taxation or Reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this agreement for the indirect benefit of residents of third jurisdictions*)", or other equivalent formulas [Art. 6 (2 -3)].

BEPS Action 6 intervenes in particular on the Art. 7, entitled, in fact, "Prevention of Treaty Abuse", whose para. 1 reflects in a mirror way the Art. 29(8) of the OECD MTC, already commented, and otherwise provides detailed terms and conditions of use of the "Simplified limitation on benefits" (LOB).

In particular, the Art. 10(1) MLI "*Anti-abuse Rule for Permanent Establishments Situated in Third Jurisdictions*" reproduces art. 29(8) of the OECD MTC.

It should be noted that – as in the case of Art. 29(8) of the OECD MTC – the two conditions indicated in letters a) and b) of the paragraph [a) *enterprise of a Contracting Jurisdiction deriving income from the other Contracting Jurisdiction treats such income as attributable to a PE situated in a third jurisdiction*; b) *the profits attributable to that PE permanent establishment are exempt*] are not alternative but they must coexist, as can be seen from the conjunction "and". Then, they both depend on the occurrence of a third condition: that "*the tax in the third Jurisdiction is less than 60 per cent of the tax that would be imposed in the first-mentioned*

142 STEINFIELD C., BOUWMAN H., ADELAAR T., *The Dynamics of Click-and-Mortar Electronic Commerce: Opportunities and Management Strategies*, in *International Journal of Electronic Commerce*, Vol. 7, No. 1 (Fall, 2002), pp. 93-119.

Contracting Jurisdiction on that item of income if that permanent establishment were situated in the first-mentioned Contracting Jurisdiction".

The Art. 12, 13, 14 of the MLI reproduce, basically, the scope and the object of BEPS Action 7, aimed at countering, respectively, the "*Artificial avoidance of PE status through commissionaire arrangements and other similar strategies*", the "*Artificial avoidance of PE status through the specific activity exemptions*" and the "*Splitting-up of contracts*", as it has been described above more in detail (see para. 2.2.).

Generally speaking, this is the "state of art" of the PE concept after the advent of the BEPS Project and the multilateral "Inclusive Framework" initiative, launched in 2016 by the OECD-G20 and variously debated among scholars ("ex multis" Baggio, Tosi, 2022; Losada, 2019; Maisto, 2019)[143].

On one point these scholars seem to agree: although both the OECD MTC and the MLI have reached such a high number of accessions and favored the signing of an impressive number of bilateral treaties to prevent double taxation and avert the risk of a double "non-taxation" on the profits of the MNEs, the process of elaborating the PE concept and, above all, of attributing the right to tax by the residence-countries rather than the source-countries will characterize the debate for many years to come, also because it needs a particular coordination with the action of the United Nations aimed at spreading its Model of DTC, aimed at welcoming the requests of the developing countries (Avi-Yonah, 2019, Ashfaq Ahmed, 2020)[144].

It is also worth mentioning that, although the Inclusive Framework include countries like Brazil, Russian Federation (the last one currently suspended), India, China, South Africa (so-called 'BRICS countries') and United States (Annex, Table 2), Brazil and United States didn't sign yet the Multilateral Convention to implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting (Annex, Table 3), which seems to

[143] BAGGIO R., TOSI L., *Lineamenti di diritto tributario internazionale*, Padova, 2022, pp. 58 – 70; LOSADA S.R., *A New Nexus Based on the Concept of Significant Economic Presence: The Digital Permanent Establishment*, in HULKÓ, G. et al, *European Financial Law in Times of Crisis of the European Union*, Budapest, 2019, pp. 377–389; MAISTO G., *New Trends in the Definition of Permanent Establishment*, Amsterdam, 2019, pp. 69 – 87; 206 – 209.

[144] AVI-YONAH R.S., *Advanced Introduction to International Tax Law*, Northampton, MA, U.S.A., 2019, pp. 73 – 74; ASHFAQ AHMED M., *United Nations Model Tax Convention Article 5: The Predatory Ploy – A Neo-Marxist Mapping of the Permanent Establishment*, in *Manchester Journal of International Economic Law*, 2020, Volume 17, Issue 2, pp. 216 -217.

say a lot about the fact that the duration of the process stems from geo-political strategies rather than from legal reasons (Herzfeld, 2020; Oats, 2021)[145].

However, in the aforementioned debate, two positions seem to be interesting.

The first, based on the "resource rich States" concept rather than on "advanced" or "developing countries" one, suggests those countries to adopt a PE provision that increases their rights to tax at source exclusive of an equivalent provision for the other treaty State (Almeida – Toledano, 2018)[146]. According to this approach and in addition to broadening the PE definition, resource rich States might also want to consider including an "*offshore clause*" in their Double Taxation Agreements, providing, as exception, that where offshore activities of a person constitute for that person a Permanent Establishment under the concerned provisions or a fixed base under the concerned provisions concerning Independent Personal Services, the DTA providing for "*an enterprise of one of the States which carries on offshore activities in the other State shall be deemed to be carrying on, in respect of those activities, business in that other State through a Permanent establishment situated therein, unless the offshore activities in question are carried on in the other State for a period or periods not exceeding in the aggregate 30 days in a calendar year*" shall not apply[147].

The scholars observe, however, that although such proposal will likely contribute to a significant increase in taxing rights, it is important to realize that it will also likely result in an increase in the source States administrative costs. In developing countries, where tax administrations will typically lack the necessary resources to deal with lengthy and complex tax disputes, this might become a challenge[148].

The second position, rather skeptical about the actual effects achieved by the BEPS project, especially with regard to Action 1 – "*Address the tax challenges of the digital economy*" – notes that, with the sole exception of the OECD MTC changes concerning

[145] HERZFELD W., *International Taxation in a nutshell*, St. Paul, MN, U.S.A., 2020, pp. 174 – 175; OATS L., *Principles of International Taxation*, London, 2021, p. 228;

[146] ALMEIDA L., TOLEDANO P., *Understanding how the various definitions of Permanent Establishment…*, New York City, U.S.A., March 2018, pp. 34-35.

[147] ALMEIDA L., TOLEDANO P. quote the case of the United States Tax Convention with the Netherlands, effective date 1 January 1994, whose Art. 27(1) – *Offshore Activities* – reads as follows: "*1. The provisions of this Article shall apply notwithstanding any other provision of this Convention. However, this Article shall not apply where offshore activities of a person constitute for that person a permanent establishment under the provisions of Article 5 (Permanent Establishment) or a fixed base under the provisions of Article 15 (Independent Personal Services). 2. In this Article the term "offshore activities" means activities which are carried on offshore in connection with the exploration or exploitation of the seabed and its sub-soil and their natural resources, situated in one of the States*".

[148] See ALMEIDA L., TOLEDANO P., *Understanding…,* March 2018, p. 35.

the PE concept, for the rest the OECD has not yet suggested the implementation of specific measures to counter the tax challenges emerging from the Digital economy (Losada, 2019) [149].

On the contrary, the introduction of a clause on PE digital services in the OECD MTC would be an interesting alternative to allocate more taxable income in market jurisdiction than the one – currently used – of applying the new PE nexus. This is also because the absence of a threshold and issues on the allocation of profits would facilitate its implementation.

2.6. The attribution of profits according to the updated OECD Models.

As seen above, the defining process of PE concept developed by BEPS Action 7 still leaves open some questions concerning the actual attribution of cross-border profits when they are generated by an enterprise operating abroad through a PE.

And this is because in the OECD Model the definition of the concept of PE is elaborated in the Art. 5, subject to numerous changes, adjustments and filings, while the definition of the attribution of profits – and consequently, the attribution of the right to tax them by a State (residence-country or source-country) – is found in the Art. 7 and, to a lesser extent, in other articles of the Model [e.g. Art. 29(8)].

This criticality of the BEPS Project, noted both before and after its beginning (Baker - Collier, 2006; Garbarino, 2019) [150], depends on the concerns of the participating States and expressed by the OECD Committee of Fiscal Affairs (hereinafter CFA) in the Report of 15 May 2015, according to which to countering the elusive strategies put in field from the MNEs it was not necessary to proceed to new changes in the Art. 7 of the Model, which reflect the final draft of the Authorized OECD Approach (AOA) in terms of attribution of profits generated by a PE (OECD, 2010) [151].

The method of analysis for the attribution of profits to a PE suggested by the OECD is the so-called "*functionally separate entity approach*" which consists of two distinct steps, assuming, in fact, that the PE behaves in its relations with the parent company as if both

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[149] See LOSADA, S.R., *A New Nexus Based on the Concept of Significant Economic Presence…*, Budapest, 2019, p. 388.

[150] BAKER P., COLLIER R. S., *The attribution of profit to Permanent Establishment*, Gent, 2006, pp. 54 – 60; GARBARINO C., *Doing Business through a Permanent Establishment (PE)* in *Taxation of Bilateral Investments – Tax Treaties after BEPS*, Northampton, MA, 2019, pp. 7 – 9.

[151] OECD, *Report on the attribution of profits to Permanent Establishments*, Paris-Cedex, 22 July 2010, pp. 12 – 28.

were separate entities on the basis of the "*arm's length principle*" – on which the Art. 7 of the OECD MTC is based – taking into account the functions performed, the assets used and the risks assumed by the enterprise through the PE and through the other parts of the enterprise (OECD, 2010; Valente, 2010) [152].

First step consists of a functional and factual analysis that must aimed at identifying the economically significant activities and responsibilities undertaken by the PE.

Under the second step, the remuneration of any dealings between the considered enterprises is determined by referring to all of them the functions performed, the assets used and the risk they assumed. The result of these two steps will be to allow the calculation of the profits (or losses) of the PE from all its activities, including transactions with other unrelated enterprises, transactions with related enterprises and dealings with other parts of the enterprise[153].

After the consolidated version of the OECD MTC (2017), the Organization published its Guidance on the same subject (OECD, 2018)[154] pointing out, first, that the 2015 Report "*concluded that the changes to the definition of PE in Article 5 of the OECD Model Tax Convention did not require substantive modifications to the existing rules and guidance on attribution of profits to PEs under Article 7 of the OECD Model Tax Convention*" and providing, on the other hand, high-level general principles aimed at the correct interpretation of the Art. 5(4), (5) and (6) of the Model (OECD, 2018)[155].

Even in this case, there have been criticisms and observations by scholars and policy makers (Spinosa, Chand, 2018; Hamdan, 2019)[156] who complain that the "*Guidance does not cover all the required areas of the problem*", with particular reference to the E-commerce sector and consider the adoption of an "Electronic Permanent Establishment"

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[152] OECD, *Report on the attribution of profits…*, 2010, p. 12, para. 8; in this this regard see, more in depth, VALENTE P., *Attribuzione del reddito alla stabile organizzazione. Il Rapporto OCSE del 2010*, in *il fisco*, n. 43/2010, pp. 7000 – 7013.

[153] OECD, *Report on the attribution of profits…*, 2010, p. 13, para. 10.

[154] OECD, *Additional Guidance on the attribution of profit to Permanent Establishment _ BEPS Action 7*, Paris-Cedex, 2018.

[155] The principles concern the Attribution of profits to a permanent establishments resulting from changes to Article 5(4) and the Commentary and the Attribution of profits to permanent establishments resulting from changes to the Article 5(5), (6) and the Commentary: see OECD, *Additional Guidance…* paragraphs 11 – 20 and 26 – 42 that provide various examples concerning Warehousing, Delivery, Merchandising and Information Collection Activities, (Art. 5(4)); Commissionaire structure; Sale of advertising on a website; Procurement of goods (Art. 5(5), (6).

[156] SPINOSA, L., CHAND, V., *A Long-Term Solution for Taxing Digitalized Business Models: Should the Permanent Establishment Definition Be Modified to Resolve the Issue or Should the Focus Be on a Shared Taxing Rights Mechanism?* in *Intertax*, 2018, Vol. 46, Issue 6, pp.476-494; HAMDAN M.A.J., *Overview of Rules Governing Attribution Profits Generated from Permanent Establishment*, in *Advances in Social Sciences Research Journal,* 2019, 6(9), pp. 339-354.

(EPE) as an option for the attribution of profits, at the international level, when they are connected to cross-border business transactions in the context of the Digital economy. Such definition should be flexible enough so to be adapted to technological progress.

2.7. The UN Model DTC 2017 and the "Force of attraction principle".

Despite the criticisms highlighted above, the two steps method so-called "*functionally separate entity approach*" (AOA) adopted by the OECD in the MTC – Art. 7 has been widely used by the countries taking part to the "OECD/G20 Inclusive Framework" and to the BEPS Action 7, for the attribution of profits to a PE.

However, it is not the sole existing method in this regard in the list of procedures for negotiating international treaties against double taxation (or "double non-taxation").

The United Nations in their 2017 Model Double Taxation Convention between Developed and Developing countries – which takes into account the demands of the Developing Countries where the "source-principle" prevails over the "residence-principle", as to the international taxation – have proposed a different approach: the so-called "*force of attraction*" principle (OECD Glossary of Tax Terms, 2022)[157].

In fact, although both models (OECD and UN) deal with the issue of the allocation of profits (Business profit) and the consequent right to tax them in Art. 7, the content of the articles coincides only in para. 1, first part. For the rest, it is profoundly different: this is because in the OECD Model the AOA system is described, while the UN Model reflects the Force of Attraction principle[158].

The reason of the difference between the two approaches has been explained directly by the United Nations in their Commentary (UN, 2021)[159]: "*Under the OECD Model Tax Convention, only profits attributable to the permanent establishment may be taxed in the source country. The United Nations Model Tax Convention amplifies this attribution principle by a limited force of attraction rule, which permits the enterprise, once it carries*

[157] See OECD Glossary of Tax Term – updated 2022 in *https://www.oecd.org/ctp/glossaryoftaxterms.htm#F*, under the voice: "Force of attraction" **-** Concept under which a permanent establishment is taxed by the country in which it is located not only on the income and property, but also on all income derived by its foreign head office from source in, and all property owned by the foreign head office situated in, the country where the permanent establishment is located. The OECD model treaty does not allow application of it.

[158] Be aware that the UN Committee of Experts on International Cooperation in Tax Matters includes representatives of countries such as China (particularly active), India and Russian Federation (BRICS), which are not represented in the OECD Committee of Fiscal Affairs - CFA.

[159] See UN Commentary 2021 on Art. 7, para. 4.

out business through a permanent establishment in the source country, to be taxed on some business profits in that country arising from transactions by the enterprise in the source country, but not through the permanent establishment. Where, owing to the force of attraction principle, the profits of an enterprise other than those attributable directly to the permanent establishment may be taxed in the State where the permanent establishment is situated, such profits should be determined in the same way as if they were attributable directly to the permanent establishment" [160].

Some scholars (Sagar, 2017; Oats, 2021)[161] consider that the effect of the 'limited force of attraction' provision is that any profits a multinational make in a developing country through sales or other business activities there are taxable if there is a PE and the activities are the same or similar to those conducted by a PE. Although this rule is permitted by the UN MDTC, not all treaties based on this Model include this rule[162].

The fact is that the UN Double Taxation Model Convention in its last does not seem to have found much following to date. This depends on several factors among which the limited ability of developing countries to obtain from developed countries the necessary

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[160] It should be mentioned that, in 2019, the representative of China in the Committee of Experts made reservations on the text, on this basis: "*The limited force of attraction rule in the UN model was designed to catch sales or other business activities "carried on in that other State of the same or similar kind as those effected through that permanent establishment", but in treaty implementation, there can be an application of this rule to activities that are not carried on in that other state, and therefore to income that's not derived from (does not arise in) that State.*
A typical case scenario of such kind is the EPC (engineering, procurement and construction) contract in which the home office of an enterprise of a Contracting State undertakes the provision of goods or merchandise (composed of engineering and procurement activities conducted in the home country) , and the permanent establishment of the enterprise situated in the other Contracting State undertakes the assembly or installation activities in connection with such goods or merchandise and has no involvement in the provision of the goods or merchandise.
Some countries would apply the force of attraction rule in the treaty to attribute to the PE the profits derived from the provision of goods or merchandise conducted by the home office. But the provision of goods or merchandise is not an activity of the same of similar kind as those effected through the PE (which undertakes assembly or installation activities only), and more importantly, all activities related to the provision of goods or merchandise including engineering and procurement are conducted by the home office in the home country.
Some countries may do so even without having the force of attraction rule in the treaty, in which case they should have attributed to that permanent establishment only the profits resulting from the activities undertaken by the permanent establishment". See UN Committee of Experts on International Cooperation in Tax Matters*, Item 3 (1) of the provisional agenda Article 7 (Business Profits) of the UN Model Convention, including the "force of attraction" principle, and its application in the case of EPC (engineering, procurement and construction) contracts*, Geneva, 2019, pp. 1 – 2, the reservations of Ms. Yan Xiong, representative of China.

[161] SAGAR S., *How "Limited" is 'Limited Force of Attraction'? An Analysis of Relevant Case Law and the Potential Implications of the OECD/G20 BEPS Initiative*, in *Bulletin for International Taxation,* 2017, Vol. 71, No. 3/4, pp. 182 – 83; OATS L., *Principles of International Taxation*, London, 2021, p. 224.

[162] OATS L., *Principles…*, p. 224, mentions some Indian treaties.

information on business transactions occurred and/or to carry out a complete analysis for tax purposes[163].

[163] At present, no official UN data are available on this matter. The only available data are those of the G-24 Group countries, for which reference is made to Annex 2 of the WP Inter-Governmental Group of Twenty-Four, *Tax treaties of G-24 Countries: Analysis Using a New Dataset*, Washington D.C., May 2021, p. 23. The analysis focuses, inter alia, on the implementation of the PE definition as resulting both from the OECD Model and the UN Model.

CHAPTER 3

THE PERMANENT ESTABLISHMENT REGIME IN THE ITALIAN INCOME TAX CODE.

3.1. The definition of Permanent Establishment (art. 162 Income Tax Code).

The PE concept is expressed in the Art. 162 of the Italian Consolidated Income Tax Code (hereinafter T.U.I.R., abbreviation meaning: "*Testo Unico delle Imposte sui Redditi*"), as amended in 2017[164].

It reflects, basically, the traditional combination of "material PE" and "agency PE", as they read in the Art. 5 of the OECD Tax Model Convention, in its latest version (OECD MTC and Commentary, 2019) [165], apart from some peculiarity, totally Italian, which will be discussed below.

Thus, the first two paragraphs of the Article 162 perfectly reproduce the first two paragraphs of the Art. 5 of the OECD MTC, concerning the "*material PE*".

However, the para. 2 of the T.U.I.R. contains a letter "f-bis", unknown in the OECD MTC text, introducing in the domestic Tax Law the new "nexus rule" of "'s*ignificant and continuous economic presence*' within the territory of the State, built in such a way as not to result in its physical presence within that territory".

Some scholars (Loconte et al, 2018)[166] renamed the new "nexus rule" as "Digital PE", pointing out the fact that the formula "*significant and continuous economic presence*" is

[164] See the Art. 162 of the Italian Consolidated Income Tax Code (abbreviation T.U.I.R.) as it read after the amendments provided by the Art. 1 of the Law 27 December 2017, n. 205, in force since 1 January 2018: "1. (…) the term "Permanent establishment" means a fixed place of business through which a non-resident enterprise carries on all or part of its activity in the territory of the State.

2. The term "Permanent establishment" includes in particular:
   (a) a place of management;
   (b) a branch;
   (c) one office;
   (d) a workshop;
   (e) a laboratory;
   (f) a mine, an oil or gas field, a quarry or other place of extraction of natural resources, including in areas outside territorial waters where, in accordance with customary international law and national law concerning the exploration andexploitation of natural resources, the State may exercise rights over the sea-bed, its subsoil andnatural resources (…)"

[165] The Model Tax Convention and the Commentary referred to, published by the OECD in 2019, contains the full version as it read on 21 November 2017.

[166] LOCONTE S., FAVI L., *A new definition of Permanent establishment in Italian domestic income tax law*, in *Insights,* 2018, Volume 5 no 3, pp. 5 – 10.

used by the lawmaker to extend the scope of the application of the material PE to those cases of business – as it is for the digital service networks – which cannot be attracted therein according to the ordinary rules, but nevertheless do realize considerable tax-exempt profits. This because of the tremendous difficulty to detect their real "*place of business*".

More recent studies ("ex multis" Picardi, 2019)[167] have suggested that the mentioned provision is an attempt to better correspond to the BEPS Action 1, aimed at countering the challenges launched by the Digital economy in terms of international taxation.

However, the main weakness of the Italian lawmaker's approach is the fact that the provision was unilaterally included in the T.U.I.R. but not poured down in the multilateral or bilateral tax treaties. With the consequence that this new Italian nexus does not affect the ordinary rules applicable in cases where a foreign MNE is resident in States with which Italy has entered into a double tax agreement.

Unilateral approaches simply run the risk of undermining the relevance and sustainability of the intervention, which result in the failure of the international negotiation on this issue[168].

A third interpretation (Forestieri, Salvini, 2019)[169] connects the aforementioned provision to the anti - avoidance rules of the OECD MLI Convention – Art. 7-10 – concerning the Prevention on Treaty Abuse, and Part IV, aimed in particular at combating Avoidance of Permanent Establishment Status, in accordance with the recommendations adopted by BEPS Action 1.

According to this opinion, the scope of Article 162, para. 2, lett. f) would be, in fact, to attract into Italy's fiscal power the profits generated by a foreign MNE that has, in the State, a non-insignificant or transitory economic presence, concretized in a physical installation in the territory.

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[167] PICARDI L., *Taxing multinationals in the digital services sector has remained a complex international challenge for local governments limited in their jurisdictional capabilities,* in *International Tax Review*, August 22, 2019, in *https://www.internationaltaxreview.com/article/2a6a3lfsp39jvzrloe2gw/taxing-the-digital-services-sector-in-italy.*

[168] See PICARDI L., *Taxing multinationals in the digital services sector…*, last paragraph "*Italy's digital tax outlook*" in *International Tax Review*, 2019.

[169] FORESTIERI V., SALVINI L., *Il nuovo articolo 162, 2° comma, lett. f-bis) del TUIR alla luce dello strumento multilaterale: il Legislatore italiano ha veramente introdotto una norma sulla stabile organizzazione virtuale? Iuris Prudentes*, 26 novembre 2019, in *https://www.iurisprudentes.it/2019/11/26/il-nuovo-articolo-162-2-comma-lett-f-bis-del-tuir-alla-luce-dello-strumento-multilaterale-il-legislatore-italiano-ha-veramente-introdotto-una-norma-sulla-stabile-organizzazione-virtuale/*

In this sense also goes the para. 3 of the Art. 162 of T.U.I.R., concerning the minimum threshold of the presence of the PE, which in the Italian version must be more than three months, while in the text of Art. 5 of the OECD MTC the minimum threshold is above twelve months (Appendix, Table 4) [170].

The disguise this material appropriation as well as the attempt of making this settlement negligible –for instance, through the fragmentation of the activity carried on, or temporary - for example, through the contractual splitting-up – does not allow the taxpayer to escape the tax power of the *source-State*.

In this sense, the "new nexus" rule aims at implementing the spirit of BEPS Action 1 in domestic Tax Law.

Finally, others (Polacco, De Carne, 2022)[171], quoting the Tax Settlement Agreement recently reached between Netflix Inc. and the Italian Revenue Agency, have highlighted the practical consequence of the new approach which conducted to claim the existence of a "fixed place of business", based on the availability of a network of servers used exclusively to provide Italian customers with a streaming service.

This conclusion stems from the fact that the qualifying economic requirement taken into account by the rule (the "*significant and continuous economic presence*") is suitable for replacing that of mere physical presence ("*fixed place of business*") in the elaboration of the PE concept and therefore in the declaration of the right to taxation by the State where this economic requirement could be easily identified.

The opposite conclusion ("no Permanent Establishment") could determine an international double "non-taxation" regime whose contrast is instead one of the corner stones of the BEPS Action Project[172].

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[170] See, *infra*, Appendix, Table 4, that shows the Construction Permanent Establishment Threshold in Tax Treaties updated 2013. Italy is included in the group of 13 OECD and Non-OECD countries which adopted the threshold of three months.

[171] POLACCO G., DE CARNE A., *Italian Tax Authorities Expand Concept of Permanent Establishment for the Digital Age*, in *Bloomberg Daily Tax Report International*, July 5, 2022, in *https://news.bloombergtax.com/daily-tax-report-international/italian-tax-authorities-expand-concept-of-permanent-establishment-for-the-digital-age.*

[172] According to the authors of the article quoted above: "*This development is a sign that the definition of a PE is continually evolving, becoming more fluid and uncertain. The tax authorities are clearly looking to expand the interpretation of a PE, adapting it to the ways in which businesses have changed over the years, particularly with respect to the explosion of the online and digital economy. As a result, as with the 2002 Philip Morris case (Ministry of Finance v Philip Morris (GmbH), No. 7682/05, May 25, 2002), the Italian tax authorities are now adopting an analysis of the business model of enterprises that uses an interpretation that goes beyond the literal wording of legal provisions in order to tax profits that would otherwise not be subject to domestic taxation*".

On the other hand, the various attempts to disguise or conceal the actual exercise of an MNE's business activity in the territory of the State, through the artificial use of PE status – which the lawmaker wished to counter with the introduction in the T.U.I.R. of the new nexus rule of the significant and continuous economic presence described in letter f-bis of the Art. 162 – have induced tax administration as well as policy makers and the Courts to elaborate the concept of "hidden permanent establishment" of which it is time to talk.

3.2. The Hidden Permanent Establishment.

The concept of "hidden permanent establishment", developed in Italy at the beginning of this century, constitutes a subset of the traditional concept of "Permanent Establishment", either "material PE" (Art. 5 OECD MTC, para. 2 – 4) or "personal PE" (Art. 5 OECD MTC, para. 5 – 8), i.e. the entities in which persons and means legally refer to a non-resident enterprise[173].

However, in this context, the "Hidden Pe" is a legal distinct entity from the above-mentioned enterprise; it becomes a center of imputation of business transactions and therefore subjected to the right of taxation of the State which attributes that entity an ability to pay (Valente, Vinciguerra, 2018)[174].

The spread of hidden PEs is constantly growing because of the coming up of the new tax planning models with which MNEs present themselves on the global market.

As already seen, the Italian legislator has introduced in the Art. 162, para. 2 of the T.U.I.R. the letter. f-bis) in which it refers to a "*significant and continuous economic presence in such a way as not to result in its physical presence*" nexus, not expressed in the Tax Convention Models neither by the OECD nor by the United Nations, both with regard to the "material PE" and with regard to the "personal PE", but resulting in the proposals of

[173] The authors who deal with "hidden PE" attribute the elaboration of the concept to the well-known "Philip Morris" case (Italian Supreme Court, 7 March 2002, Nos. 3667, 3368, 7682 and 1095) for which reference is made "ex multis" to VALENTE P., VINCIGUERRA L., *Stabile Organizzazione*, Milan, 2018, pp. 120 – 126. The case globally remains known as "The Italian case" in the field of taxation of MNEs. See, in this regard, SCHOUERI E., GÜNTHER O., *The Subsidiary as a Permanent Establishmen*t, in Bulletin for International Taxation, February 2011, pp. 69 - 74, reporting the Seminar A of the 64th Congress of the International Fiscal Association, held in Rome, Italy on 30 August 2010. Finally, see also OECD Commentary, 2019, art. 5, para. 116.

[174]VALENTE P., VINCIGUERRA L., *Stabile Organizzazione*, Milan, 2018, pp. 3 – 38.

TFTD OECD 2015 Action 1 Report as "*significant economic presence*" test (OECD/G20, 2018)[175].

That's why the Consolidated Italian Income Tax Act (T.U.I.R.) has tried to fill a gap in the international definition of PE, amending the pertinent domestic provisions.

Anyhow, it must be acknowledged, that up to date the Tax Administration has not made a systematic and massive use of this category.

It has mostly challenged a foreign Parent the presence on the Italian territory of a hidden PE in cases of limited autonomy and substantial dependence of the Italian Subsidiary on the decisions of the Parent[176].

In practice, thus, the notion of "hidden PE" refers to a fixed place of business in which a foreign enterprise carries on all or part of its business, in a conscious or unconscious form - through an organization of persons and means or through an entity acting as an employee/independent agent - without declaring, however, to the Tax Authority of the country in which it is located, the related profits generated by it and to it directly attributable.

The notion of hidden PE (of the "material" or "personal" type) refers to a plurality of circumstances concealed, disguised, dissimulated and however undeclared, found according to a logical-deductive procedure based on detectable indicators and items recognized during a tax audit by the competent authorities[177].

In this logical-deductive procedure, the Tax Administration cannot of course ignore the principle contained in the Art. 5(7) of the OECD MTC, reproduced in the Art. 162(9) of the T.U.I.R., i.e. "*The fact that a company resident in one Contracting State controls or is controlled by a company resident in another Contracting State or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other*".

On the basis of this legal premise, the following situations of "hidden PE" have been hypothesized (Valente, Vinciguerra, 2018)[178]:

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[175] See, OECD/G20, *Tax Challenges Arising from Digitalization Interim-Report*, Paris-Cedex, 2018, para. 1.3.3. (20) "The broader tax challenges raised by digitalization". The TFED is the Task Force on Tax and Development.

[176] See again VALENTE P., VINCIGUERRA L., Stabile organizzazione, Milano, 2018, p. 8, which cite in this regard the "*spirit of law*" evoked in the *OECD Guidelines for Multiple Enterprises*, Paris-Cedex, 2011, para. 100.

[177] The definition of "hidden PE" used here is excerpt from VALENTE P., VINCIGUERRA L., *Stabile organizzazione*, Milano, 2018, p. 16.

[178] See VALENTE P., VINCIGUERRA L., *Stabile* ..., pp. 17 – 18.

(1) the redevelopment as “hidden (*material*) PE” may mostly stem from the fact that the business conducted by the Italian company (i.e. the “*place of business*”) may consist, by reason of the *ordinary business* and its operating methods, in business activity on behalf of the parent company;

(2) the branch of an Italian company which is controlled, directly or indirectly, by a foreign company (“*holding*”) may be qualified, by reason of the business carried on and of its operating methods, as “enterprise dependent agent” (OECD MTC, 2017; OECD BEPS Action 7, 2018)[179] of the foreign holding and, therefore, “*hidden personal PE*”;

(3) an Italian company is controlled by a foreign company (“*holding*”) as it is under subparagraph (2); the Italian branch may be qualified, by reason of the business carried on and of its operating methods, as “*hidden PE*”, either “*material*” or “*personal*”;

(4) a foreign company has a representative office in Italy: the office, by reason of the business carried on and of its operating methods, may be qualified as “*hidden PE*” for tax purposes;

(5) a foreign company does not have in Italy either a shareholding in a resident company or a representative office, but still carries on, in the shadow and mostly consciously, business activities through persons and means that, collectively considered, constitute an “*hidden PE*”.

Among the criteria for the identification of a “*hidden PE*” with regard to the aforementioned circumstances, the same authors (Valente, Vinciguerra, 2018)[180] suggest the following:

a. the lack of an authentic separation – from the point of view of the persons entrusted of the management of the business and/or of the pertinent functions – between the Italian company and the foreign one;

b. the existence of a substantial subordination of the managerial staff of the Italian company to the top management of the foreign one;

c. the fact that the Italian entity carries on activities in favor of one or more foreign companies of the group, though no consideration or fee is requested;

[179] See the Art. 5 (5,6) of the OECD MTC, as it read on 21 November 2017 and OECD *Additional Guidance on the attribution of profits to Permanent Establishments*, Paris – Cedex, 2018, para. 2(30).

[180] See VALENTE P., VINCIGUERRA L., *Stabile …*, p. 19.

d. the existence of specific agreements concerning the prior determination of the economic regulation of transactions concluded between the Italian resident company and the non-resident one;
e. the participation of the Italian entity, possibly even without the power to negotiate the terms of the contracts in its head, in one or more of the stages necessary for their conclusion in the name and on behalf of the foreign company;
f. the fact that the entities involved use the same information tools[181].

Finally, common to the activity of ascertaining the existence of a "hidden PE" is the circumstance of the move of the mere Registered Office of the Parent Company or of the holding in a non-tax or lower-tax jurisdiction[182].

Thus, in practice if an Italian parent company or an holding company move their registered office to a foreign State with a lower level of taxation, leaving, for the rest, that the actual operating and managerial structure, their employees and the former "*value chain*" continue to conduct the business in their name and on their behalf, generating profits, without notice to the competent tax authority, the Internal Revenue Agency may presume the actual presence in Italy ("*source-country*") of at least one "hidden PE" and that the entire procedure of moving abroad their registered office had the sole or the main purpose of obtaining a tax advantage.

The jurisprudence has faced and resolved differently over time the questions examined here, until 2018, the year of entry into force of the a.m. "new-nexus rule" of the "*significant and continuous economic presence*", which has marked a more univocal interpretation and induced the foreign MNEs to search for a Tax Settlement Agreement with the competent Italian authorities.

3.3. Case law evolution.

The jurisprudence and practice have largely contributed to the elaboration of the PE concept in Italy, pouring down even in the international context (OECD/G20, 2018)[183], some interpretative questions emerging from the Tax treaties, in an attempt to fill the gap that the various models (OECD MTC; OECD MLI Convention, UN DTMC) present in

[181] See, in this regard, Italian Supreme Court, cases Nos 3367, 3368 and 7682 respectively filed on 7 March 2002 and 25 July 2002, "Italian Revenue Agency vs Philip Morris Inc."

[182] Arguing from Art. 7 of the OECD MTC and from art. 7 to 12 of the OECD MLI Convention.

[183] See OECD/G20 *Tax Challenges Arising from Digitalization Interim-Report*, Paris-Cedex, 2018, para. 1.3.3. (20).

the prevention of the Aggressive Tax Planning strategy adopted by the MNEs with the view of the achievement of a substantial double "*non-taxation*".
It does not belong to the purpose of this work to deepen the different interpretations and legal trends but rather to understand how they have contributed to form a legal basis, may be in a "soft law" type, on which to face and possibly solve the problems concerning the attribution of profits to a PE, arising from phenomena of exceptional global reach such as the Covid-19 pandemic and, more recently, those resulting from the Russia - Ukraine crisis.
Therefore, here below four cases are briefly reported – one of which has been resolved out of the Court – selected in order to show the case law evolution before and after the advent of the BEPS Action Project.

3.3.1. The "Philip Morris" case.

The "Philip Morris" case, which became famous within the OECD as the "*Italian case*" (Melis et al, 2015)[184], is a real milestone in the Italian case law evolution about the PE definition for having first produced the concept of "*multiple permanent establishment*".
The case originates from the tax audit made by the Agenzia delle Entrate (Italian Revenue Agency) to "Intertaba" – Italian subsidiary of the Philip Morris Group – contesting to it and to various Group companies, respectively, as far as Intertaba, to have acted, and as to the other companies and to the Group itself, to have used Intertaba as a Permanent establishment (as defined in the Article 5 of the existing Tax Treaty between Italy and the United States), for the conclusion of contracts with foreign companies of the Philip Morris group and this to the sole purpose to conceal the activities really carried on and the functions performed, on behalf of the same Group, in the Italian territory.
The case was the subject of several rulings by the Court of Cassation[185], in which it essentially upheld the allegations of the Tax Administration, which affirmed that the

[184] See MELIS G., RUGGERO E., *Impact of the digital economy on taxation*, Roma, 2015, pp. 38 – 40, who report the contents of the debate followed in the OECD to the various judgements of the Italian Court of Cassation on the case and the replies of the Financial Administration on the interpretation of art. 5 of the OECD MTC, 1977 version.
[185] Cass., Sez. V^ Civ., 20 December 2001, (filed on 7 March 2002), Nos. 3367 and 3368; 20 December 2001, n. 7682. See U.N.G.D.C.E.C. - Commissione di studio "Fiscalità, *La Stabile Organizzazione tra normativa fiscale nazionale e sovranazionale: limitazioni ed opportunità per l'impresa multinazionale*, 2013, Roma, 2013, pp. 35 – 39; MAIR S., SANTACROCE B., *La stabile organizzazione delle imprese industriali e commerciali*, Vicenza, 2016, pp. 19 – 31; VALENTE P., VINCIGUERRA L., *Stabile organizzazione…*, 2018, pp. 120 – 128.

Italian subsidiary belonging to the Philip Morris group, and dedicated to the production and distribution of cigarette filters as its main activity, was a permanent establishment of foreign companies belonging to the same group.

In particular, the Supreme Court argued that "Intertaba" constituted a "*multiple permanent establishment*" of the Group's foreign companies, since it was involved in the group's business activities without having any autonomy.

In its motivation, the Court stated the following principles, both procedural and substantive:

- in the view of the Tax settlement, all the elements acquired during the investigation activity must be considered usable, even if they do not relate directly to the relationship between the Italian company and the applicant companies (Philip Morris GmbH, Parent company and the companies belonging to the same Group). The tax audit, therefore, especially if it is aimed at establishing the existence of a hidden PE, must concern the activity carried out by the national structure outside its *ordinary business* and as a whole, with respect to the other enterprises, in their mutual connection with the general objectives of the Group;
- in order for the national structure not to be considered dependent, it is necessary that:
  - ✓ it has legal and economic independence;
  - ✓ acts for another undertaking within its ordinary business sector;
  - ✓ does not assume any entrepreneurial risk for the activities carried on in the interest of another enterprise;
- structures with the power to conclude contracts on behalf of the parent company cannot be considered independent. This power is not limited to direct representation, but must include all those activities that have contributed to the conclusion of contracts, even though they have been concluded on behalf of the Parent company;
- the participation of representatives or tasked of a national structure at a stage of the conclusion of contracts between foreign companies and other resident entities may be attributed to the power to conclude contracts on behalf of the company even outside the power to representation;
- the activity of monitoring the proper execution of contracts cannot be considered as preparatory or ancillary in nature, being strictly functional to the production of income;

- finally, the assessment of the requirements of the permanent establishment, including those of dependency and that of participation in the conclusion of contracts, must be conducted not only on the formal level, but also and above all on the substantial one ("*the substance over the form*")[186].

In conclusion, therefore, the Supreme Court ruled that "*a company established in Italy can assume the role of 'multiple PE' of foreign companies belonging to the same group and pursuing a unified strategy. In order to ascertain whether or not the activity carried out by the national company is of a preparatory or auxiliary nature, the reconstruction of the same must be unitary and related to the program of the Group considered as a whole*"[187].

3.3.2. The "Boston Scientific" case.

In the case "Agenzia delle Entrate *vs* Boston Scientific Spa", the Court of Cassation (2012)[188] seems to overturn the orientation expressed ten years earlier on the subject of PE, having rejected the last appeal of the Tax Administration and thus confirmed the judgments of first instance and appeal in favor of the company.

The case originates from the notice of Tax assessment in which the income produced by the Dutch company BSI BV was taxed in Italy on the premise that it was made through an Italian PE, identified in the Boston Scientific spa which is a company under Italian law controlled for 99% by the Dutch BSI BV and for the remaining 1% by the Boston Scientific Corporation USA, the latter identifiable as the Parent company, carrying on an activity aimed at "*design, production and marketing of less invasive medical devices*", whose distribution in Europe is entrusted to companies belonging to the Group, but based in various European countries.

In this organization chart the BSI BV plays the role of purchaser for the sale of the products of the group and stipulates commission contracts with the subsidiaries based in the various European countries that deal with the marketing and distribution of products

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[186] See in particular Cass., Sez. V Civ., Nos. 3368/2002; 7682/2002.

[187] See Cass., Sez. V Civ., 7 March 2002, No. 3368.

[188] Cass., Sez. V Civ., 9 March 2012, No. 3769. See for comments ROSSI M., *Italian Supreme Court Reverses Course on Permanent Establishment Issue*, in *European Union and Italian International Tax Law Blog,* November 23, 2012, in *https://www.euitalianinternationaltax.com/2012/11/articles/international-taxation/italian-supreme-court-reverses-course-on-permanent-establishment-issue/.*

(and therefore operating in its own name but on behalf of BSI BV), then obtaining a contractually agreed fee.

Having regard to the fact that BS S.p.A. is not legally or economically independent of its Parent company and that the company under Dutch law is also the sole customer of the Italian company, the Italian Revenue Agency has drawn the consequence that the former has operated as a PE of the latter, taking the view that the latter was liable to tax in Italy and that it should account separately for the revenue from the supplies of products made in Italy and make the relevant tax return in this country[189].

BSI BV appealed against those submissions on the basis of the Art. 5 of the Tax Treaty Italy – Netherlands, of the Art. 5 of the Tax Treaty Italy - U.S.A. and of the Art. 5 of the OECD MTC, version 2011, pointing out the fact that BS SPA had its own separate business organization of which it sustained all the costs, had assumed the economic risks of its business operations and was legally bound by the contracts it signed with the final buyers of the products under its own name as seller, resulting victorious before the Provincial Tax Committee and the Regional Tax Committee.

The Financial Administration appealed against those decisions to the Supreme Court, confirming the grounds for its findings.

The Court of Cassation rejected the application, observing that "*for the purposes of determining whether or not there is a PE, it is necessary to take into account all the factual elements put forward by the public party, because only the combination of these elements allows (in the light of the Art. 5 of the Conventions cited against double taxation of income taxes) to resolve the core of the controversial issue, which consists in determining whether the Italian company had the power to conclude contracts on behalf of the superior company, for which purposes, however, it is not significant neither the existence of a relationship of mediation/ agency, nor the existence of a shareholding control, however stringent*"[190]. And this criterion was not followed by the Revenue Agency in its notice of the Tax assessment.

The Court in particular referred to the provisions of the Art. 5 of U.S.-Italy Tax Treaty and argued that the Italian Revenue Agency failed to explain the reasons why those provisions should be read in a way to create a Permanent establishment when an Italian company contracts under its own name and risks and bears the economic cost of its

[189] See Cass., Sez. V Civ., 9 March 2012, No. 3769. para. 2.
[190] See Cass., Sez. V Civ., 9 March 2012, No. 3769. para. 2.

business organization through which it conducts its business in Italy, for the sole fact that it is owned and controlled by a foreign company and operates under the supervision and directions of its foreign parent company.
But, in closer inspection, the Court has not adopted any "*revirement*", recalling rather the principle already stated in its judgment 3368/2002 in the "Philip Morris" case, namely that: "*in order to ascertain whether or not the activity carried on by the national company is of a preparatory or auxiliary nature rather than the one carried on by a Permanent establishment the reconstruction of that activity must be unitary and related to the program of the group considered as a whole*".

3.3.3. The "Gulf Shipping" case.

Among the judgements of the Italian Court of Cassation on the PE concept, the one concerning the case "Gulf Shipping" is undoubtedly worth mentioning, and that for several reasons.
First, the judgement has been issued in the aftermath of the publication of the current OECD MTC (OECD, 2017) which, in turn, is influenced by the revising process of the international rules on double taxation (or double "non-taxation") resulting from the BEPS Action Project and, in particular, from the Action 7 aimed at "*Preventing the artificial avoidance of PE status, including through the use of commissionaire arrangements and the specific activity exemptions*".
Secondly, it rules on the basis of a reformed Art. 162 T.U.I.R.[191].
Finally, the decision is based on general principles ruling the PE status, since no Tax treaty on double taxation exists between Italy and the residence - country of the company "Gulf Shipping".
The case originates from the tax assessment made by the Italian Revenue Agency against a Panamanian shipping company and trade (Gulf Shipping & Trading Corporation Ltd Inc.) to whom the Agency had later contested a disguised taxable income, on the basis of the presumed existence of a PE in Italy through which the Panamanian company had carried on the business of trade in building materials.
Gulf Shipping challenged the notice, being victorious before the Provincial Tax Commission of Massa Carrara and the Tuscany Regional Tax Commission.

[191] See the Art. 1 of the Law 27 November 2017, n. 205 entry into force on 1 January 2018.

Therefore, the Tax Administration, appealed to the Supreme Court, pointed out towards the judges of the lower Courts that they had not fully evaluated the elements gathered by the investigative bodies, such as to exclude that the role of the Parent company was, as claimed by the taxpayers, totally marginal and limited to carry on – through the Italian entity – a purely preparatory and auxiliary activity not deemed to be classified as (*material*) PE [Art. 5(4) OECD MTC].

The case originates from the tax assessment made by the Italian Revenue Agency against a Panamanian shipping company and trade (Gulf Shipping (Gulf Shipping & Trading Corporation Ltd Inc.) to whom the Agency had later contested a disguised taxable income, on the basis of the presumed existence of a PE in Italy through which the Panamanian company had carried out the business of trade in building materials.

Gulf Shipping challenged the notice, being victorious before the Provincial Tax Commission of Massa Carrara and the Tuscany Regional Tax Commission.

The Tax Administration, on its side, appealed to the Supreme Court, pointed out towards the judges of the lower Courts that they had not fully evaluated the elements gathered by the investigative bodies, such as to exclude that the role of the Parent company was, as claimed by the taxpayers, limited to carrying out – through the Italian entity – a purely preparatory and auxiliary activity [Art. 5(4) OECD MTc].

The Supreme Court set aside the decisions of the Regional Tax Commission (judge of appeal) and sent the case back to a different chamber thereof setting forth four principles to be followed by the lower judge.

The Court, in brief, affirmed that, in order to declare a non-resident company liable to a taxable business income in Italy, it is necessary:

(1) a presence which is incorporated in the territory of the other State and has a certain stability;

(2) a fixed place of business capable, even if only potentially, of generating income;

(3) an activity independent of that carried on by the Parent company;

(4) for the purpose of applying direct taxes, the relevant investigation must be carried out not only formally but also, and above all, on the substantive level.

According to the Supreme Court, therefore, "*where it is established that a fixed place of business carries out both preparatory and auxiliary activities and activities which may constitute the existence of a permanent establishment, the fixed place of business cannot be considered as a PE for the whole. On the other hand, the PE exists solely because it has been established that business activities have been carried on by the PE itself, since*

it is irrelevant that, together with them, they have been carried on ancillary or preparatory activities in relation to further activities.
Where the above activities in fact result in a financing function or a provision of services to other undertakings, even if they form part of the group in which the parent undertaking is situated, cannot be reasoned in terms of the role played with merely preparatory or auxiliary purposes of the parent company to which it belongs, the pursuit of an independent economic result compared to that achieved by the head office by carrying on activities that are not directed exclusively according to the production cycle of the business activity of the parent company"[192].
With reference to the principles affirmed by the Court and especially to some seemingly contradictory parts of the motivation, some scholars (Arginelli, 2020)[193] have considered the arguments not to be shared, observing that in many respects the distinction between preparatory and/or auxiliary activities and the overall activities carried on by the PE, turns out to be of little use.
First, that conclusion appears at odds with the firstly principle affirmed by the Court in the very some decision, where it stated that, where a fixed place of business is used to carry on both preparatory/auxiliary activities and other (non-preparatory/auxiliary) activities, that place of business "*should constitute a PE for all activities performed*"[194].
Second, and most significantly the Italian domestic law provision dealing with the attribution of profits to PEs — Article 152 T.U.I.R. — does not encompass any exclusion from Italian taxation of income stemming from preparatory or auxiliary activities carried out by non-resident enterprises through a PE.
Therefore and in conclusion, whether or not the relevant activity is part of a complete business operation in Italy is absolutely irrelevant for the purpose of its taxation in Italy: if a PE exists (since no exception under the Article 162(4) T.U.I.R. applies and that activity is carried on through such a PE, the profits stemming from that activity must be taxed in Italy under the fiction of the PE being a distinct and separate enterprise engaged in the same or similar conditions and dealing wholly independently with the enterprise of which it is a PE.

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[192] See Court of Cass., Sez. V Civ., 8 October 2020, No. 21693.
[193] ARGINELLI P., *Italian Supreme Court deals with the notion of preparatory and auxiliary activities for the purpose of establishing the existence of a Permanent Establishment in Italy and determining its taxable profit,* in *Riv. dir. trib.*, n. 6/2020, pp. 1-12.
[194] See, textually, ARGINELLI P., *Italian Supreme Court…*, p. 6.

And this is also the leading legal reason why the Supreme Court in this case set aside the decisions of the Regional Tax Commission.

3.3.4. The "Netflix" case.

The fourth case here reviewed and worthy of attention concerns Netflix Inc., operating in the Sector of the Digital Economy, although its resolution has come, as mentioned above, in a non-judicial way, albeit with the consent of the Office of the Public Prosecutor of Milan[195].

This is the first known and most relevant application of the provision contained in art. 162, para. 2, lett. f-bis) of the T.U.I.R. (Italian Consolidated Tax Code) which introduces into the Italian Tax System the concept of PE as "*significant and continuous economic presence*", due to the 2017 reform, receiving the indications provided by the OECD BEPS Action 1[196].

The fact is that – according to the Guardia di Finanza Unit in Milan (Law Enforcement, exclusively entrusted by the Legislative Decree No. 68/2001 to protect the economic and financial interests of the State, of the regions, of the local entities and of the European Union) – the investigation conducted to the discovery of the Netflix availability in Italy of a network of servers used exclusively to provide a streaming service to Italian customers qualified as a foreign hidden PE by creating a "*fixed place of business*".

The network avails of over 350 servers, which would be used exclusively and installed permanently on the entire national territory in data centers and major telephone operators.

In the Netflix case the tax authorities considered that the sole presence of an advanced technological infrastructure on Italian territory, at data centers belonging to third parties, that was used exclusively by Netflix with the purpose of facilitating the transmission of information (thus qualifying the data centers as servers), could be considered to be a fixed place of business, even in the absence of any staff in Italy, because the relevant role of the so-called "*content delivery network*" was not preparatory or auxiliary to the business

[195] See MINCUZZI A., *Netflix versa 56 milioni al Fisco italiano. Procura: «Società occulta senza personale»*, in *Il Sole 24Ore,* May 20, 2022 in https://www.ilsole24ore.com/art/netflix-versa-56-milioni-fisco-italiano-procura-societa-occulta-senza-personale-AEvzoBaB?refresh_ce=1; POLACCO G., DE CARNE A., *Italian Tax Authorities Expand Concept of Permanent Establishment for the Digital Age*, July 5, 2022, in *https://news.bloombergtax.com/daily-tax-report-international/italian-tax-authorities-expand-concept-of-permanent-establishment-for-the-digital-age.*

[196] See, OECD/G20, *Tax Challenges Arising from Digitalization Interim-Report*, Paris-Cedex, 2018, para. 1.3.3. (20) "The broader tax challenges raised by digitalization". The TFED is the Task Force on Tax and Development.

activity. As a consequence of the settlement, Netflix had to pay approximately 56 million euros ($63.31 million) for taxes, interest and penalties for the fiscal years open to tax assessments (2016 to 2019), reaching a Tax Settlement Agreement with the Italian Tax Authorities.

3.4. The "*Marketplace*" case: the Employee's Dwelling as Hidden Permanent Establishment.

The "*Marketplace*" case, so called by the Italian Guardia di Finanza (the Economic and Financial Law Enforcement Agency) refers to the tax investigation then resulted in a notice of tax assessment by the Italian Revenue Agency (Agenzia delle Entrate) against the MNE "Farfetch UK Ltd", operating in the sector of "online" sales of luxury clothing concluded, on 31 July 2022 – with the consent of the Office of the Public Prosecutor of Bologna – through a Tax Settlement Agreement and a payment for about 12 million euros[197].

The investigations have revealed the existence and the operativity in Italy, from 2011 to 2019, of a hidden (*personal*) PE of the aforementioned British MNE.

The investigations started from the development of a complex and articulated risk analysis, conducted on the main business models of *e-Commerce*.

The multinational Group, operating worldwide as a virtual "*marketplace*" and service provider for physical stores active in the sale of clothing and accessories (*boutiques*) was one of the first to move in the field of *e-Commerce* of high fashion designer clothing (luxury fashion), revolutionizing the retail world through the winning strategy of integration between channels, so as to reach customers in over 190 countries around the world.

Tax auditors have noted the sudden expansion in the domestic market of the marketplace reaching, only in Italy, a portfolio of over 200 affiliated partners of the highest profile, all located in the most famous shopping streets and structured in such a way as to compose a sort of virtual network of warehouses, to be identified in the individual boutiques.

In particular, the foreign company, without ever formalizing its presence in Italy, formally hiring employees and start offices and/ or shops, has operated, in an absolutely hidden

[197] See RIZZI M., *Farfetch, stabile organizzazione a casa*, in *Italia Oggi*, 5 agosto 2022, p. 27.

way, exploiting the affiliated boutiques that, assuming any risk, have provided physical spaces for the storage of goods to be sold *"indirectly"* on the platform.
They were sifted through, therefore, over 400 Gigabytes of data, including 21 thousand emails, 20 thousand conversations via chat, 800 thousand images, 22 thousand text files and metadata through which it was possible, among other things, proceed to the georeferencing of the subjects and reconstruct the relationships between them. By way of example, by documenting the date and place of access to the various accounts (social, email accounts) used by employees, as well as wi-fi networks, the movements were reconstructed with precision and the exact location of the usual workplaces.
It was thus possible to ascertain that a team composed of Italian agents (*employees* of the British company) had carried on decisive activities (*core activities*) for the management of economic-business relations, negotiation, negotiating and concluding contracts with hundreds of national boutiques.
Compared to the online sales management services of the products present in physical stores, the marketplace (similar to a real virtual showcase) has collected fees of large amount from Italian partners calculated, on average, on 30% of sales.
Moreover, a real network of "*fixed places of business*" of the entrepreneurial activity has been established, constituted, in fact, by the employees' dwelling and by the working modalities ("*home working*") agreed with the Parent company.
The case is worth mentioning in several respects: first it represents an application of the case included in the Art. 162, para. 2 letter f-bis) T.U.I.R. of the definition of PE as "*significant and continuous economic presence*", entry into force in 2018. In fact, the investigation covers a period of 9 years of activity (2011 - 19).
Secondly, it is the first example of *"(personal) hidden PE*", in Italy, since the operating structure was mostly based on fixed place of business represented by employees' dwellings, in which the *agents* acted as "virtual contact points".
Third, the procedures which lead the investigation were triggered taking into account the principle stated by the Supreme Court in the "Philip Morris" case (N° 3368/2002), according to which "*the reconstruction of that activity must be unitary and related to the program of the Group considered as a whole*".
Finally, as in the Netflix case, the Tax Settlement Agreement and the Judicial conciliation method has been widely used, pursuant to the Art. 2, para. 4 of Legislative Decree No

218/97, before tax courts and Court of Cassation[198], thus speeding up the tax recovery action.

[198] This explains the prior consent of the Public Prosecutor to the Tax Settlement Agreement.

CHAPTER 4

THE IMPACT OF THE COVID-19 PANDEMIC ON THE EXISTING RULES CONCERNING THE CREATION OF PERMANENT ESTABLISHMENTS.

4.1. The OECD updated guidance on tax treaties and the impact of the COVID-19 pandemic.

4.1.1. Setting.

In the previous pages it has been overviewed the evolution of legislation, doctrine and case law that has characterized, for over a century, the legal grounds of the PE concept in international taxation.

As already seen, in the elaboration of the concept, the position of the concerned countries was mainly aimed at establishing which principle ("*source-country*", "*residence-country*") should prevail in the attribution of the right to taxation upon the income produced by a MNE – through a PE – outside the territory of origin (territory of incorporation).

It has also been seen how the tax treaty models established in this regard by the main International Organizations (League of Nations, United Nations and OECD), since the last century, were aimed, in the same time, at the prevention of the risk of double taxation and of the risk of double "non-taxation".

This approach has increased the need to safeguard the interests of developing countries with reference to, on one hand, the sudden evolution of the process of globalization of the markets as well as the progressive entry and increased influence in the organizations of global importance (e.g. WTO, IMF) of the so called "emerging" countries (i.e. "BRICS"), starting from the beginning of this century and, on the other hand, the impact of such processes in the elaboration of the rules concerning PEs ("*material*" or "*personal*")[199] .

Furthermore, it has been seen how the progressive digitalization of trade has encouraged even more the development of the business transactions and induced the main international organizations (e.g. UN and OECD) to revise the rules included in the Models

[199] See IMF, *BRICs Drive Global Economic Recovery*, Washington D.C., 2009, in *https://www.imf.org/en/News/Articles/2015/09/28/04/53/sorea072209a*.

of Convention, for the obvious difficulty to identify – through rules that seemed obsolete – where the "*place of business*" was located and the consequent income came from, so as to subject it to taxation.

Finally, the reaction of the advanced economies (i.e. BEPS Action Project, 2013) to the aggressive tax strategies of the MNEs has been examined, and the specific measures adopted to combat the artificial abuse of the PE status as a cornerstone of the fight against international tax avoidance, both bilaterally and multilaterally have been analyzed.

It is in this setting that the concepts of "*digital PE*" (OECD, 2015)[200], of "*significant and continuous economic presence*" (OECD/G-20, 2018; Italy, 2018)[201], of "*hidden permanent establishment*" and "*multiple permanent establishment*" (Italy, 2002 – 2018)[202] have been elaborated.

The pandemic from COVID-19 and the effects which followed, such as the restrictions on the movement of people, the curtailment of production and trade, the shortage of energy and food, aggravated by the crisis Russia - Ukraine (IMF, 2022)[203] mark the "*turning point*" in this process. These effects are also reflected in the definition of the rules governing the acquisition by States of both raw material (cereals, oil and its derivatives, silicon and lithium, for the production of microchips and batteries, logistics), and financial resources as well as in terms of work organization (so – called "*teleworking*"), in times of "*lockdown*" (OECD, 2021; OECD/G20, 2021)[204].

It is the OECD itself that admitted, on 21 January 2021, the exceptionality of the moment in its "*Updated guidance on tax treaties and the impact of the COVID-19 pandemic"* explaining that *"Unprecedented measures imposed or recommended by governments, including travel restrictions and curtailment of business operations (broadly referred to in this guidance as public health measures), have been in effect in most jurisdictions in*

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[200] OECD, *Addressing the Tax Challenges of the Digital Economy, Action 1 - 2015 Final Report*, 2015, available in *https://read.oecd-ilibrary.org/taxation/addressing-the-tax-challenges-of-the-digital-economy-action-1-2015-final-report_9789264241046-en.*

[201] See, OECD/G20, *Tax Challenges Arising from Digitalization Interim-Report*, Paris-Cedex, 2018, para. 1.3.3. (20) "The broader tax challenges raised by digitalization". The TFED is the Task Force on Tax and Development. See also art. 162, para. 2, lett. f-bis of the Italian Tax Income Code (T.U.I.R.) as it read since 1 January 2018.

[202] See the case law "Philip Morris" and "Marketplace" described above, Chapter 3, para. 3.1.1. and 3.4.

[203] IMF, *Fiscal Monitor (Fiscal Policy from Pandemic to war)*, Washington D.C., U.S.A., 2022, pp. 1 – 23.

[204] OECD, *Teleworking in the COVID-19 Pandemic: Trends and Prospects*, Paris – Cedex, 2021. See, also, Ker D., P. Montagnier P., Spiezia V. (2021), *Measuring Telework in the COVID-19 pandemic, Digital Economy Papers*, No. 314, OECD Publishing, Paris, in *https://doi.org/10.1787/0a76109f-en.* See, also, OECD/G20, *Inclusive Framework on BEPS*, *Progress report July 2020 – September 2021*, Paris, 2021, pp. 20 – 25.

various forms and stages during most of 2020 due to the COVID-19 pandemic and this situation is expected to continue in 2021”[205].

The unprecedented scenario caused by the pandemic has also spilled over effects on the interpretation of the OECD Model Tax Convention, with particular reference to the “*creation of permanent establishments (i.e. home office, dependent agent PE) and the interruption of construction sites*” (OECD, 2021) [206] which has led many States to adopt exceptional measures of disapplication – considered however temporary, in the reported cases – of the ordinary PE concept, as it is defined, to date, by the Art. 5 of the OECD MT Convention.

The purpose of this Chapter is, then, to verify whether the simple disapplication of the pertinent rules in this regard can be considered sufficient for an effective “*governance*” of such phenomena.

It is also proposed to examine whether or not the experience acquired and the possible continuing state of crisis require the development of a more broaden PE concept, aimed at regulating exceptional situations dependent on force majeure, unforeseeable and prolonged in time – such as, for example, pandemics, wars, etc. – in which the current rules may be automatically suspended, both at international and at domestic level, inviting States to adopt the Mutual Agreement Procedures provided for in the Articles 25 through 29 of the OECD Model Tax Convention and other similar existing instruments, both bilaterally and multilaterally.

4.1.2. The documents issued by the OECD et al during the pandemic.

Several documents have been issued by the main global Organizations (OECD, IMF, UN) to show the spillover effects of the COVID-19 pandemic, from the time of “lockdown” onwards, trying to describe the unprecedented situation, to predict its possible duration and to suggest the possible countermeasures.

Here, due to reasons of space, only a few of these documents will be examined.

They seem of particular importance for the richness of the data and the specificity of the fields of investigation.

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[205] OECD, *Updated guidance on tax treaties and the impact of the COVID-19 pandemic*, Paris-Cedex, 21 January, 2021, Introduction.

[206] OECD*, Updated guidance …*, p. 3.

One of these documents (IMF, 2022) [207] also takes into account the Russian – Ukrainian crisis of March 2022, which broke out immediately after the time when – at least in Western countries, thanks to the production and the mass administration of anti-Covid vaccines – it had been declared the exit from the "lockdown" and the progressive reduction of the other health measures.

The first heavy effect of the pandemic crisis is recorded in trade. The OECD gives details in a report published in March 2022, which reads as follows: "*International trade plunged in 2020 but recovered sharply in 2021 (...) Trade impacts across specific goods, services and trade partners are highly diverse, creating pressures on specific sectors and supply chains. The changes in the trade structure caused by the COVID-19 pandemic in a single year was of a similar magnitude to changes otherwise typically seen over 4-5 years. Substantial imbalances across trade partners and products remained at the end of 2021, and not all of the accumulated losses from the earlier steep declines were recuperated. The heterogeneity of trade impacts and changes in trade flows across products, sources and destinations signifies high uncertainty and adjustment costs, and implies additional incentives for consumers, firms and governments to adopt new — or to intensify existing — risk mitigation strategies*" [208].

The Report, based on data provided by an international observatory (CPB World Trade Monitor, 2022) [209], highlights the collapse in international trade in the period from the second quarter of 2020 to the second quarter of 2021 (Appendix, Figure 7) with non-uniform global effects both with regard to the import-export of individual countries and with regard to the economic sectors concerned (Appendix, Figure 8).

In particular, the production and export of semi-conductors in China and South Korea collapsed in the first quarter of 2020 due to the "*lockdown*" and so-called "*zero-Covid*" policy adopted by the Government of Xi Jinping and subsequently by the entire Far - East, but resumed robustly in the first quarter of 2021. However, this recovery does not reach the United States, Germany and the Netherlands. This happened not because of the increase in duties and the sanctions adopted by the G7 against China, but because in the

[207] IMF, *Fiscal Monitor (Fiscal Policy from Pandemic to war)*, Washington D.C., U.S.A., 2022.
[208] See OECD, *International trade during the COVID-19 pandemic: Big shifts and uncertainty*, Paris-Cedex, 10 March 2022, p, 1.
[209] The CPB is a Research Center (Netherlands Bureau for Economic Policy Analysis) based in Amsterdam (NL) that publishes annual and monthly reports on the performance of international trade. The data reported by the OECD report are more broadly summarized in CPB Memo, Amsterdam, 23 September 2022, p. 4.

same period West countries started to adopt the agreed restrictive measures, similar to those already in force in China[210].

On the other hand, the OECD, based on WTO data, stressed that, in the same period, the level of import-export within the African countries and the Middle East remained almost unchanged (Appendix, Figure 9)[211].

According to the OECD Report, in the G7area (Appendix, Figure 10) there was a similar collapse in the export of goods and services in the period March - August 2020, with a slow recovery in the following period until January 2021. The services sector, however, remained below the pre - pandemic levels until August of the same year[212].

The conclusion drawn by the OECD is that "*The unprecedented heterogeneity of changes in trade flows across products, sources and destinations signifies high uncertainty and adjustment costs, and implies additional incentives for consumers, firms and governments to adopt new — or to intensify existing — risk mitigation strategies. Some firms may want to rethink the resilience and reliability of their supply chains and may decide to try to shorten distances travelled from factories to consumers or internalize larger segments of their value chains within their own corporate structures (e.g. an affiliate supplying a component rather than an external firm). This might contribute to resilience of some supply chains but it might also have negative impacts on productivity and it may not necessarily boost systemic resilience and stability of the global economy*"[213].

With regard to the services sector, the OECD issued a specific report on the so-called "*teleworking*" (OECD, 2021)[214], observing preliminarily how "*the COVID-19 crisis created a sudden need for businesses and their employees to start or increase working from home*".

More in details – according to the Report – "*in Australia, France and the United Kingdom, 47% of employees teleworked during lockdowns in 2020. In Japan, which did not institute a nationwide lockdown, the teleworking rate increased from 10% to 28% between December 2019 and May 2020. Highly digitalized industries, including information and communication services, professional, scientific and technical services as well as financial services, achieved the highest rates of teleworking during the pandemic – over 50% of employees, on average. Teleworking rates during the pandemic*

[210] See OECD, *International trade during the COVID-19 pandemic* ..., p. 3.
[211] See OECD, *International trade during the COVID-19 pandemic* ..., p. 9.
[212] See OECD, *International trade during the COVID-19 pandemic* ..., p. 3.
[213] See OECD, *International trade during the COVID-19 pandemic* ..., p. 13.
[214] OECD, *Teleworking in the COVID-19 Pandemic: Trends and Prospects*, Paris-Cedex, 2021.

were higher among workers in large firms than in small ones, reflecting lower digital uptake among small firms and their specialization in activities less amenable to remote working. Workers with a higher level of qualifications were more likely to telework during the pandemic. In the United States, for instance, teleworking rates for individuals holding a Master's degree or a PhD were fifteen times higher than for the least qualified employees"[215].

The impact of Covid-19 in the advanced economies is detailed *infra* (Appendix, Figure 16)[216].

On the basis of its analysis, OECD concludes that: "*Governments should take appropriate actions to sustain the benefits from telework into the future, by ensuring that businesses and their employees have the flexibility they need to drive economic and social recovery and achieve improved well-being. Relevant policies to achieve these goals pertain to three main areas: supporting complementary investments; helping surmount cultural and legal hurdles; and mitigating potential side effects*"[217].

On its side, the IMF (IMF, 2022)[218] first relates the effects of the pandemic on global trade in goods and services, comparing them, on the one hand, with the recession of 2008 and, on the other, with the restrictive measures (Stringency index) on the movements of people (Appendix, Figures 11, 12)[219] and on the workplace closings (Appendix, Figure 14)[220].

The IMF highlights how "*data covering about 95 percent of global goods trade reveals sizable negative international spillovers to trade from supply disruptions due to domestic lockdowns. These international spillovers accounted for up to 60 percent of the observed decline in trade in the early phase of the pandemic*"[221].

The Fund also analyzes the heterogeneous international spillover effect of lockdowns due to the fiscal response (Appendix, Figure 13), highlighting how the most part of countries gave, generally, a small fiscal response which reflected in "*low teleworkability*", with

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[215] See OECD, *Teleworking in the COVID-19 Pandemic…*, pp. 2 – 3.
[216] The figure is excerpt from OECD, *Teleworking in the COVID-19 Pandemic…*, p. 3.
[217] See, for further details, OECD, *Teleworking in the COVID-19 Pandemic…*, p. 9.
[218] See IMF, *International Trade Spillovers from Domestic COVID-19 Lockdowns*, Washington D.C., June 2022. pp. 2, 24 – 28.
[219] See IMF, *International Trade Spillovers …*, *Abstract*.
[220] See IMF, *International Trade Spillovers*, p. 40.
[221] Particular importance has the counter-factual analysis carried out by the IMF on the effects of the lockdown, translated primarily into the preference of acquiring goods rather than services. See, again, IMF, *International Trade Spillovers…*, p. 18. In this sense, see also GUERRIERI, V., LORENZONI, G., STRAUB, L. and WERNING, I. *Macroeconomic Implications of COVID-19: Can Negative Supply Shocks Cause Demand Shortages?* in *American Economic Review*, 2022, 112 (5), 1437–1474.

particular reference to the textiles, medical, electronics and automotive sectors[222]. Finally, the international spillover effect of lockdowns over time (excluding China as an exporter), are summarized in Appendix, Figure 15[223].

On the basis of these premises and taking into account another exceptional event, just occurred – the invasion of Ukraine by the Russian Federation – the IMF, in its usual annual report (IMF, 2022) [224], highlights the importance of coordinating fiscal policies, to safeguard the economies of the countries affected by the pandemic and the lockdown and support them in their efforts to prevent and manage new pandemics, to combat the inflation caused by the energy crisis and to support sustainable growth, especially in the developing countries[225].

According to the IMF "*Both the pandemic and the war in Ukraine highlight the need for global initiatives to solve global crises. Unilateral actions could worsen the crisis (for example, restricting exports of food could increase risk of food shortages). International cooperation will lead to better solutions to address the risks and costs of energy and food disruptions—including addressing supply constraints. Cooperation is also crucial to better prevent and mitigate potential future pandemics and other health-related crises (...) International coordination on tax matters is needed now more than ever. Recent achievements toward international tax coordination include the agreement in October 2021 under the Organization for Economic Co-operation and Development (OECD)/Group of Twenty (G20) Inclusive Framework to reform the taxation of multinationals*"[226].

However, the IMF acknowledges that the efforts made in the area of attribution and taxation of profits at the global level have so far been insufficient: *"Current outdated arrangements, loosely, split the place of taxation between a headquarters (residence) country (which taxes the foreign "passive" incomes of its multinational affiliates abroad, such as interest income) and a source country where production is located (which taxes the "active" income of the multinational affiliate physically present in the country). This distinction is meant to prevent double taxation when both countries claim to tax a multinational. It is not fit, however, for a digitalized globalized economy, considering it*

[222] See IMF, *International Trade Spillovers…*, pp. 9 - 12.
[223] See, for further details, IMF, *International Trade Spillovers…*, p. 41.
[224] IMF, *Fiscal Monitor. Fiscal Policy from Pandemic to War,* Washington D.C.
[225] IMF, *Fiscal Monitor,* ..., p. 3; 9.
[226] See IMF, *Fiscal Monitor. Fiscal policy from Pandemic to War...*, p. 16; 25.

ignores a third possible location of taxation, namely, that of consumers and users (in the destination, or market, countries)"[227].

These are statements of great relevance, especially in time of Covid-19, and in relation to the effects that the pandemic has produced in the global economy and on the rules that govern it, including those relating to a concept of PE which should take into account of exceptional events such as those just mentioned. Exceptional events that the OECD has not failed to grasp already in the drafting of its "*Updated guidance on tax treaties and the impact of the COVID-19 pandemic*", dated 21 January 2021 and that, in the light of the documents mentioned so far, can now be deepened.

4.1.3. In particular: the OECD "Updated guidance on tax treaties and the impact of the COVID-19 pandemic".

The Guidance is preceded by another document (OECD Secretariat, 2020) [228] which identifies the effects of the pandemic on the international taxation in the following:

a) restrictions on the cross-border movement of persons and other similar measures have physically prevented many workers from performing their duties and functions in the country where they were normally employed;
b) the duration of the restrictions has raised issues about the right to taxation by States that are not the "*residence-countries*" of persons forcibly remaining in their territories, for the salaries and wages that they continue to receive from the foreign companies for which they work;
c) some enterprises and, in particular, the MNEs have expressed concerns about the possibility that their employees physically located in countries other than that of residence and in which they continue to operate in the form of "*home working*" by the effect of Covid-19, can be considered objectively responsible, if not even protagonists, of the creation of a real (*personal*) PE.

In reply to the question raised in letter c), the OECD Secretariat hastens to clarify how it is unlikely that the situation described therein can produce a change in the interpretation of the PE concept, because of its exceptionality and temporariness. Quoting in this regard

[227] See IMF, *Fiscal Monitor. Fiscal policy from Pandemic to War…*, p. 28.

[228] OECD Secretariat, *Analysis of Tax Treaties and the Impact of the Covid-19 Crisis*, Paris – Cedex, 2020, para. 2 – 4.

the para. 18 of the Art. 5 of the Commentary, the Secretariat excludes that a PE may be created in this case[229].

The document, however, admits immediately after that, in some countries, "*the threshold presence required by domestic law (including state/provincial legislation) to register for tax purposes may be lower than those applicable under a tax treaty and may therefore trigger corporate income tax registration requirements*" (Appendix, Table 4) [230] and that if the way in which the work is carried on follows those provided for in the residence-country, the question can be legitimately raised, with reference to the "*Home Office*", as well as to the "*Agency PE*" and even to the "*Construction site* PE"[231].

The aforementioned issues do not appear to have been overcome even in the "*Updated guidance*" published nine months later[232].

In fact, the Guidance takes up the issues already addressed by the Secretariat's Document, namely:

(1) the creation of permanent establishments (i.e. home office, dependent agent PE) and the interruption of construction sites;

(2) changes in residence for entities and individuals and the application of tie-breaker rules to dual residents; and

(3) income from employment, i.e. payments under stimulus packages, stranded workers, cross-border (frontier) workers and teleworking from abroad.

The Guidance returns to the issues already addressed by the Secretariat on the basis of two assumptions:

- ✓ the continuation of restrictive measures to contain the Covid-19 pandemic in several Member States;
- ✓ the uncertainty conditions about the duration of these measures.

Only the issues mentioned under numbers (1) and (3) will be addressed below, for their intimate connection.

With respect to the Secretariat's document, the Guidance provides a thorough overview of the instructions issued by certain Member States (Australia, Austria, Canada,

[229] See OECD Secretariat, *Analysis…*, para. 6 through 13.
[230] In Italy, for instance, the threshold is established in three months. See the Art. 162, para. 3 of T.U.I.R.
[231] See OECD MTC Commentary, Paris-Cedex, 2019, under the Art. 5(5), para. 55.
[232] OECD, *Updated guidance on tax treaties and the impact of the Covid-19 pandemic*, Paris-Cedex, 21 January 2021.

Germany, Greece, Ireland, New Zealand, the United Kingdom and the United States of America) to resolve the issues, at domestic level[233].

Basically, all the Tax Administrations concerned have expressed the opinion that, in view of the exceptional and unforeseeable circumstances resulting from the Covid-19 pandemic, the presence of individuals in a certain State and the fact that they continued to carry on their work outside their residence-country for reasons of force majeure does not in itself entail the creation of a PE in that State by a foreign company, provided that such PE had not been created before the pandemic, and that the unplanned presence of employees in that State is the short-term result of them being temporarily relocated or restricted in their travel because of Covid-19[234].

All the instructions issued also stress the unpredictability of the situation and the impossibility of providing, in a short time, to remove the conditions that may suggest the creation of an undeclared PE, taking advantage of this extraordinary event and of the tax measures adopted accordingly.

Turning to the questions raised in more detail under Nos. (1) and (3) and with specific reference to the "*Home Office*", the Guidance recalls the Art. 5, para. 18 of the OECD 2019 Commentary. According to the Commentary "*even though part of the business of an enterprise may be carried on at a location such as an individual's home office, that should not lead to the conclusion that that location is 'at the disposal' of that enterprise simply because that location is used by an individual (e.g. an employee) who works for the enterprise. The carrying on of intermittent business activities at the home of an employee does not make that home a place at the disposal of the enterprise. A home office may be a PE for an enterprise if it is used on a continuous basis for carrying on business of that enterprise and the enterprise generally has required the individual to use that location to carry on the enterprise's business*"[235].

The Guidance excludes that the situation determined because of the pandemic fulfills the conditions last mentioned and this because it is clear that "*During the COVID-19, individuals who stay at home to work remotely are typically doing so as a result of public health measures: it is an extraordinary event not an enterprise's requirement. Therefore, considering the extraordinary nature of the COVID-19 pandemic, teleworking from home*

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233 See OECD, *Updated guidance…*, para. 9 through 13.

234 See, in particular, *https://www.ato.gov.au/business/international-tax-for-business/working-out-your-residency/*, largely recalled and commented by OECD in its *Updated Guidance*.

235 See OECD, *Updated guidance…*, para. 15.

(i.e. the 'home office') because of an extraordinary event or public health measures imposed or recommended by government would 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. In addition, it still provides an office which in the absence of public health measures is available to the relevant employee. This applies whether the temporary work location is the individual's home or a temporary dwelling in a jurisdiction that is not their primary place of residence"[236].

The Guidance, therefore, concludes, that: "*individuals teleworking from home (i.e. the home office) as a public health measure imposed or recommended by at least one of the governments of the jurisdictions involved to prevent the spread of the COVID-19 virus would not create a fixed place of business PE for the business/employer*"[237].

As far as the concept of "*Agency PE*" is concerned, the Guidance focuses the attention on the moment of the beginning of the activity by the "*agent*".

In brief: "*an employee's or agent's activity in a jurisdiction is unlikely to be regarded as habitual if they are only working at home in that jurisdiction because of an extraordinary event or public health measures imposed or recommended by government*"[238].

The above in accordance with the indications of para. 98 of the Commentary 2019, with reference to the Art. 5(5) of the OECD MTC. The situation would be very different if the employee in question habitually concluded contracts on behalf of the company located in another jurisdiction and had started this activity before the outbreak of the pandemic, since in that case the activity would still be considered "*habitual*" and would not fall within the exception considered by the Guidance[239].

Finally, with reference to the "*Construction site PE*" the Guidance highlights the fact that, in general, a construction site constitutes a PE if its duration is more than twelve months (OECD Model) or six months (UN Model) and that, according to para. 55 of the Commentary to the Art. 5(3) of the OECD MTC, the site does not cease to exist due to temporary interruptions of activity, cause adverse weather events, shortage of raw materials or abstentions from work[240].

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[236] See OECD, *Updated guidance…*, para. 16.
[237] See OECD, *Updated guidance…*, para. 19.
[238] See OECD, *Updated guidance…*, para. 21.
[239] See OECD, *Updated guidance…*, para. 24.
[240] See OECD, *Updated guidance…*, para. 25.

Consequently, a construction site cannot be considered terminated for a "*temporary*" interruption of activity.

However, States may consider that, in the light of the extraordinary situation determined by Covid-19 and of facts and circumstances to be assessed from time to time, certain business transactions interrupted by measures imposed or even only recommended by the countries where the construction site is located constitute an interruption that should be excluded from the calculation of the threshold necessary to consider the construction site as a seat of a PE[241].

Something remains to be said about the issue indicated by No (3), namely the "Income of cross-border workers that cannot perform their work due to Covid-19 restrictions (e.g. wage Subsidies to employers)".

In this regard, the Guidance, quoting the paragraph 2.6. of the Commentary on the Article 15 of the OECD Model, suggests that where a government has stepped in to subsidize the keeping of an employee on a company's payroll during the Covid-19 pandemic despite being unable to work, the income that the employee receives from the employer should be attributable to the place where the employment is used to be exercised.

The Guidance assimilates the related payments to vacation pay, paid sick leave, or paid furlough, on which the employer makes a withholding tax and for which no disputes to be raised in international taxation seem to be raised[242].

In conclusion, where an employee resident in one jurisdiction and who formerly exercised an employment in another jurisdiction receives a Covid-19 related government subsidy from the work jurisdiction to maintain the relationship with the employer, the payment would be attributable to the work jurisdiction under the Article 15 of the OECD Model[243].

These, in a nutshell, are the answers provided by the Guidance to the international tax issues raised by member countries in relation to the Covid-19 pandemic.

At first sight, and postponing the further deepening that will be accomplished in the next para. 4.4. dedicated to the reactions of Academia, it seems that the Guidance has not fully grasped its first goal: to "*provide more certainty to taxpayers during the exceptional period*" of pandemic[244].

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[241] See OECD, *Updated guidance…*, para. 27.
[242] See OECD, *Updated guidance…*, para. 50.
[243] See OECD, *Updated guidance…*, para. 52.
[244] See OECD, *Updated guidance…*, Abstract, third sentence.

Both in terms of PE concept that of income of cross-border workers the document follows the interpretations coming, in general, from the Commentary, reporting for the rest the solutions adopted at domestic level by the concerned countries, explaining that the provisions issued therein have a temporal scope, limited to the duration and to the circumstances of the pandemic crisis and referring, for the rest, the issues raised to the tax policies of the States. This approach did not remain without criticisms.

4.2. The impact of COVID-19 on Tax policy and Administration: a case study.

4.2.1. The impact on Chinese Tax policy and Administration.

In reporting the content of the “Updated Guidance” (OECD, 2021), mention was made of the fact that some OECD countries, aftermath the advent of the pandemic from Covid-19, issued tax instructions at domestic level, so to clarify the controversial points in the interpretation of the tax treaties with regard to the PE definition and to the taxation of “income from employment” and, indeed, the tax policies adopted gave rise to doubts and uncertainties about the rules, then transferred to the OECD.
It has also been seen that the countries mentioned by the “Guidance” are the Western ones, mostly of the G7 area (Canada, United Kingdom, United States of America) and therefore representatives of the advanced economies.
That’s why it seems now appropriate, for the sake of completeness of analysis, to review the instructions issued by the Chinese Tax Administration, if no other reason than China – a member of the OECD/G20 Inclusive Framework on BEPS and of the United Nations Committee of Experts on International Cooperation in Tax Matters – was the first to face the impact of the pandemic on its civil society and therefore on individuals and businesses, either resident or not.
Since the early COVID-19 crisis, non-resident businesses have raised concerns on PE and tax residence risks, which the Chinese State Taxation Administration (STA) has sought to address in a Q&A Notice issued on August 14, 2020.

The notice cross-references the most substantive piece of Chinese Tax guidance on tax treaties (UN and OECD Models) interpretation issued to-date, entry into force in 2010 through STA Circular 75 (LU, 2020)[245].

The first issue the Notice tries to solve is that of the notion of PE as a "*fixed place of business*". Circular 75, drawing on elements of the OECD Model Treaty Commentary, had already clarified that a place of business is relatively fixed, with a certain degree of permanence. It also stated that carrying on activities 'through' a place of business applies to any situation where business activities are carried on at a particular location that is '*at the disposal of the enterprise*'.

In the same interpretative lines, the IRD of the Government of the Hong Kong Special Administrative Region of the People's Republic of China (Hong Kong, 2019)[246], clarified that "*Whether a location may be considered to be 'at the disposal of' an enterprise in such way that it may constitute a 'place of business through which the business of that enterprise is wholly or partly carried on' will depend on that enterprise having the effective power to use that location as well as the extent of the presence of the enterprise at that location and the activities that it performs there*".

However, in explaining the content of the Commentary of the OECD Model TC on this point, both the aforementioned Circular and Notes did not provide any further guidance on the meaning of '*at the disposal*'.

The STA Notice 2020 has clarified that "*intermittent and occasional*" homework activity during the COVID-19 disruption period should not result in fixed place PE. This is in line with the OECD's April 2020 Secretariat's Document and January 2021 OECD Updated Guidance that 'temporary' or 'exceptional' home working should not result in PE, given that it lacks permanency and that home working resulting from government movement and travel restrictions should not be viewed as putting an employee's home '*at the disposal*' of the enterprise[247].

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[245] LU L., *A look at China's COVID-19 guidance on permanent establishment and tax residence*, in *International Tax Review*, 2020, Sept. 2020, *https://www.internationaltaxreview.com/article/2a6a6xqsdyvp89w2pnitc/a-look-at-chinas-covid-19-guidance-on-permanent-establishment-and-tax-residence*.

[246] See Inland Revenue Department of the Government of the Hong Kong Special Administrative Region of the People's Republic of China, Departmental interpretation and practice notes No. 60, July 2019, on Attribution of profits to Permanent establishments in Hong Kong, para. 40.

[247] See Q&A Notice issued on August 14, 2020, issue 9, in http://www.chinatax.gov.cn/chinatax/n810219/n810744/c101520/c101520/c5155584/content.html. The STA also clarifies that "Given that the COVID-19 pandemic will not come to an end in a short period of time, working from home may gradually evolve into a new semi-normal business operation mode, thus the interpretation of "temporary or exceptional" must be assessed according to a case-by-case analysis which

The second issue addressed by the Notice concerns the concept of "*Agency* PE*"*.

In general terms, according to STA, in the context of the COVID-19 crisis, if employees or agents have to work '*temporarily*' from home and conclude contracts in their home for and on behalf of their non-resident employers or principals, which, under normal circumstances, is '*exceptional*', therefore this should not create an agent PE.

This interpretation takes the similar view as the OECD Analysis[248].

However, the Notice considers two exceptions:

- an individual has been conducting activities in China on behalf of an overseas enterprise for a long period of time 'before' the outbreak of the COVID-19;
- an agent shifts to conduct activities on behalf of an overseas enterprise in China on a 'long term basis after the outbreak of COVID-19', has and 'habitually' exercises such authority to conclude contracts on behalf of the overseas enterprise.

It should be noted that in the second scenario, the criteria for "conducting activities on behalf of an overseas enterprise in China on a long term after the outbreak of COVID-19" are not specifically defined. Since the pandemic situation varies around the world, and a relapse is possible yet, the criterion may be subjective to some extent in assessing "temporary" and "long term". The Notice seems, then, not to solve uncertainty in this regard.

As far as the "Construction site PE" concept is concerned, provided that all constructors and managers from certain construction projects depart from the site, because of COVID-19, resulting in a complete shutdown of the construction project, it will not be considered to be "temporary cessation", by STA, which holds that the complete shutdown due to COVID-19 can be excluded in determining the duration of the project.

This interpretation is less restrictive than the OECD analysis, which asserts that temporary interruption of activities on a construction site due to COVID-19 should not be excluded[249].

takes also into account whether or not the working from home had begun before the pandemic or was a consequence of the restrictions on travel movements and of the imposed lockdown".

[248] In its interpretation, the STA refers to the Double Tax Agreement "*between the Government of the People's Republic of China and the Government of the Republic of Singapore for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income*" signed in 2010 and later updated following the Art. 5 (3-5) of the OECD MTC and its Commentary, published in 2019. All the tax treaties signed by China with other countries on the same legal basis are included in the STA Notice dated 14 August 2020 and follow the same address.

[249] See above, under footnote 246.

4.2.2. One case study.

On the basis of the above interpretative lines, some (Feng, Zhang, 2020)[250] have pointed out the concrete possibility of PE risk in relation to specific situations, reporting one case study and suggesting some operational solutions.

In brief: a US University which enrolls students from all over the world is used to employ them, where they are on the campus, as research fellows, paying them through US bank accounts.

However, due to COVID-19 pandemic, many international students have been banned from entering the U.S.A. Among them, some Chinese students were stranded in China.

The US University has two options:

- to let the Chinese students continuing their research assistance, working remotely, and being paid through their US bank accounts;
- to have its wholly foreign-owned enterprise (WFOE) set up in China hire the Chinese students locally.

The first option induces some concerns about the potential PE risk.

According to the aforementioned August 14 2020 China's State Tax Administration (STA) Q&As regarding PE and tax residence risks caused by the COVID-19, temporary home-based work during the epidemic prevention and control period, which is considered an "intermittent and occasional" activity, does not constitute a fixed place PE. In fact, according to the US – China DTA, which provides that "*the furnishing of services (...) within the country for a period or periods aggregating more than six months within any twelve-month period*", students' presence in China does not represent a condition of service PE status in China if it is less than six months within any 12 consecutive months throughout the duration of the employment. However, the burden of proof about duration lies with the US University.

This means that, in general, the measure of the employee's total days (183) resided in China is based on two factors:

- the employment contract, based on which the assessment period of the PE can be traced back to the date of employment;

[250] FENG H., ZHANG Z., *Permanent Establishment Risks in China amid COVID-19: A Case Study*, 2020, inx*https://www.china-briefing.com/news/ways-reduce-tax-risks-china-case-study-permanent-establishment-liability-covid-scenario/*. In fact, the authors reported and analyze one case study proposed by the Dezan, Shira & Associates Legal Office, place in Hong Kong, in their blog "China Briefing", on November 11, 2020.

- the number of days or months the employee stays in China from the start date of the employment contract.

According to Feng and Zhang[251], in order to avoid higher PE risks some points have to be noted.

Firstly, PE can be assessed according to the master contract, thus the assessment period of the service PE in China could be measured from the start date of the master contract. This may increase the potential service PE risk. To mitigate the possible risk, the foreign entity is recommended to split the sub-contract from the master contract and re-sign the contract each year or for each project[252].

Secondly, when determining a PE, the relevant authorities are entitled to look into connected projects, that is, the projects which are sufficiently related to be added together. They may look for connectivity between projects to determine the project continuity, for instance, whether one project provides the foundation for another, or whether the projects are executed or supervised in the same way.

So, DSA suggests US University had better to re-sign the contract with the Chinese students each year and redraw the scope of research work of individual Chinese students, thus to limit US University potential tax liabilities in China.

In brief, the contract should include a clause about the place of employment (making it clear that the work is not being conducted remotely from China or from another country) and a clause that the supervisor must monitor the number of days the students travel in China to "*not exceed*" six months during the duration of the contract.

These clauses can be used to prove that the students' remote work from China is "*occasional*" and is caused by the COVID-19 crisis[253].

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[251] See FENG H., ZHANG Z., *Permanent Establishment Risks in China* ..., p. 5.

[252] It should be noted that, under Chinese Corporation Income Tax (CIT) Law, if a non-resident enterprise has no PE in China, it is only subject to a CIT with a withholding tax rate of 10% on China-sourced income, whilst if a non-resident enterprise has a PE in China or STA asses the constitution of a PE measured from the start date of the master contract, then it will be subject to a CIT of 25% on all of its China-sourced income and on its non-China sourced income that has an actual connection to the PE. See, for further details *https://www.asiabriefing.com/countryguide/china/taxation-and-accounting/corporate-income-tax-in-china*.

[253] See FENG H., ZHANG Z., *Permanent Establishment Risks in China* ..., p. 5.

4.3. The UN Committee of Experts. Report by the Secretariat on Taxation and Coronavirus disease (COVID-19).

The debate developed during the first two years of the COVID-19 pandemic about the interpretation of treaties against double taxation and of the most widespread and recently updated Convention Models (OECD Commentary, 2019; UN MDTC, 2021) could not fail to spill over into the greatest global organization: the United Nations.

Indeed, on 24 March 2022, the Secretariat of the UN "Committee of Experts on International Cooperation in Tax Matters" drew up a document to provide the Committee with updated elements of reflection[254].

Based on the aforementioned existing document developed by the OECD Secretariat (April 2020) on tax treaties and the impact of the COVID-19 pandemic, the UN Committee's Secretariat Report takes up all the issues already discussed by the OECD in the field of international taxation, highlighting that despite the OECD documents, "*there are a number of areas where additional clarification may be necessary regarding the application of the many treaties that are based on the UN Model*"[255] .

Here below will be considered the following:

- ✓ the time thresholds that rely on physical location in the Article 5 on permanent establishment, in the Article 14 on independent personal services and in Article 15 on income from employment;
- ✓ the situation of working from "*home*" or "*remote working*" in the Article 5 and in the Article 15.

The key expression is "*time threshold*" which concerns:

- a building site, a construction, an assembly or installation project or supervisory activities in connection therewith [paragraph 3(a) of the Article 5];
- the furnishing of services, including consultancy services [paragraph 3(b) of the Article 5];
- independent personal services (Article 14);
- income from employment (Article 15),

and represents a potential issue in connection with a permanent establishment[256].

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[254] See United Nations – Committee of Experts on International Cooperation in Tax Matters Twenty-fourth session, Item 3 (1) of the Provisional agenda: *Taxation and Coronavirus disease (COVID-19): pandemic and post-pandemic issues Report by the Secretariat*, New York, March 2022, pp. 4 – 8.

[255] See UN Committee of Experts…, p. 3

[256] See again UN Committee of Experts…, p. 3.

As regard to the first sentence above (a building site etc.), a building site, a construction, assembly or installation project or supervisory activities in connection therewith constitutes a PE only if such site, project or activities last more than six months[257].

According to the UN Model Commentary, such site, project or activities exist from the date on which work begins, including any preparatory work, until the date on which the work is completed or permanently abandoned. Moreover, such site, project or activities should not be regarded as ceasing to exist when work is temporarily discontinued by bad weather, a shortage of material or labor difficulties.

As per above, the issue raised stems from the fact that in the UN Model there is no guidance on whether the periods of interruption, as a result of public health measures imposed or recommended by the government during the COVID-19 crisis, should or should not be excluded from the calculation of the "*time threshold*" for such site, project or activities when deciding whether a PE has been created or not[258].

Finally, the document dreads another potential issue: the one concerning the home working by a dependent agent.

In fact, the Article 5 paragraph 5 of the UN Model, has already stated that a "dependent agent" PE arises where a person habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts, on behalf of a non-resident business. During the COVID-19 pandemic, some employees or agents for non-resident businesses started working from home. The question may arise whether the activities of an individual temporarily working from home for a non-resident employer could give rise to a dependent agent PE.

The documents recall, in this regard, the circumstance that, during the 21st session of the Committee, a footnote was added to paragraph 18 of the Commentary on the Article 5 clarifying that where the employer, due to special circumstances (such as a pandemic), requires employees to work from home rather than to report to the offices that it normally provides to these employees, the "*home office does not create a PE*". Thus – the document concludes – "*a similar clarification could be added with respect to the dependent agent paragraph*"[259].

[257] This is established by paragraph 3(a) of the Article 5 of the UN Model. See also paragraph 28 of the Commentary on the Article 5 of the UN Model, citing paragraph 55 of the Commentary on the Article 5 of the OECD Model as it relates to paragraph 3(*a*) of the Article 5.
[258] See UN Committee of Experts…, p. 5.
[259] See UN Committee of Experts, …, p. 7.

The Secretariat of the Committee proposed to include the mentioned issues and gaps in the 25th Session Agenda (18-21 October 2022), but that Agenda does not offer any points dealing with the COVID-19 pandemic or with discussion concerning additional guidance to the Commentary on the UN Model in this regard.
So, as it occurred for the OECD MTC Model, the UN documents seem to leave the aforementioned issues still unsolved.

4.4. The reactions of the Academia.

The impact of the crisis from COVID-19 in Academia has fueled a remarkable number of comments on the effects that it would have produced in the economy and in the rule system, at global level.
With regard to the subject matter of this work - international taxation and, in particular, the spillover effect of COVID-19 on the PE concept, as it read in the existing Model Tax Conventions - there will be examined, below, those that seem to be the most worth mentioning.
Some scholars (Collier, Pirlot, Vella, June 2020)[260] have focused their attention on the impact of COVID-19 on the global ferment already underway, aimed at reforming the most widespread Convention Models at global level (OECD MTC and UN DTMC) and just updated, on the initiatives already undertaken within the OECD/G20 Inclusive framework about the digitalization of the economy and, on the contrary, about the benefits that could have been achieved by the "online business" (e.g. "Netflix" and "Zoom").
In that regard, the COVID-19 crisis added significant impetus to the focus on the two central themes of the ongoing work of the Inclusive Framework on the digitalization of business, namely the development of a solution to address the digitalization issue (Pillar 1) and the closing of remaining avoidance opportunities (Pillar 2)[261].
Others (Savastano, June 2020)[262] paused, instead, on the domestic effects of the first indications provided by the OECD Secretariat (OECD, April 2020) about the practical spillovers of the pandemic on the major international tax provisions.

[260] COLLIER R., PIRLOT A., VELLA J., *Tax Policy and the COVID-19 Crisis*, in *Intertax,* Vol. 48 (2020), Issue 8/9, pp. 794 – 804.
[261] See COLLIER et al, *Tax Policy and the COVID-19 Crisis…*, p. 803.
[262] SAVASTANO L., *Il COVID-19 non "infetta" le condizioni di esistenza della stabile organizzazione*, 2020, in *https://iltributario.it/articoli/focus/il-covid-19-non-infetta-le-condizioni-di-esistenza-della-stabile-organizzazione.* See, in the same interpretative direction, CRUGLIANO G., *Stabile Organizzazione e Covid-19: quali indicazioni dall'OCSE?* 7 August 2021, in *https://www.iusinitinere.it/stabile-organizzazione-e-covid-19-quali-indicazioni-dallocse-39690.*

In this regard, they focused their attention on the theme of "construction site PE", given that the OECD Secretariat (3 April 2020) confirmed the interpretative guidelines already expressed in paragraph 55 of the OECD Model Tax Convention, with regard to the Art. 5(3) of the Model, in which it is recognized that a construction may suffer physiological interruptions, without however causing them to cease, which can be said to have occurred only when the construction is "*permanently abandoned*"[263].

However, the OECD indications may prove to be particularly penalizing for construction or assembly or installation sites, or for the exercise of supervisory activities connected with those which have been established in countries where the configuration time threshold of a PE is reduced to only 3 months (Appendix, Table 4)[264].

The note issued by the OECD Secretariat also aroused particularly critical positions (Moreno, August 2020)[265], which complained about the lack of realism, being it basically oriented to reassure the OECD member countries that, even after the advent of the COVID-19, nothing had changed in the interpretation of the Model Tax Convention and its Commentary, with particular regard to the creation of a PE, to the Place of Effective Management (POEM), to the treatment of Cross-Border Workers and to the Residence of Individuals.

In the analysis of the risk configuration a PE in time of COVID-19, the recalled critical position notes that the OECD document refers to three very specific issues: (1) employees working from their 'home offices' as possible Article 5(1) fixed place PEs; (2) individuals temporarily working from home as possible Article 5(5) dependent Agent PEs; and (3) the impact of the absence of workers on the existence of Article 5(3) Construction Site PE, each of which deserves an equally specific comment[266].

As to the issue (1) [fixed place of PE related to the '*home workers*'], it is observed that according to the Commentary on the Article 5 of the OECD Model Tax Convention, a home office used on a continuous basis can be understood to be '*at the disposal*' of the

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[263] See OECD Secretariat, *Analysis of Tax Treaties and the Impact of the COVID-19 Crisis,* Paris-Cedex, 3 April 2020, p. 13.

[264] The Annex, Table 4 shows how a total of 39 countries, both OECD (including Italy) and non-OECD have a Construction Permanent Establishment Threshold of three months. As far as Italy is concerned, the threshold is established by the Art. 162, para. 3 of the Income Tax Code (T.U.I.R.).

[265] MORENO BÀEZ A., *Covid-19 and Fiscal Policy. Unnecessary and Yet Harmful: Some Critical Remarks to the OECD Note on the Impact of the COVID-19 Crisis on Tax Treaties*, in *Intertax,* Volume 48, Issue 8/9, 2020, pp. 814 – 830.

[266] MORENO BÀEZ A., *Covid-19 and Fiscal Policy. Unnecessary…*, p. 817.

enterprise if the company has requested the employee to use that location to conduct the enterprise's business[267].

In this context, the note 'hastily'[268] states that, during the COVID-19 crisis, individuals who stay at home to work remotely are typically doing so as a result of government directives, therefore, due to a situation of force majeure and not because of an enterprise's requirement.

However, the lack of a clear and practicable reference to the purpose of the PE concept makes OECD's interpretation a difficult task if it is taken into account that, in a significant number of occasions, it is precisely the purpose of a provision that clarifies which of its possible meanings should prevail in a specific case. It has sometimes been indicated that the purpose of the concept of a permanent establishment is, on the one hand, to provide certainty and, on the other hand, to facilitate control and enforceability of tax liabilities in the source-state.

As to the issue (2) [Agency PE], it seems "surprising" – according to the author – that the note, in the case of the Art. 5(1) of the Model fixed place PEs, acknowledges the possibility of the displacement situation being prolonged over time[269] and does not make the same analysis in respect of possible ex art. 5(5) Dependent Agent PEs. It seems again that the aim of the note is to defend that, 'whatever happens', the displacements due to the pandemic should not change anything.

Finally, as to the issue (3) [Construction Site PE], the author fully shares the note's assertion that a site should not be regarded as ceasing to exist when work is temporarily discontinued, in particular when this is the result of temporary interruptions by the COVID-19 crisis[270].

However, once again, it is observed that in the case of COVID-19 a number of different situations may occur and the solution provided by the Art. 5(3) of the OECD MTC should be coordinated with the other provisions of the same Model or with the ones contained in the UN DTCM where a service PE or fixed base could eventually emerge in the new location of the employees or individual entrepreneurs[271].

And all these possible cases are not considered at all in the OECD Secretariat's note.

[267] See OECD Model Tax Convention Commentary (2019) to the Art. 5 para. 18.

[268] The adverb "hastily" is used by MORENO BÀEZ A. in its comments.

[269] According to MORENO BÀEZ A., this is the only way to explain why, with regard to the Art. 5(1) fixed place PEs, the note also addresses the question of whether or not the home office is available to the taxpayer.

[270] See OECD Secretariat, *Analysis* ..., p. 13.

[271] See MORENO BÀEZ A., *Covid-19 and Fiscal Policy. Unnecessary*..., p. 818 – 22 with particular reference to the number of the examples presented in support of his comment.

More recent observations (Kalonji, February 2022)[272] focus their attention on the theme of the "building site or construction or installation project" as a PE, wondering if, according to the Art. 5(3) of the OECD Model Tax Convention, the duration of this interruption dictated by the Covid-19 pandemic should be taken nevertheless into account for the calculation of the 12-month period necessary for the qualification of a "building site or construction or installation project" as a PE.

The issue is relevant because, according to the "Updated guidance" (OECD, 2021), "*The duration of such an interruption of activities* '*should, however, be included*' *in determining the life of a site and therefore will affect the determination whether a construction site constitutes a PE*", while in its French version the text appears to exclude from the count the interruption due to the pandemic crisis[273].

The fact is – according to the comment – that the OECD Commentary does not provide a clear criterion for what constitutes a "*temporary*" interruption, with the result that States may have differing views on the duration of a "*non-temporary*" interruption, as well as on the other conditions that distinguish it from the examples provided by the Commentary.

The induced conclusion is therefore that, in view of the exceptional circumstances related to the Covid-19 pandemic, and having regard to the factual and circumstantial considerations specific to each case to be examined, certain periods during which operations or work were interrupted or suspended in compliance with public health measures (against Covid-19) dictated by the public authorities of the location of the building site, constitute a type of interruption that 'should be excluded' from the calculation of the duration thresholds applicable to building sites constituting a PE[274].

The observations made so far about the tremendous difficulty of assessing the possible come up of a PE on the basis of a time threshold – as the OECD and UN models and commentaries do – including in it the advent and duration of the pandemic, seem to be

[272] KALONJI TRESOR-GAUTHIER M., *Controversy over the qualification of a "building site or construction or installation project" as a PE in the Covid-19 era,* 2022, in *http://kluwertaxblog.com/2022/02/18/controversy-over-the-qualification-of-a-building-site-or-construction-or-installation-project-as-a-pe-in-the-covid-19-era/.*

[273] In French, it says: "*la durée de cette interruption ne devrait toutefois pas entrer dans le calcul de la durée d'existence d'un chantier et* '*ne devrait donc pas être prise en compte*' *pour déterminer si un chantier de construction constitue* un *établissements stable*". The author, French mother tongue, did not fail to notice the "mismatch".

[274] The conclusion seems to be supported by OECD itself in the Updated Guidance, para. 27.

supported by a recent study on business exits in the time of Covid-19 conducted by the US Federal Reserve (Crane et al, June 2022)[275].

The authors of the paper, comparing the data of the first months of the pandemic emergency (March 2020 - February 2021), with those of the period 2015 - 19 have found that the closure of many activities (business exit) in the considered period was in the United States generally lower than in previous periods, more intense in some sectors and very sudden since the start of lockdown[276].

The last worth mentioning study, in this overview of academic articles, is the one concerning the effects of the pandemic crisis on public finance (Agraval, Bütikofer, November 2022) [277], with particular regard to the so-called "*online shopping*" and to the income tax on the so-called "*teleworking*".

As to the first issue – according to the authors of the study – there is a broad consensus that taxes on online purchases should be sourced to the destination state, e.g., the state where the consumer resides.

Although such a consensus for destination taxation has emerged, the Covid-19 pandemic has highlighted that enforcing consumption taxes on a destination based can be challenging in the presence of e-Commerce. Internationally, for a physical good shipped from another country – especially a country outside of the European Union – enforcement may be difficult, especially in the case of small or informal sellers (*Agency PE, Service PE, Digital PE*). The same is true for small online sellers across state borders within the USA.

In practice, these challenges arise because States adopt thresholds for firms to be required to remit taxes and, moreover, enforcement of these rules for small sellers that are external to the jurisdiction is costly. As a result, more focus on tax administration and the enforcement of remittance rules for commodity taxes are necessary.

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[275] CRANE L.D., DECKER R. A., FLAAEN A., ADRIAN HAMINS-PUERTOLAS A., KURZ C. (Federal Reserve Board), *Business exit during the COVID-19 pandemic: Non-traditional measures in historical context*, June 2022 in *Journal of Macroeconomics*, Volume 72 (2022) 103419, in *https://www.sciencedirect.com/science/article/pii/S0164070422000210?via%3Dihub.*

[276] The reported data (Tables and Figures) are excerpted from the ADP, Automatic Data Processing, an American provider of human resources management software and services. ADP, Inc. ADP Headquarters in Roseland, NJ. Type. Public company. The authors observe: "*Widespread business exit—death—resulting from the Pandemic Recession would have long-lasting consequences for the U.S. economy. Unfortunately, actual business exit is difficult to measure in real time since official statistics on business dynamics are released with substantial lags: Bureau of Labor Statistics (BLS) data on establishment deaths during the first year of the pandemic will become available in mid-2022, and Census Bureau data on firm deaths will likely not be public until 2023*".

[277] AGRAWAL D. R., BÜTIKOFER, *Public Finance in the era of the COVID-19 crisis*, in *International Tax and Public Finance,* 2022, pp. 1349 – 72, in *https://doi.org/10.1007/s10797-022-09769-3.*

As to the second issue ("*teleworking*"), like it is for e-Commerce, Covid-19 made work-from-home commonplace, with survey evidence indicating that it will persist into the future[278].

Then, the question is whether a residence-based or employment-based sourcing rule is most appropriate for the taxation of teleworkers, in tie of Covid-19 and in similar exceptional times and whether the one or the other choice is relevant to determining the constitution of a PE.

Finally – according to the study – the longer-term cross-country effects on inequality resulting from lost human capital development or the pandemic exacerbating pre-existing conditions in labor markets remain uncertain and should be an area of focus in comparative studies of the pandemic.

4.5. The guidelines of the Italian Tax Authorities (ruling no. 458 of July 7, 2021).

In the end of this brief review concerning the impact of the Covid-19 pandemic on the international taxation existing rules, with particular reference to the creation of Permanent establishments, it seems appropriate to mention the directives issued by the Italian Tax Administration (Agenzia delle Entrate), after the issuance of the above mentioned and commented OECD notes in this regard.

It is worth mentioning that the pandemic occurred in the aftermath of the revision of the PE rules contained in the Italian Income Corporation Tax Act (Art. 162, para. 2, let. f-bis T.U.I.R), the elaboration of the concept of PE "*significant and continuous economic presence*", as well as the pertinent case-law evolution already commented on in Chapter 3 of this work.

It was in this period of particular administrative and operational ferment that the Italian Revenue Agency (Agenzia delle Entrate) issued the Ruling No. 458/2021[279], dedicated to the "*Tax treatment of wages and salaries paid to residents and non-residents, operating in 'smart working' mode (home working) during the pandemic, in Italy, instead of in the country where they were already seconded*" (Chiarenza, Grilli; Rossetti, Gatto; Valente A.; 2021)[280].

[278] See AGRAWAL D. R., BÜTIKOFER, *Public Finance in the era of the COVID-19 crisis*, p. 1360.

[279] See Agenzia delle Entrate, Risposta n. 458/2021 on July 7, 2021.

[280] The Ruling has been commented by CHIARENZA F., GRILLI S., *Italian Tax Authorities (ruling no. 458 of July 7, 2021) address the matter concerning the tax treatment of workers that are temporarily in Italy during the Covid-19 pandemic*, 15 July 2021, in

Even though the Ruling does not expressly mention the matter of the Permanent Establishment (and in fact between the norms cited therein it does not recur the aforementioned Art. 162 T.U.I.R.) it is worth mentioning here for the intimate connection of the matter with that concerning the possible PE risk assessment.

The note of the Italian Revenue Service responds to the call from a MNE whose staff is partially composed of employees who carry out their work abroad (*outbound workers*) at the Group's offices and also by employees, Italian and non-Italian citizens, coming from abroad and working in Italy (*inbound workers*).

In particular, it is frequent for the employees of the instant company to carry out their work abroad through the legal institution of the "*secondment*" or through employment contracts of foreign law, with other foreign subsidiaries of the Group.

The sudden international health crisis caused by the spread of Covid-19 has upset the ordinary ways of carrying out work for "*expatriate workers*". The closure of most productive activities in the first months of 2020 and the restrictive measures to the movement of people imposed by the States (i.e. China) to contain the spread of the virus have reduced the possibility of movement and induced companies to adopt flexible working methods (so-called "*smart working*" or "*remote working*").

The exceptional nature of these emergency measures and the interruption of physical mobility have meant that workers have been working for more or less long periods in a different, purely physical place, the contract of employment or secondment.

In particular, the implementation of these strict restrictions has led to some cases of "*forced immobility*" or, on the contrary, the need for sudden returns to the countries of origin, then preventing employees from returning to the place where the activity was ordinarily conducted.

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https://www.gop.it/doc_pubblicazioni/913_2e2m6cjq2v_ita.pdf; ROSSETTI D., GATTO A., *Lavoratori dipendenti bloccati in Italia dalle restrizioni Covid-19: determinazione della residenza fiscale e individuazione dello Stato cui spetta il potere di tassare i redditi prodotti lavorando da remoto*, in *Rivista telematica di Diritto Tributario*, n. 2/2021, pp. 902 – 907, in *https://www.rivistadirittotributario.it/2021/10/29/lavoratori-dipendenti-bloccati-in-italia-dalle-restrizioni-covid-19-determinazione-della-residenza-fiscale-e-individuazione-dello-stato-cui-spetta-il-potere-di-tassare-i-redditi-prodotti-lavorando-da/*; VALENTE A., *Assessing the tax treatment of employees working in Italy during the pandemic*, in *International Tax Review*, July 26, 2021, in *https://www.internationaltaxreview.com/article/2a6a9d8lm8s67f6b4txq8/assessing-the-tax-treatment-of-employees-working-in-italy-during-the-pandemic.*

As per above, the MNE asked the following:

(1) whether, for employees who have spent less than 184 days in Italy in the leap year 2020, the salary for working days in Italy is to be considered as income generated in the territory of the State by non-residents and, as such, it must be taxed in Italy;

(2) whether the employee's stay in Italy for more than 184 days during 2020 has led, in principle, to a change in their status of tax residence;

(3) if the latter employees were to be considered as resident in Italy, whether the taxable basis of employment can be determined by considering the income derived from activities carried out in Italy should be of a "*fictitious foreign-source*", for causes attributable to the emergency health and definable as "*force majeure*", with relative credit worthiness for taxes paid abroad;

(4) what should be the day counting method[281].

Preliminarily, the Agency reports that it has taken into account the two OECD documents on the effects of the pandemic from Covid-19 (OECD Secretariat, 2020, Updated Guidance 2021) on the interpretation of the Model Convention and of the Commentary which, however, have no relevance to the interpretation of the domestic law.

In ruling the case, it therefore complies with the T.U.I.R. (ICTA) and the rules of the Italy - China Convention on double taxation.

As per above, in order to the first question, on the basis of the Article 15 of the Convention and the Article 23 of the T.U.I.R., the Agency is of the opinion that the income from employment received by employees of the applicant Company who reside in China, for the work carried out in Italy, tax also takes over in Italy, pursuant to the Articles 49 and 51, paragraphs 1 through 8, of the T.U.I.R.[282].

In addition, according to the Art. 15 of the Italy – China DTC, the referred income is taxable in both countries.

[281] See Agenzia delle Entrate, Risposta n. 458/2021, p. 4.

[282] The Art. 49, para. 1, of T.U.I.R. reads as follows: "*Income from employment shall be that resulting in respect of employment, with all qualifications, as dependent and under the direction of others, including home working where it is considered to be dependent work in accordance with the rules of labor law*". Art. 51, para. 1, reads as follows: "1. *Income from employment shall consist of all sums and values in general, in whatever form, received during the tax period, including in the form of liberal payments, in relation to the employment. The amounts and values generally paid by employers by the 12th day of January of the tax period following the tax period to which they relate shall also be deemed to have been received during the tax period*".

As a consequence, the issue (1) must be solved on the basis of the Art. 23, para. 3 of the Convention, through the acknowledgement of a deduction (credit method) by Chines Tax Administration on the income tax paid in Italy by the China-resident workers[283].

As to the issue (2), the Agency, in the lack of specific rules which takes into account the effects of the Covid-19, considers, jointly, the Art. 2 of T.U.I.R. and the Art. 4 of the Italy – China Convention, in the light of para. 44 of the OECD Secretariat's note on 3 April 2020.

In brief, where the concerned person avails of a "*permanent home*" in both countries, other criteria should be followed. The residence dispute will be solved by utilizing the "*habitual abode*" criterion.

As to the issue (3), the Agency considers that the workers holding the Italian-resident *status* cannot benefit of the rule provided by the Art. 51, para. 8-bis of the T.U.I.R.[284], since that provision requires their stay abroad for more than 183 days in a period of 12 months, which is not the case described in the request[285].

Finally, as to the issue (4), the Agency considers that the reply to the issue (3) also fits the issue (4), concerning the correctness of the counting method.

Others (Rossetti, Gatto, 2021)[286] arguing from a different orientation (Ruling No 626/2021)[287] expressed by the Italian Revenue Agency on the same subject, noted how the Tax Administration, which would seem formally to take into account the valid

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[283] Art. 23, para 3 of the Agreement between the Government of the Italian Republic and the Government of the People's Republic of China for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income reads as follows: "*In the case of a resident of China: - where a resident of the People's Republic of China derives income from Italy, the amount of tax payable in Italy in respect of that income in accordance with the provisions of this Agreement shall be allowed as a credit against the Chinese tax imposed on that resident. The amount of credit, however, shall not exceed the amount of the Chinese tax computed as appropriate to that income in accordance with the taxation laws and regulations of the People's Republic of China; - where the income derived from Italy is a dividend paid by a company which is a resident of Italy to a company which is a resident of the People's Republic of China and which owns not less than 10% of the shares of the company paying the dividend, the credit shall take into account the tax payable in Italy by the company paying the dividend in respect of its income*".

[284] Art. 51, para. 8-bis of T.U.I.R. (Italian Consolidated Income Tax Act - ICTA) reads as follows: "8-bis. *By way of derogation from the provisions of paragraphs 1 to 8, the income from employment, which is paid continuously abroad and is the exclusive object of the relationship between employees who, over a period of 12 months, stay in the foreign State for a period exceeding 183 days, is determined on the basis of the conventional wages defined annually by the decree of the Minister of Labor and Social Security referred to in article 4, paragraph 1, of Decree-Law No. 317 of 31 July 1987, converted, with amendments, by Law No. 398 of 3 October 1987*".

[285] See Agenzia delle Entrate, Risposta n. 458/2021, p. 14.

[286] See ROSSETTI D., GATTO A., *Lavoratori dipendenti bloccati in Italia dalle restrizioni Covid-19…*, p. 906.

[287] See Agenzia delle Entrate, Ruling No 626/2021 on September 27, 2021 concerning "Tax treatment of the income from employment received by a non-resident who, due to the epidemiological emergency, carries out the work in Italy, in smart working, instead of in the foreign country - articles 49 and 51 of the TUIR".

interpretative support provided by the clarifications of the OECD, didn’t take the chance to provide a systematic organic intervention to resolve the individual cases, as the emergency required, if not at the legislative level (with the adoption of an “*ad hoc*” discipline), at least at the practice level.

In brief – according to the referred opinion – the Italian Revenue Agency should take a position, through general directives, on issues of no immediate solution, to comply hopefully with the interpretations already come up in the OECD framework (Secretariat, Inclusive Framework, Global Forum, etc.).

This last remark seems to be broadly acceptable.

CONCLUSION

A first conclusion that may be stemmed from the overview provided so far on the work conducted in a century of history of international taxation by lawmakers, academics, analysts, tax administrations, international organizations, is that there is no uniquely understood concept of permanent establishment.

The binomial "*material*" PE/ "*personal*" PE produced by the work of the Financial Experts' Committee, appointed by the League of Nations at the aftermath of World War I (1923 - 27) and aimed at searching a compromise between the "*residence-based taxation*" and the "*source-based taxation*" principles, to determine which country should be entitled to tax profits generated abroad, has lost its "*appeal*" over time.

The expansion of the markets, the growth and development of the world trade, the entry of new actors (China, 2001; Russian Federation, 2012) and, above all, of the developing countries into international bodies (WTO, G20) devoted to the "*governance*" of these processes, have made the original PE concept less and less effective.

Hence, the need for a revision of the rules laid down in the existing Models of Tax Convention for the prevention of double taxation on Income and Capital (OECD MTC and UN DTMC) [288] as well as the search of multilateral instruments (OECD/G20 Inclusive Framework) [289] of negotiation and mutual assistance in this regard, became increasingly urgent.

The advent of globalization, the expansion of the global services sector, of the electronic commerce and of the digital economy have introduced into the relevant global debate the concepts of "*service PE*" and "*digital PE*", aimed at solving the crucial question (for the concerned Tax Administrations) of where to locate a "*fixed place of business*" or a "*PE Agency*", when the "*core business*" was (and still is) carried on by an ISP, seated, on behalf of the so-called "GAFAM" [290], in a lower tax jurisdiction.

The BEPS Project launched in 2013 by the OECD/G20, precisely to counter the growing sophistication of tax planners in identifying and exploiting legal arbitrage opportunities and boundaries of acceptable tax planning, thus providing MNEs to open opportunities

[288] See, in particular, the Art. 5(3-8) of the OECD MTC as it read on 21 November 2017 and the Art. 5, para. 3, lett. b) of the United Nations MDTC as it read in September 2021.

[289] See the Art. 10 of the OECD Multilateral Convention to implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting.

[290] GAFAM is the acronym for Google, Apple, Facebook, Amazon, Microsoft, that's to say the major computing companies.

to significantly reduce their tax burden, introduced, on its side, a new PE concept: that of "*significant economic presence*" (OECD Action 1 Report, 2015; OECD/ G20, 2018) [291]. The formula was also poured in the Italian Consolidated Income Tax Act (Art. 162, para. 2, lett. f-bis) T.U.I.R.) under the expression "*significant and continuous economic presence*".

To these concepts, jurisprudence and practice have added in Italy those of "*hidden permanent establishment*" and "*multiple permanent establishment*", aimed either at attracting to the domestic tax law a business activity (and the related income) actually carried on by foreign MNEs on the domestic territory, through a PE, or at facing the impact of globalization on the corporate tax domestic regime[292].

The COVID-19 pandemic and, even more, the Russian-Ukraine war, have completely reversed this process, as widely documented by Figures 7 through 16, exhibited in the Appendix of this work.

OECD highlighted "*unprecedented measures imposed or recommended by governments, including travel restrictions and curtailment of business operations*" [293] and IMF stressed that "*the sudden lockdown and reduction in trade as well as the high energy prices and the shortage of raw materials, including food, have been in effect in most jurisdictions in various forms and stages during the period 2020 - 2021 due to the COVID-19 pandemic and with the advent of the war this situation is expected to continue at least in the months to come*"[294].

In this context, both the OECD Secretariat's "*Analysis*" (2020) and the subsequent "*Updated guidance*" (2021), aimed at reassuring Member States about the modest and entirely temporary tax consequences of the COVID-19 pandemics, have maintained (if not increased) the uncertainty on tax administrations and taxpayers on the reach of PE concept, remitting, on one hand, to individual countries the solution of international

[291] See, OECD/G20, *Tax Challenges Arising from Digitalization Interim-Report*, Paris-Cedex, 2018, para. 1.3.3. (20) "The broader tax challenges raised by digitalization".

[292] See Cass., Sez. V^ Civ., 20 December 2001, (filed on 7 March 2002), Nos. 3367 and 3368.

[293] See OECD, *Tackling Coronavirus (COVID-19): Contributing to a Global Effort, Updated guidance on tax treaties and the impact of the COVID-19 Pandemic*, Paris-Cedex, 2021, Introduction, which recalls OECD Secretariat, *Analysis of Tax Treaties and the Impact of the COVID-19 Crisis,* Paris-Cedex, 3 April 2020, Introduction, para. 1.

[294] Excerpt from IMF, *Fiscal Monitor (Fiscal Policy from Pandemic to war)*, Washington D.C., U.S.A., 2022, pp. 1 – 23. In the same path run United Nations – Committee of Experts on International Cooperation in Tax Matters Twenty-fourth session, Item 3 (1) of the Provisional agenda: *Taxation and Coronavirus disease (COVID-19): pandemic and post-pandemic issues Report by the Secretariat*, New York, March 2022; WTO, *Overview of discussions in the Committee on technical barriers to trade relating to COVID-19*, Geneva, 27 October 2022.

disputes resulting from situations not foreseen and not regulated by the existing tax treaties, and entrusting, on the other hand, the domestic law and "*ad hoc*" measures to perform the function of filling the interpretative gaps still remaining in the international debate, disregarding temporarily and case-by-case the provisions contained in the Models[295].

The reactions of the academic world (Báez Moreno, 2020; Rossetti, Gatto, 2021) [296] and of relevant international bodies (UN, WTO, IMF) [297] seem even obvious, in this regard.

Academia bewailed, on the one hand (Báez Moreno, 2020) [298], the "*hasty approach*" with which the OECD has faced the emergency, constituting the interpretations it has provided nothing but "*an attempt, sometimes almost desperate, to demonstrate that the movements of individuals caused by the pandemic will not alter the final outcome in the application of international tax rules*", while the OECD Secretariat's note "*although correctly identifies two fundamental issues of relevance that impact double tax treaties arising from the pandemic or, rather, from decisions taken by public authorities and private parties as a result of it: (a) the limitation of (international) mobility and the consequent need to perform services from a location other than that of habitual residence; and (b) the emergence of new remuneration schemes as a result of the impossibility of providing such services in the normal manner, neither focuses on the most relevant ones nor provides answers to all of them*".

On the other hand, some (Rossetti, Gatto, 2021)[299] have observed that – though formally taking due note of the legal framework prepared by the OECD in its interpretative "*Updated guidance*" about the effects of COVID-19 on the PE concept and related issues

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[295] See, in this regard, OECD Secretariat 2020 Analysis of Tax Treaties and the Impact of the Covid 19 Crisis, para. 9, which observes: "*During the COVID-19 crisis, individuals who stay at home to work remotely are typically doing so as a result of government directives: it is force majeure not an enterprise's requirement. Therefore, considering the extraordinary nature of the COVID-19 crisis, and to the extent that it does not become the new norm over time, teleworking from home (i.e. the home office) would not create a PE for the business/employer, either because such activity lacks a sufficient degree of permanency or continuity or because, except through that one employee, the enterprise has no access or control over the home office*", and the consequent contradictory interpretation provided, for instance, by the Italian Revenue Agency in its Tax Ruling Nos. 458/2021 and 626/2021 on the taxation of income from employment received by non-resident employees.

[296] MORENO BÀEZ A., *Covid-19 and Fiscal Policy. Unnecessary and Yet Harmful: Some Critical Remarks to the OECD Note on the Impact of the COVID-19 Crisis on Tax Treaties*, in *Intertax,* Volume 48, Issue 8/9, 2020, pp. 814 – 830; ROSSETTI D., GATTO A., *Lavoratori dipendenti bloccati in Italia dalle restrizioni Covid-19: determinazione della residenza fiscale e individuazione dello Stato cui spetta il potere di tassare i redditi prodotti lavorando da remoto*, in *Rivista telematica di Diritto Tributario*, n. 2/2021, pp. 902 – 907.

[297] IMF, *Fiscal Monitor (Fiscal Policy from Pandemic to war)*, Washington D.C., U.S.A., 2022, pp. 1 – 23.

[298] See MORENO BÀEZ A., *Covid-19 and Fiscal Policy…,* pp. 814 – 15.

[299] See ROSSETTI D., GATTO A., *Lavoratori…*, p. 906.

– some Governments and tax administrations, Italy in particular "*have adopted partial when not contradictory rulings and didn't take the chance to provide a systematic organic intervention to resolve the individual cases, as the emergency required, if not at the legislative level (with the adoption of an "ad hoc" discipline), at least at the practice level, through general directives, on issues of no immediate solution*".

As to the international bodies, WTO[300] stressed, on the one hand, the fact that "*The majority (66 per cent) of COVID-19 related notifications were submitted under the urgent notification provisions of the TBT Agreement in response to the urgent problems of health the pandemic caused. Under these notification provisions, WTO members can adopt measures immediately without first notifying the measure in draft form or providing the usual 60-day comment period (or allowing the usual six-month transition period prior to entry into force). A substantial number of the notified measures were reported as 'temporary' (generally applying for a period of six months or one year, or for the duration of the public health emergency). Members also tended to extend their trade facilitating measures beyond the initially notified period of application, in light of the continuing public health emergency*".

United Nations[301], on their side, stressed the fact that "*During Covid 19, force majeure was declared in some countries. This fact may trigger a PE of the enterprises resident in those countries that have projects, such as a building site, a construction, assembly or installation project or supervisory activities in connection therewith if they exceed the threshold set out in the treaty due to the non-delivery of products or raw materials coming from their countries. Thus, the question of the application of tax treaties may be raised in such scenario*". This, in order to take on "*the work forward through the integration of relevant issues identified on taxation and COVID-19 into the work plans on the update of the United Nations Model Double Taxation Convention between Developed and Developing Countries and the Subcommittee on Taxation of the Digitalized and Globalized Economy for the issues related to the interpretation and application of tax treaties*".

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300 WTO, *Overview of discussions in the Committee on technical barriers to trade relating to COVID-19*, Geneva, 27 October 2022. The Technical Barriers to Trade (TBT) Agreement aims at ensuring that technical regulations, standards, and conformity assessment procedures are non-discriminatory and do not create unnecessary obstacles to trade.

301 See United Nations – Committee of Experts on International Cooperation in Tax Matters Twenty-fourth session, Item 3 (1) of the Provisional agenda: *Taxation and Coronavirus disease (COVID-19): pandemic and post-pandemic issues Report by the Secretariat*, New York, March 2022, pp. 7-8.

Finally, IMF[302] highlighted how "*Fiscal policy is operating in a highly uncertain environment, under pressure from a lingering pandemic, the economic consequences of a recently erupted war, and elevated inflation. Just as increasing vaccinations offered hope to many countries, Russia's invasion of Ukraine disrupted the global economic recovery. Both the pandemic and the war in Ukraine highlight the need for global initiatives to solve global crises. Unilateral actions could worsen the crisis. International cooperation will lead to better solutions to address the risks and costs of energy and food disruptions, including addressing supply constraints. Cooperation is also crucial to better prevent and mitigate potential future pandemics and other health-related crises*".

Given these authoritative indications, it appears in its whole evidence the need to revise the PE concept in the sense of introducing in the existing DTC Models a "*safeguard clause*" that takes into account such situations, where exceptional and unpredictable either in their occurrence or in their duration (pandemics, wars, seismic events, climatic upheavals, etc.).

Such a clause should induce the Contracting States to "*disregard*" the ordinary rules and to promote mutual administrative assistance and/or arbitrage procedures aimed at regulating individual cases on the basis of evidence, rather than driven by the need to attract into their tax system any profits that may be generated by a company, assuming that it has carried on a business through a PE, relying – depending on the convenience – on the principle of "*source-based taxation*" or "*residence-based taxation*" to determine who has the right to tax what.

Continuing to make individuals and businesses believe (if not delude) that they will go back to "*as we were*" pre-pandemics or pre-war, does not seem an appropriate approach to achieve that "*legal certainty*" which is instead the basis for the solution of any interpretation dispute.

In such a scenario in which processes and decisions are becoming more and more rapid and, sometimes, overlapping, not intervening in due time or proceeding in an individual and patched up way, could worsen rather than solve crises that seem to follow each other. It is also clear that such a response can only be sought in a multilateral framework, i.e. the OECD, the G20 and the United Nations.

A great economist, Luigi Einaudi[303], already member of that Expert's Committee which, about a century ago, in the League of Nations, drew up the first model of Double Taxation

[302] IMF, *Fiscal Monitor (Fiscal Policy from Pandemic to war)*, Washington D.C., U.S.A., 2022, pp. 1, 16.
[303] EINAUDI L., *Lo scrittoio del Presidente*, Torino, 1956.

Convention, and later the first President-elect of the Italian Republic, had to say: "*In the life of Nations the error of not knowing how to grasp the fleeting moment is usually irreparable*".

His words echo today as a warning, and, at the same time, an exhortation to act.

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APPENDIX

Table 1 – List of OECD Member countries - Ratification of the Convention on the OECD.

No.	Country	Year of Accession
1.	Australia	1971
2.	Austria	1961
3.	Belgium	1961
4.	Canada	1961
5.	Chile	2010
6.	Colombia	2020
7.	Costa Rica	2021
8.	Czech Republic	1995
9.	Denmark	1961
10.	Estonia	2010
11.	Finland	1969
12.	France	1961
13.	Germany	1961
14.	Greece	1961
15.	Hungary	1996
16.	Iceland	1961
17.	Ireland	1961
18.	Israel	2010
19.	Italy	1962
20.	Japan	1964
21.	Korea	1996
22.	Latvia	2016
23.	Lithuania	2018
24.	Luxembourg	1961
25.	Mexico	1994
26.	Netherlands	1961
27.	New Zealand	1973
28.	Norway	1961
29.	Poland	1996
30.	Portugal	1961
31.	Slovak Republic	2000
32.	Slovenia	2010
33.	Spain	1961
34.	Sweden	1961
35.	Switzerland	1961
36.	Türkiye	1961
37.	United Kingdom	1961
38.	United States	1961

Key Partners

- Brazil
- China
- India
- Indonesia
- South Africa

Table 2 – Members of the OECD/G20 Inclusive Framework on BEPS (updated November 2021).

1. Albania
2. Andorra
3. Angola
4. Anguilla
5. Antigua and Barbuda
6. Argentina
7. Armenia
8. Aruba
9. Australia
10. Austria
11. The Bahamas
12. Bahrain
13. Barbados
14. Belarus *(Suspended)*
15. Belgium
16. Belize
17. Benin
18. Bermuda
19. Bosnia and Herzegovina
20. Botswana
21. Brazil
22. British Virgin Islands
23. Brunei Darussalam
24. Bulgaria
25. Burkina Faso
26. Cabo Verde
27. Cameroon
28. Canada
29. Cayman Islands
30. Chile
31. China (People's Republic of)
32. Colombia
33. Congo
34. Cook Islands
35. Costa Rica
36. Côte d'Ivoire
37. Croatia
38. Curaçao
39. Czech Republic
40. Democratic Republic of the Congo
41. Denmark
42. Djibouti
43. Dominica
44. Dominican Republic
45. Egypt
46. Estonia
47. Eswatini
48. Faroe Islands
49. Finland
50. France
51. Gabon
52. Georgia
53. Germany
54. Gibraltar
55. Greece
56. Greenland
57. Grenada
58. Guernsey
59. Haiti
60. Honduras
61. Hong Kong, China
62. Hungary
63. Iceland
64. India
65. Indonesia
66. Ireland
67. Isle of Man
68. Israel
69. Italy
70. Jamaica
71. Japan
72. Jersey
73. Jordan
74. Kazakhstan
75. Kenya
76. Korea
77. Latvia
78. Liberia
79. Liechtenstein
80. Lithuania
81. Luxembourg
82. Macau, China
83. Malaysia
84. Maldives
85. Malta
86. Mauritania
87. Mauritius
88. Mexico
89. Monaco
90. Mongolia
91. Montenegro
92. Montserrat
93. Morocco
94. Namibia
95. Netherlands
96. New Zealand
97. Nigeria
98. North Macedonia
99. Norway
100. Oman
101. Pakistan
102. Panama
103. Papua New Guinea
104. Paraguay
105. Peru
106. Poland
107. Portugal
108. Qatar
109. Romania
110. Russian Federation *(Suspended)*
111. Saint Kitts and Nevis
112. Saint Lucia
113. Saint Vincent and the Grenadines
114. Samoa
115. San Marino
116. Saudi Arabia
117. Senegal
118. Serbia
119. Seychelles
120. Sierra Leone
121. Singapore
122. Slovak Republic
123. Slovenia
124. South Africa
125. Spain
126. Sri Lanka
127. Sweden
128. Switzerland
129. Thailand
130. Togo
131. Trinidad and Tobago
132. Tunisia
133. Türkiye
134. Turks and Caicos Islands
135. Ukraine
136. United Arab Emirates
137. United Kingdom
138. United States
139. Uruguay
140. Viet Nam
141. Zambia

Note: For more information on the OECD/G20 Base Erosion and Profit Shifting Project, visit *www.oecd.org/tax/beps/about.*

Table 3 - Signatories and Parties to the Multilateral Convention to implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting status as of 10 November 2022.

No	Jurisdiction	Signature	Deposit of Instrument of Ratification, Acceptance or Approval	Entry into Force	Notifications made pursuant to Article 35(7)(b) of the MLI	Notifications made after becoming a Party	Arbitration Profile
1	Albania	28-05-2019	22-09-2020	01-01-2021			
2	Andorra	07-06-2017	29-09-2021	01-01-2022			28-06-2022
3	Argentina	07-06-2017					
4	Armenia	07-06-2017					
5	Australia	07-06-2017	26-09-2018	01-01-2019		02-10-2020	28-06-2022
6	Austria	07-06-2017	22-09-2017	01-07-2018			28-06-2022
7	Bahrain	27-11-2020	23-02-2022	01-06-2022			
8	Barbados	24-01-2018	21-12-2020	01-04-2021			25-03-2021
9	Belgium	07-06-2017	26-06-2019	01-10-2019		25-11-2021	28-06-2022
10	Belize	11-01-2019	07-04-2022	01-08-2022			
11	Bosnia and Herzegovina	30-10-2019	16-09-2020	01-01-2021			
12	Bulgaria	07-06-2017	16-09-2022	01-01-2023			
13	Burkina Faso	07-06-2017	30-10-2020	01-02-2021			
14	Cameroon	11-07-2017	21-04-2022	01-08-2022			
15	Canada	07-06-2017	29-08-2019	01-12-2019		08-10-2020	28-06-2022
16	Chile	07-06-2017	26-11-2020	01-03-2021			
17	China (People's Republic of)	07-06-2017	25-05-2022	01-09-2022			
18	Colombia	07-06-2017					
19	Costa Rica	07-06-2017	22-09-2020	01-01-2021			
20	Côte d'Ivoire	24-01-2018					
21	Croatia	07-06-2017	18-02-2021	01-06-2021			
22	Curaçao	20-12-2017 [1]	29-03-2019	01-07-2019			25-03-2021
23	Cyprus	07-06-2017	23-01-2020	01-05-2020			
24	Czech Republic	07-06-2017	13-05-2020[2]	01-09-2020			
25	Denmark	07-06-2017	30-09-2019	01-01-2020		29-06-2021	
26	Egypt	07-06-2017	30-09-2020	01-01-2021			
27	Estonia	29-06-2018	15-01-2021	01-05-2021	01-06-2022		
28	Fiji	07-06-2017					25-03-2021
29	Finland	07-06-2017	25-02-2019	01-06-2019			28-06-2022
30	France	07-06-2017	26-09-2018	01-01-2019		22-09-2020	16-09-2022
31	Gabon	07-06-2017					
32	Georgia	07-06-2017	29-03-2019	01-07-2019			
33	Germany	07-06-2017	18-12-2020	01-04-2021			28-06-2022
34	Greece	07-06-2017	30-03-2021	01-07-2021			25-03-2021
35	Guernsey	07-06-2017	12-02-2019	01-06-2019			
36	Hong Kong (China)	07-06-2017	25-05-2022	01-09-2022			
37	Hungary	07-06-2017	25-03-2021	01-07-2021			28-06-2022
38	Iceland	07-06-2017	26-09-2019	01-01-2020		14-12-2021	
39	India	07-06-2017	25-06-2019	01-10-2019			
40	Indonesia	07-06-2017	28-04-2020	01-08-2020	10-11-2022		
41	Ireland	07-06-2017	29-01-2019	01-05-2019			25-03-2021
42	Isle of Man	07-06-2017	25-10-2017	01-07-2018			
43	Israel	07-06-2017	13-09-2018	01-01-2019			
44	Italy	07-06-2017					28-06-2022
45	Jamaica	24-01-2018					
46	Japan	07-06-2017	26-09-2018	01-01-2019		21-04-2022	28-06-2022
47	Jersey	07-06-2017	15-12-2017	01-07-2018			
48	Jordan	19-12-2019	29-09-2020	01-01-2021			
49	Kazakhstan	25-06-2018	24-06-2020	01-10-2020		26-11-2020	
50	Kenya	26-11-2019					
51	Korea	07-06-2017	13-05-2020	01-09-2020			
52	Kuwait	07-06-2017					
53	Latvia	07-06-2017	29-10-2019	01-02-2020		20-04-2021	

Following Table 3

No	Jurisdiction	Signature	Deposit of Instrument of Ratification, Acceptance or Approval	Entry into Force	Notifications made pursuant to Article 35(7)(b) of the MLI	Notifications made after becoming a Party	Arbitration Profile
54	Lesotho	09-02-2022	28-07-2022	01-11-2022			28-06-2022
55	Liechtenstein	07-06-2017	19-12-2019	01-04-2020			25-03-2021
56	Lithuania	07-06-2017	11-09-2018	01-01-2019			
57	Luxembourg	07-06-2017	09-04-2019	01-08-2019			28-06-2022
58	Malaysia	24-01-2018	18-02-2021	01-06-2021		10-11-2022	
59	Malta	07-06-2017	18-12-2018	01-04-2019			28-06-2022
60	Mauritius	05-07-2017 [3]	18-10-2019	01-02-2020			28-06-2022
61	Mexico	07-06-2017					
62	Monaco	07-06-2017	10-01-2019	01-05-2019			
63	Mongolia	06-10-2022					
64	Morocco	25-06-2019					
65	Namibia	30-09-2021					
66	Netherlands	07-06-2017	29-03-2019	01-07-2019		25-11-2021	25-03-2021
67	New Zealand	07-06-2017	27-06-2018	01-10-2018			25-03-2021
68	Nigeria	17-08-2017					
69	North Macedonia	29-01-2020					
70	Norway	07-06-2017	17-07-2019	01-11-2019			
71	Oman	26-11-2019	07-07-2020	01-11-2020			
72	Pakistan	07-06-2017	18-12-2020	01-04-2021			
73	Panama	24-01-2018	05-11-2020	01-03-2021			
74	Papua New Guinea	23-01-2019					28-06-2022
75	Peru	27-06-2018					
76	Poland	07-06-2017	23-01-2018	01-07-2018			
77	Portugal	07-06-2017	28-02-2020	01-06-2020			25-03-2021
78	Qatar	04-12-2018	23-12-2019	01-04-2020		25-11-2021	
79	Romania	07-06-2017	28-02-2022	01-06-2022			
80	Russian Federation	07-06-2017	18-06-2019	01-10-2019	21-10-2021		
81	San Marino	07-06-2017	11-03-2020	01-07-2020			
82	Saudi Arabia	18-09-2018	23-01-2020	01-05-2020			
83	Senegal	07-06-2017	10-05-2022	01-09-2022			
84	Serbia	07-06-2017	05-06-2018	01-10-2018			
85	Seychelles	07-06-2017	14-12-2021	01-04-2022			
86	Singapore	07-06-2017	21-12-2018	01-04-2019		11-08-2021	28-06-2022
87	Slovak Republic	07-06-2017	20-09-2018	01-01-2019			
88	Slovenia	07-06-2017	22-03-2018	01-07-2018			28-06-2022
89	South Africa	07-06-2017	30-09-2022	01-01-2023			
90	Spain	07-06-2017 [4]	28-09-2021	01-01-2022	01-06-2022		25-03-2021
91	Sweden	07-06-2017	22-06-2018	01-10-2018			25-03-2021
92	Switzerland	07-06-2017	29-08-2019	01-12-2019	18-12-2020		28-06-2022
93	Thailand	09-02-2022	31-03-2022	01-07-2022			
94	Tunisia	24-01-2018					
95	Türkiye	07-06-2017 [5]					
96	Ukraine	23-07-2018	08-08-2019	01-12-2019			
97	United Arab Emirates	27-06-2018	29-05-2019	01-09-2019			
98	United Kingdom	07-06-2017	29-06-2018	01-10-2018			28-06-2022
99	Uruguay	07-06-2017	06-02-2020	01-06-2020			
100	Viet Nam	09-02-2022					

The following jurisdictions have expressed their intent to sign the Convention:

- Algeria
- Eswatini
- Lebanon

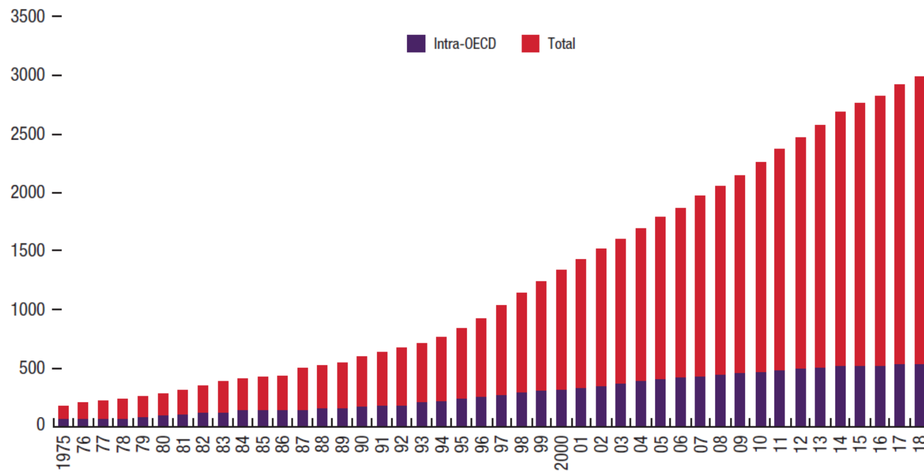
Table 4 - Construction Permanent Establishment Threshold in Tax Treaties

	Two Non-OECD	OECD and Non-OECD	Two OECD
No threshold	1	1	0
3 months	26	13	0
4 months	2	1	0
5 months	1	1	0
6 months	391	337	57
7 months	1	0	0
8 months	7	2	0
9 months	131	130	14
10 months	0	1	1
12 months	190	328	150
15 months	0	1	0
18 months	9	5	0
24 months	1	0	2

Source: IMF staff based on Wijnen and De Goede (2014).
Note: Covers 1,811 tax treaties concluded between April 1997 and January 2013.

Figure 1 - Development of Worldwide Tax Treaty Network

Number of Tax Treaties

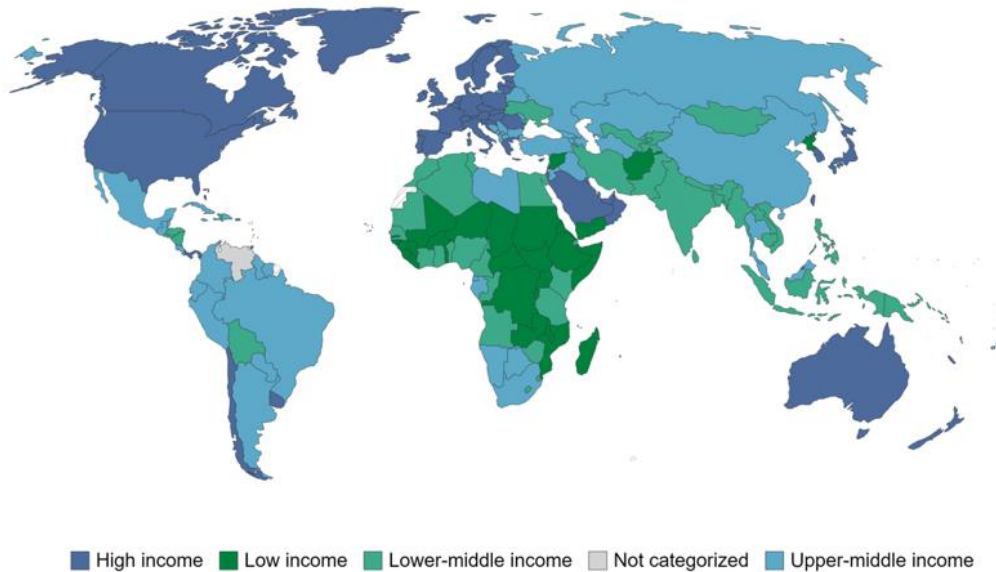


Source: IMF staff based on IBFD data.

Figure 2 – World Income Groups Map

World Bank income groups, 2021

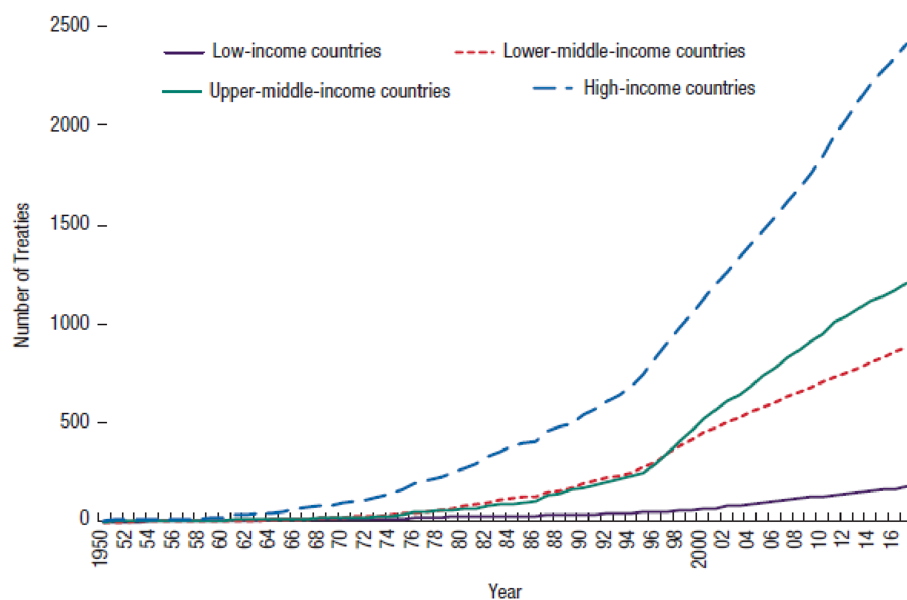
The World Bank's income classifications split countries into one of four categories determined by the country's gross national income (GNI) per capita in US$. The GNI thresholds between income groups has changed through time based on World Bank definitions.



Source: World Bank

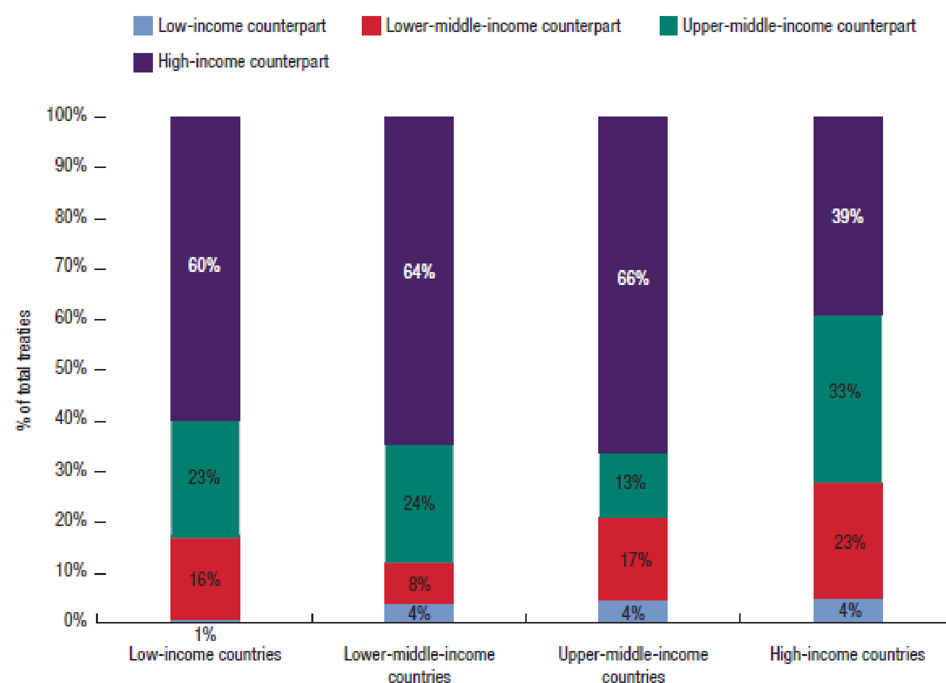
CC BY

Figure 3 - Total Number of Tax Treaty in Force by Country Income Group



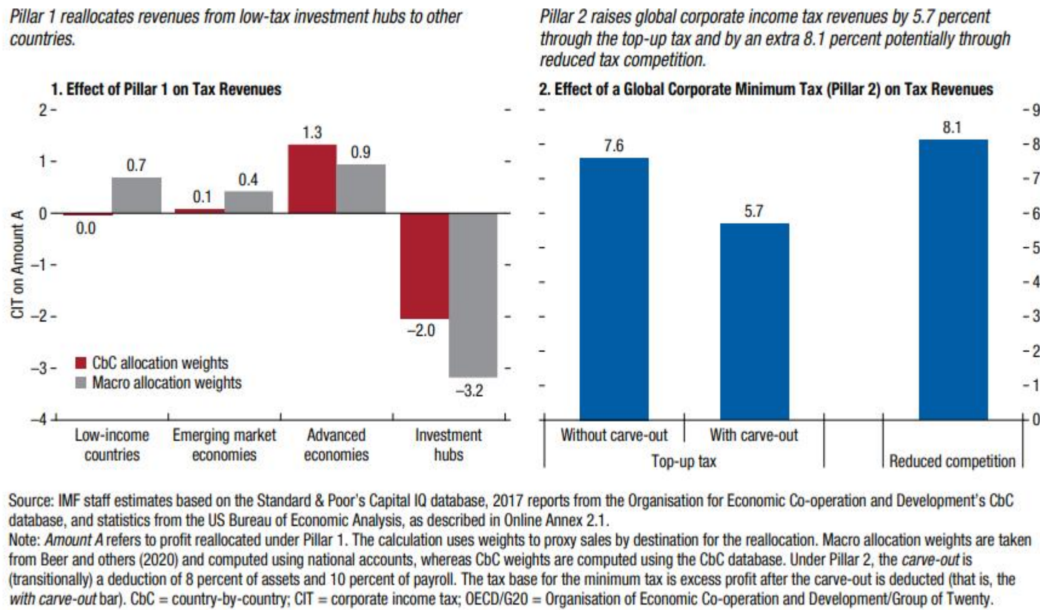
Source: IMF staff based on IBFD data.
Note: Cumulative number of tax treaties concluded where at least one of the contracting states is part of a given country income group. There is, therefore, duplication of treaties where contracting states are part of different income groups.

Figure 4 - Tax Treaty in Force, by Counterpart Country Income Group (Year 2021)



Source: IMF staff based on IBFD data.

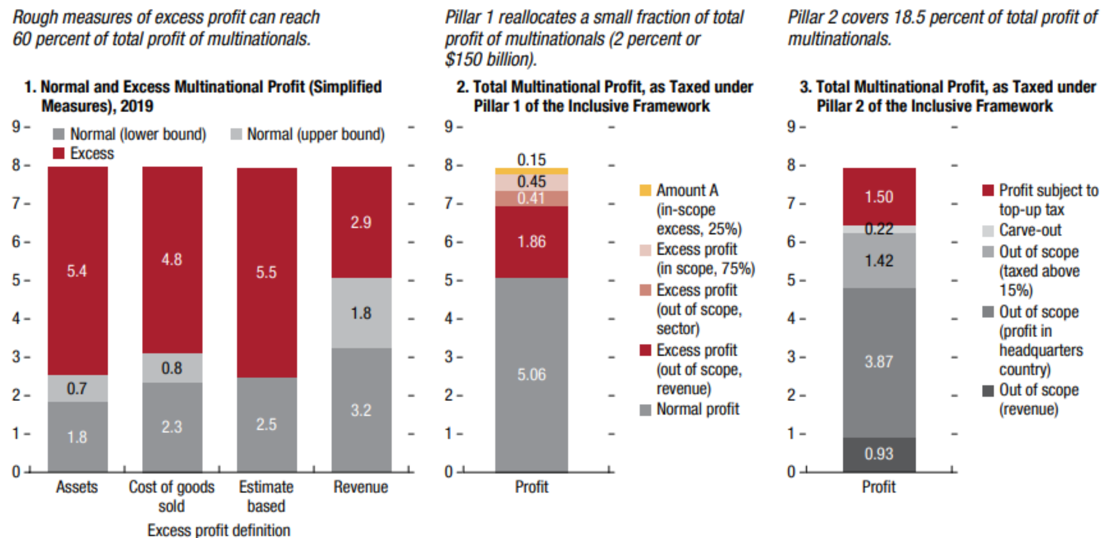
Figure 5 – Revenue Effects of the OECD/G20 Inclusive Framework Agreement, Pillars 1 and 2 (*Percent of current global income tax*).



Source: IMF staff estimates based on the Standard & Poor's Capital IQ database, 2017 reports from the Organisation for Economic Co-operation and Development's CbC database, and statistics from the US Bureau of Economic Analysis, as described in Online Annex 2.1.
Note: *Amount A* refers to profit reallocated under Pillar 1. The calculation uses weights to proxy sales by destination for the reallocation. Macro allocation weights are taken from Beer and others (2020) and computed using national accounts, whereas CbC weights are computed using the CbC database. Under Pillar 2, the *carve-out* is (transitionally) a deduction of 8 percent of assets and 10 percent of payroll. The tax base for the minimum tax is excess profit after the carve-out is deducted (that is, the *with carve-out* bar). CbC = country-by-country; CIT = corporate income tax; OECD/G20 = Organisation of Economic Co-operation and Development/Group of Twenty.

Note: Excerpt from IMF, *Fiscal Monitor – Coordinating Taxation Across Borders*, Washington D.C., April 2022, p. 31.

Figure 6 – Disaggregation of Total Profit of Multinational Corporations (*Trillions of US Dollars*).

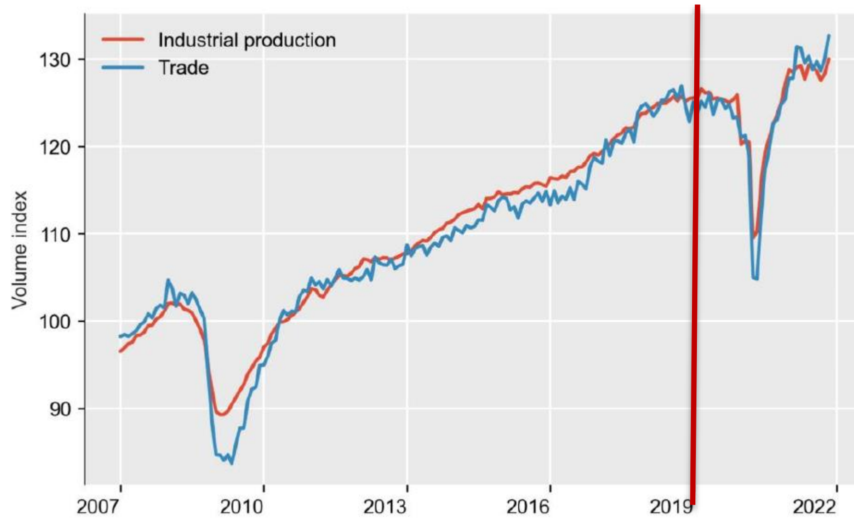


Source: IMF staff estimates, as described in Online Annex 2.1.
Note: These analyses use the Standard & Poor's Capital IQ database. Panel 1 shows empirical proxies for normal and excess profit across four simplifying measures (5.0–7.5 percent of total assets; 5.0–7.5 percent of costs of goods sold; estimate-based model using econometric specifications as specified in Online Annex 2.1; and 5.0–10 percent of revenue). *Amount A* refers to profit reallocated under Pillar 1. Panels 2 and 3 disaggregate total multinational profit into amounts included and excluded in Pillar 1 and Pillar 2, respectively. The *carve-out* is (transitionally) a deduction of 8 percent of assets and 10 percent of payroll. *Out-of-scope (revenue)* refers to companies below the revenue thresholds to be included under Pillars 1 or 2, whereas *out-of-scope (sector)* refers to excluded regulated financial and extractive sectors under Pillar 1. In panel 3, *out-of-scope (profit in headquarters country)* is the sum of profits that multinationals reported in their headquarters countries, and hence are not subject to the income inclusion rule of Pillar 2.

Note: Excerpt from IMF, *Fiscal Monitor – Coordinating Taxation Across Borders*, Washington D.C., April 2022, p. 30.

Figure 7 - International spillover effect of COVID-19 on volume of world trade and industrial production.

Seasonally adjusted (2010=100)

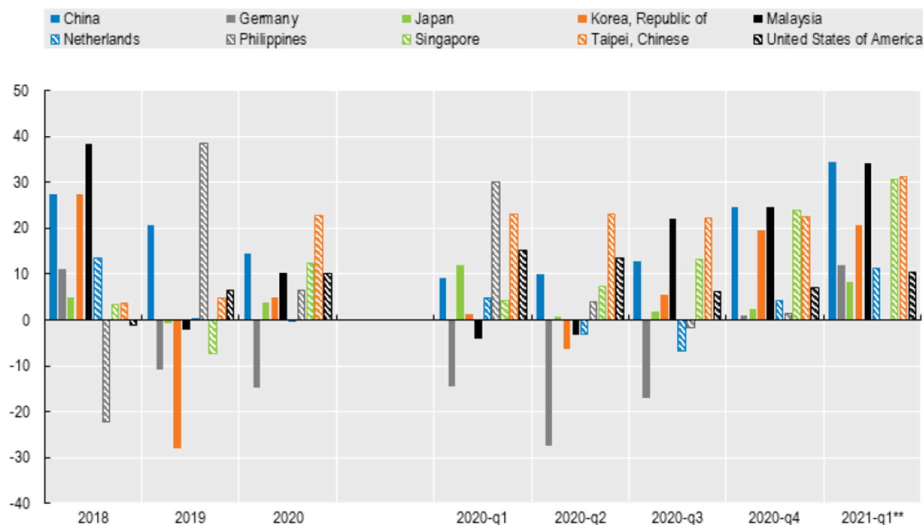


Source: OECD calculations based on CPB World Trade Monitor.

Note: Excerpt from OECD, *International trade during the COVID-19 Pandemic: Big shifts and uncertainty*, Paris – Cedex, 10 March 2022, p. 2, focusing the 2019 – 2022 time period.

Figure 8 - Supply of semiconductors (HS-8542) during the COVID-19 pandemic (10 largest suppliers).

Year-on-year growth rates (%) in the value of exports to all countries by source country

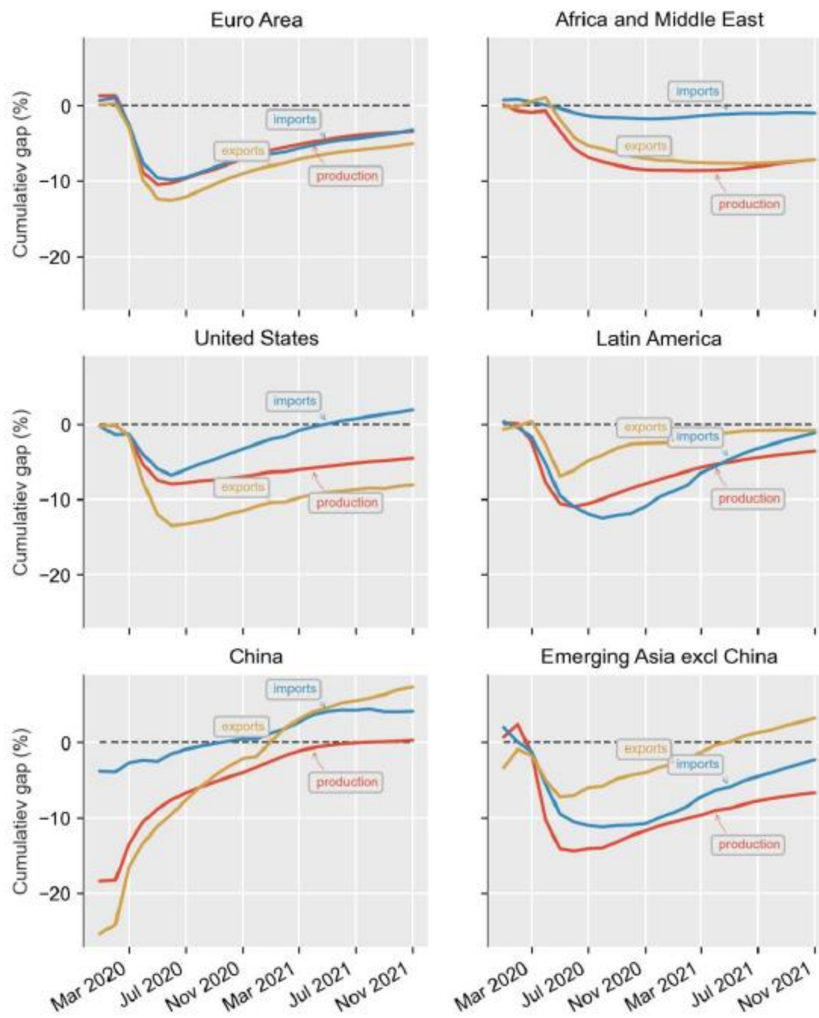


Note: The ranking of the world's largest world suppliers is based on world export shares in 2019.
** The first 'quarter' of 2021 covers the period Jan-April 2021 and the comparison is with the period Jan-Apr 2020.
Source: Authors' calculations based on ITC's Trade Map database.

Note: Excerpt from OECD, *International trade during the COVID-19 Pandemic: Big shifts and uncertainty*, Paris – Cedex, 10 March 2022, p. 5, focusing the 2018 – 2021 time period.

Figure 9 - Trade and production gaps, major traders in the time of COVID-19.

Gaps relative to trend

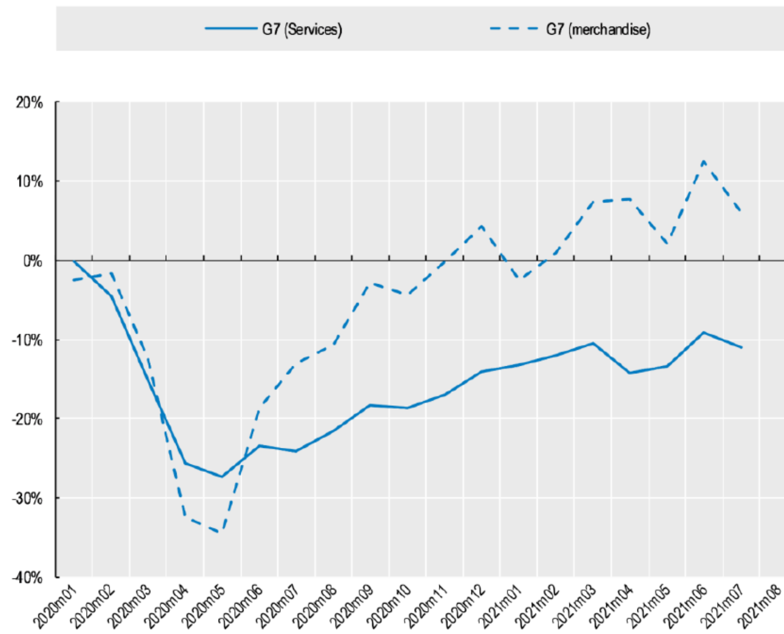


Note: Data include intra-regional trade.
Source: OECD calculations based on CPB World Trade Monitor.

Note: Excerpt from OECD, *International trade during the COVID-19 Pandemic: Big shifts and uncertainty*, Paris – Cedex, 10 March 2022, p. 9.

Figure 10 - Exports of services and merchandise relative to same month in 2019. G7 economies.

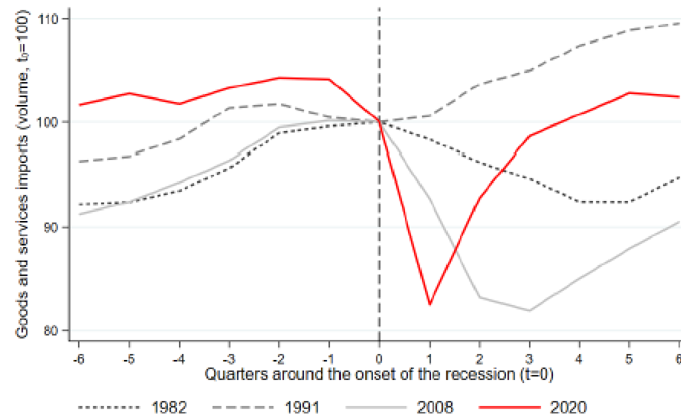
Exports of services and merchandise relative to same month in 2019. G7 economies



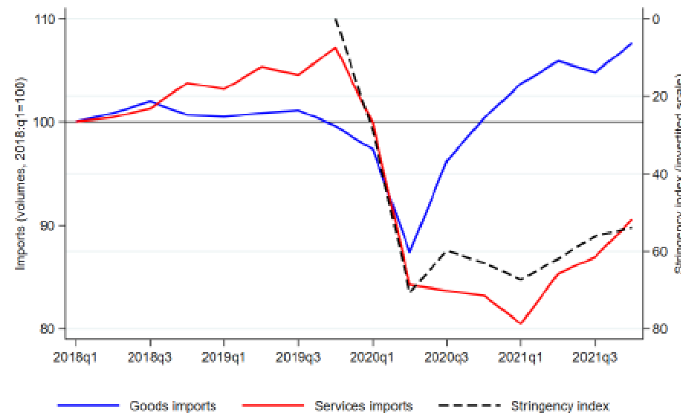
Source: OECD calculations using WTO data in current USD.

Note: Excerpt from OECD, *International trade during the COVID-19 Pandemic: Big shifts and uncertainty*, Paris – Cedex, 10 March 2022, p. 3.

Figure 11 – Trade in the pandemic.



(a) Trade around global recessions

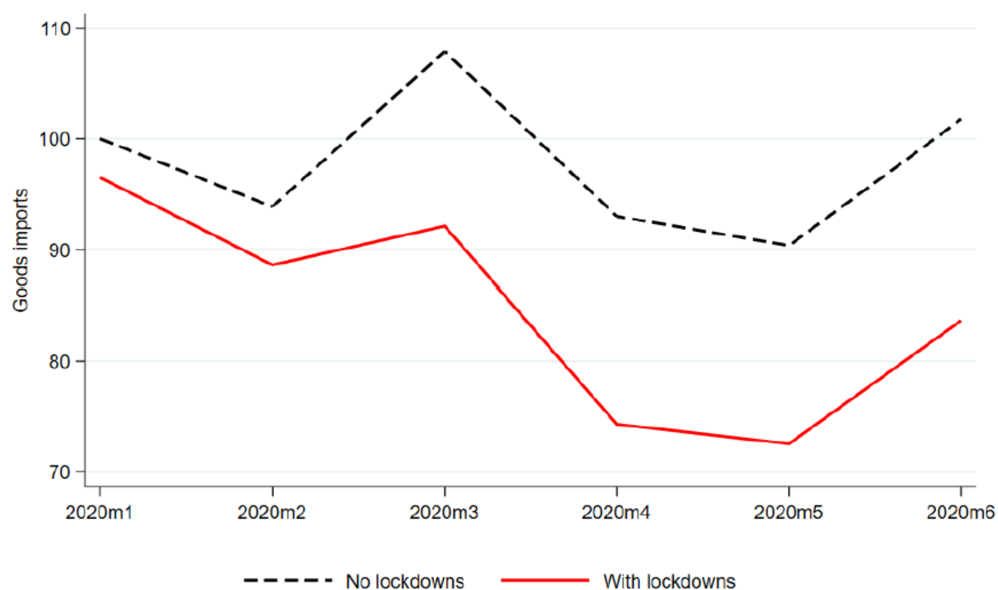


(b) Trade in goods and services during the pandemic

Notes: Panel A plots the evolution of real imports of goods and services for 12 quarters around global recessions, as dated by Kose *et al.* (2020). Real imports are set to 100 in the initial quarter of the recession. Quarterly imports data are from the IMF World Economic Outlook. Panel B plots global trade in goods and services between 2018:q1 and 2021:q4. Quarterly volumes of goods and services imports, taken from CPB World Trade Monitor, are normalized at 100 in 2018:q1. The dashed line plots the world import-weighted average of the Oxford COVID-19 Government Response Stringency Index (Hale *et al.*, 2021).

Note: Excerpt from IMF, *International Trade Spillovers from Domestic COVID-19 Lockdowns*, Washington D.C., 2022, p. 24. The "Stringency Index" is a composite measure based on nine response indicators including school closures, workplace closures, travel bans rescaled to a value from 0 to 100 (100 = strictest). The CPB World Trade Monitor (WTM) is an instrument for bringing together, aggregating, and summarizing worldwide monthly data on international trade and industrial production.

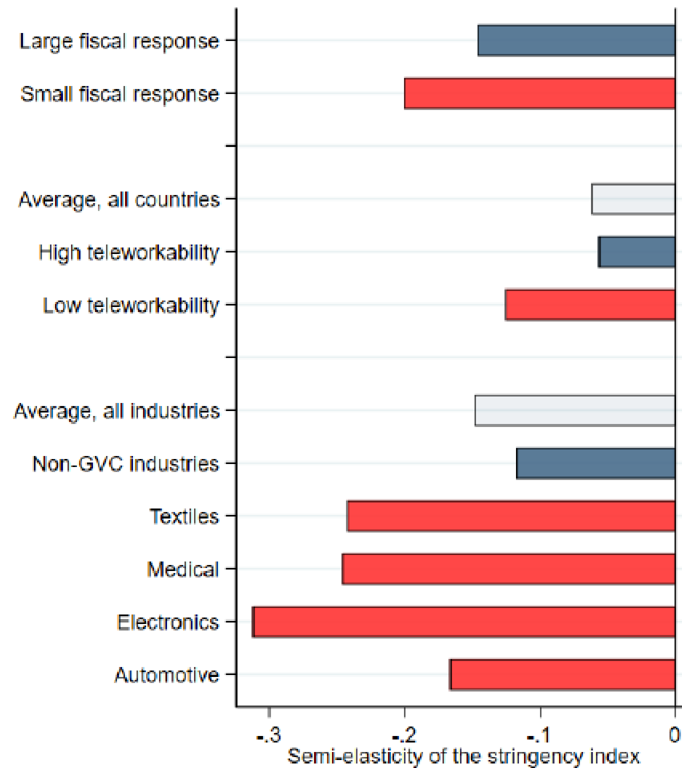
Figure 12 – Quantifying the international spillover effect of lockdowns.



Notes: The chart plots the evolution of good imports under a counterfactual without any containment policy in place in trade partner countries. The counterfactual of no lockdown (dashed line) is obtained using the results reported in Table 4 (column 6) and imposing a value of zero for the Stringency index over the entire period. The solid line plots the actual evolution of imports (in the same sample) in percent of the value with no lockdown in January 2020. Goods imports are measured in percent of predicted value with no lockdown in January 2020.

Note: Excerpt from IMF, *International Trade Spillovers from Domestic COVID-19 Lockdowns*, Washington D.C., 2022, p. 28. The “Stringency Index” is a composite measure based on nine response indicators including school closures, workplace closures, travel bans rescaled to a value from 0 to 100 (100 = strictest).

Figure 13 - The heterogeneous international spillover effect of lockdowns due to the fiscal response.

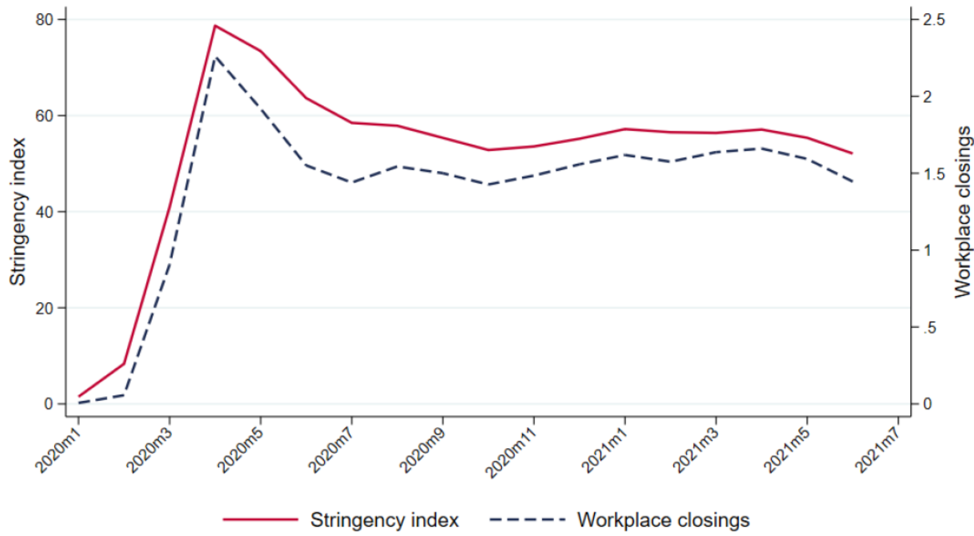


Notes: The chart plots the semi-elasticity of the stringency index separately for: 1) trade partners which have annnounced and implemented high and low discrectionary fiscal measures in response to the pandemic between January and June 2020 (fiscal spending is scaled by GDP and the sample is split along the first quartile of the distribution of fiscal spending over GDP); 2) trade partners with high and low values of the teleworkability index, as computed by Dingel and Neiman (2020) (the sample is split along the first quartile of the distribution of the index; the average value is smaller than in the overall sample as the sample is different from the baseline); and 3) for goods in GVC-intensive industries (Automotive, electronics, medical, textiles) and in non-GVC-intensive ones. The semi-elasticities are computed based on the results reported in Table 4 (columns 7-10, respectively).

Note: Excerpt from IMF, *International Trade Spillovers from Domestic COVID-19 Lockdowns*, Washington D.C., 2022, p. 29. The “Stringency Index” is a composite measure based on nine response indicators including school closures, workplace closures, travel bans rescaled to a value from 0 to 100 (100 = strictest). Fiscal response means the fiscal measures adopted by the Governments to maintain or even increase entities’ ability to meet their current and future obligations.

Abbreviations: GDP stands for Gross Domestic Product; GVC stands for Global Value Chain.

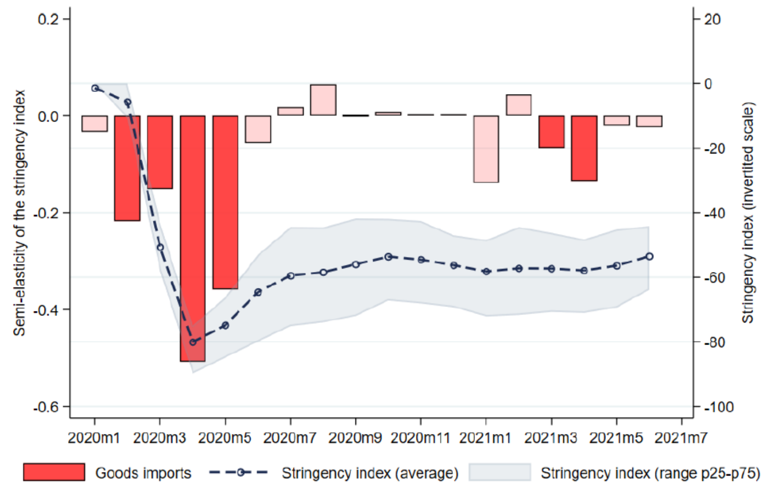
Figure 14 - The stringency index and workplace closings.



Notes: The chart plots the average values of the stringency index and of the measure of workplace closings across exporting coountries for each month. The country-level monthly values of the indexes are calculated as averages of daily values of the month.

Note: Excerpt from IMF, *International Trade Spillovers from Domestic COVID-19 Lockdowns*, Washington D.C., 2022, p. 40.

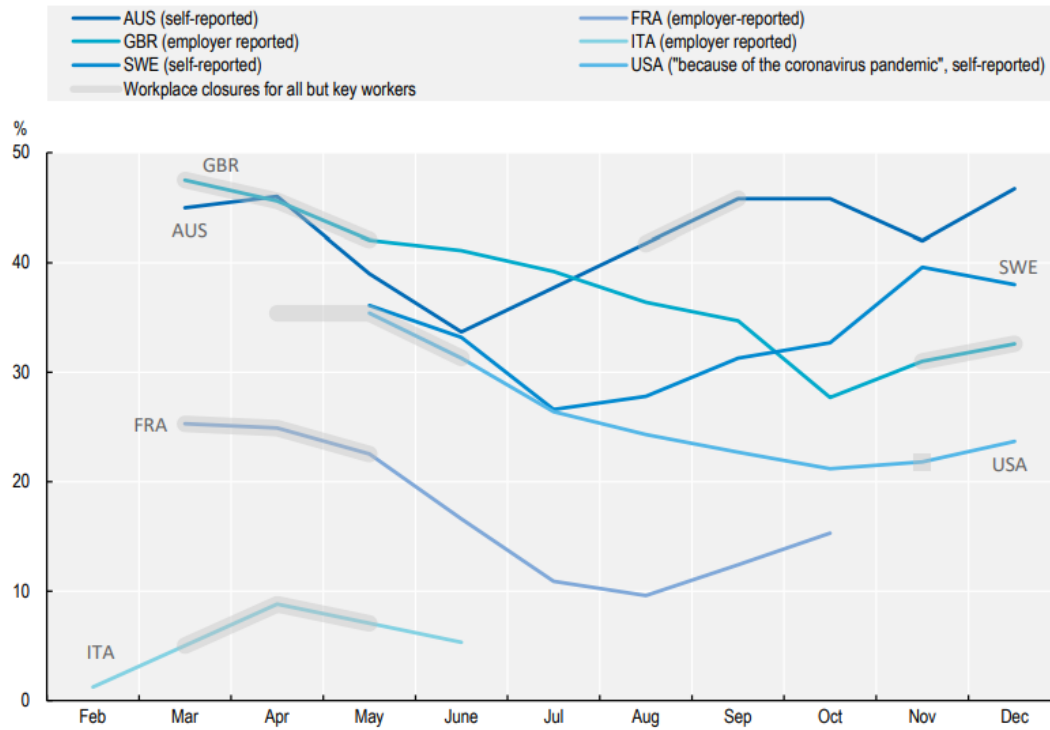
Figure 15 - The international spillover effect of lockdowns over time, excluding China as an exporter.



Notes: The chart plots the semi-elasticity of the stringency index for each month obtained estimating the baseline specification of equation 5 (Table 4, column 2) and interacting the stringency index with the time dummies. China as exporting country is excluded from the sample. Darker bars show semi-elasticities which are statistically significants, lighter bars show those that are not. The dashed line measures the average stringency index of partner countries and the shaded are measures its interquantile range.

Note: Excerpt from IMF, *International Trade Spillovers from Domestic COVID-19 Lockdowns*, Washington D.C., 2022, p. 41.

Figure 16 - Telework during the COVID-19 pandemic, 2020.



Note: Excerpt from OECD, *Teleworking in the COVID-19 Pandemic: Trends and Prospects*, Paris – Cedex, 2021, p. 3.

The figure shows monthly figures of the share of employees teleworking in several OECD countries over 2020, highlighting periods of workplace closures applied to all but key workers. School closures were also common around these times. In general, the share of employees teleworking increased around the times when workplace closures were mandated, though the regions and industries affected by these restrictions varied among countries and over time. This may help to explain why several countries saw falling teleworking rates even during periods with workplace closures.