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Employees working from home: Permanent establishment risks in a Swiss intercantonal context

On 27 April 2022, the Swiss Tax Conference published a statement on when a permanent establishment might arise in an intercantonal context in cases in which employees work from home.

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1. Background

As a result of the COVID-19 pandemic, remote working has become a new norm for businesses and their employees and this trend of people working outside of the office setting is set to continue.

From a tax perspective, these developments pose a certain risk for the businesses that an employee's home office activity constitutes a permanent establishment, resulting in a limited tax liability at the respective place. While these tax issues are widely discussed in a cross-border context, the same challenges occur in a mere domestic context in Switzerland as the cantons are widely sovereign and the corporate income tax rates vary from canton to canton.

On 27 April 2022, the Swiss Tax Conference addressed these issues by publishing a statement on how to interpret and apply existing domestic tax rules to the current circumstances. This statement also looks at issues related to the place of the effective management.

2. Permanent establishment according to Swiss domestic law

2.1. In general

Under Swiss domestic law, a permanent establishment is defined as (i) a fixed place of business (ii) which is wholly or partly engaged in the business activities of an enterprise (art. 51 para. 2 of the Direct Federal Tax Act [DFTA]).

2.2. Fixed place of business

In general, the term "*fixed place of business*" is very wide and the mere fact that an enterprise has a certain amount of space at its disposal is sufficient. Thus, the question arises whether the employee's home office constitutes a fixed place of business.

In this context, pursuant to the newly issued statement, the employee's home cannot generally be classified as a permanent establishment since an

individual's home office should not be regarded as being at the employer's disposal. Even though the area dedicated to work from home is sufficient to create a "fixed place of business", the employer normally has no right to dispose of the employee's place of residence as the employer is neither the owner nor the tenant of all or part of the employee's home.

Furthermore, it is laid down in the statement that the employee's home office will not be at the enterprise's disposal if the employer pays the employee compensation for the use of a private room irrespective of whether the employee works from home on a voluntary basis or if he/she is mandated to do so by the employer. This is because, in return for his/her compensation, the employee has not undertaken to let the landlord use the premises, as is the case with a rental agreement.

2.3. Criterion of qualitative and quantitative business activities

Pursuant to art. 51 para. 2 DFTL and the jurisprudence of the Swiss Federal Supreme Court, a qualitatively and quantitatively significant part of the enterprise's business activities must be carried on in its fixed place of business for a given permanent establishment.

In this regard, the Swiss Tax Conference held in its statement that the recognition of a permanent establishment at the place of the employee's home would lead to a fragmentation of the tax substrate, which should be avoided according to case law. It is further stated that the quantitative criterion is usually not met since the company has only one employee at the employee's place of residence. Even if several employees reside in the same canton/municipality, they should not be counted together for the purpose of the intercantonal tax allocation as each place of activity must meet the criteria for a permanent establishment in itself.

It should be noted that the aforementioned criteria also apply in the event that the CEO or other executive personnel works from home.

3. Employees working from home who are assigned to a secondary tax domicile of the company

A company may have a permanent establishment in a second canton to which certain employees are assigned. If the employees are working from home, the question arises as to whether the employees can continue to be assigned to the permanent establishment or whether they should be directly assigned to the main tax domicile of the company.

In this context, in its statement, the Swiss Tax Conference mentions that, if a company gives up its own office premises at the location of the secondary tax domicile and solely rents conference rooms or offices for specific needs every now and then, there will be a lack of "permanence" and the location used by the company can no longer be classified as a permanent establishment for intercantonal tax allocation purposes. In such a case, the employees are newly assigned to the main tax domicile of the company. If, on the other hand, the company still has a physical presence at a secondary tax domicile which is used by employees working from home for meetings or on special occasions only, such employees will generally stay assigned to the permanent establishment and there will be no change with regard to the intercantonal tax allocation. However, in cases in which the company does not give up its office premises altogether, but reduces its size, visibility and function in a way that calls into question the existence of a fixed place of business, a detailed analysis of the entire case must be conducted.

4. Effective place of management

According to the statement of the Swiss tax conferences, there will be no transfer of the place of effective management of

larger companies if an employee – even if such an employee has a management function – is working from home. In smaller setups, however, in which the operational management of the company is in the hand of a single person, the place of effective management may be located at this person's home if certain circumstances are given.

5. Conclusion

With regard to the intercantonal tax allocation, employees working from home do not create a permanent establishment for the company as a general rule.

Even in the particular case in which a company operates under a fully decentralised business model, where all employees are required to work from home and the company does not offer work places on its own premises, the current rules, as determined by case law, do not allow permanent establishments to be created at the various home offices of the employees.

In the event that a company has a permanent establishment in a second canton, the employees will stay assigned to such a secondary tax domicile even if they work from home, provided that the company still has a physical presence at this location.

Particularly in small companies with only one or a very limited number of employees, it must be considered that there may be a transfer of the company's place of effective management to another canton if such an employee is conducting the day-to-day management of the company from his or her home office.

Switzerland has a well-established tax ruling practice. It is thus quite common for taxpayers to file an advance tax ruling request in order to get legal certainty from the competent tax authorities on a specific inquiry and fact pattern.

The Walder Wyss Newsletter provides comments on new developments and significant issues of Swiss law. These comments are not intended to provide legal advice. Before taking action or relying on the comments and the information given, addressees of this Newsletter should seek specific advice on the matters which concern them.

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