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TAX MATTERS

Working from home can mean tax complications

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I recall a story from The Guardian a number of years ago of Ian Jewell, an employee of the West Somerset district council in southwest England. Mr. Jewell saved his employer approximately £18,000 ($31,000) after he became suspicious when the toilet rolls in his workplace were running out too quickly. The rolls were supposed to contain 320 sheets, but he counted several rolls and realized they were in fact only 200 sheets long. His employer sued the manufacturer, won the case and recovered the equivalent of thousands of dollars.

One thing's for sure: Ever since the pandemic started, many employers around the country are saving a lot of money with their employees working from home. Lower toilet paper costs. And in some cases, lower rent costs. There are many employers that have decided to no longer maintain physical workplaces and offices, and instead require employees to work from home on a permanent basis – or at least for an indefinite period.

Many tax pros across the country have recognized the potential Pandora's box that results from so many employees working from home. What could be the problem? Well, in tax lingo there's something known as a "Permanent Establishment" (PE) – typically a company's fixed place of business. Having a PE in a location means that the company will generally have to pay tax in that jurisdiction – so the PE is an important concept.

THE ISSUES

So, if a company no longer maintains a physical workspace and employees are now working from home, where is the company's PE? And are there implications for employees depending on the answer? The law firm McCarthy Tétrault has written a helpful article on the topic.

The first point to note is that, in the absence of a fixed place of business, the jurisdictions in which a company pays tax might have changed during COVID-19 depending on where employees are working. The reason? A company is generally considered to have a PE where an employee has a general authority to enter contracts on behalf of the corporation. So, if your company has senior employees working from home or another location in another province, a PE may exist there. Which means a tax liability might also exist in that jurisdiction.

Secondly, an employer is required to deduct withholding taxes from salary, wages or other remuneration in particular jurisdictions, which might have changed. Each province imposes its own tax rates, and the amount of the payroll deductions are calculated based on the rates of the province where the employee reports for work. If the employee's home office is a PE of the employer, the employer may be required to change its payroll withholding rate for a different jurisdiction.

Thirdly, the employee may be affected here. Your personal tax liability will depend on whether you're resident in the province where your employer is located, or where your home office is located. Generally, you'll be considered resident for tax purposes in the province in which you reside on Dec. 31 each year. But what does "residence" in a province look like? You'll generally be resident where you have significant residential ties, the most important of which include the availability of a dwelling place, the location of your spouse or common-law partner, and the location of your dependants.

THE CONCLUSIONS

From an analysis of the law, court decisions and government pronouncements, McCarthy Tétrault concluded that:

- An employee's home office is not normally considered to be a "fixed place of business" of the employer, provided the home office is not objectively identified with the business of the employer (no signage with the employer's name, for example). So, a home office should generally not result in a fixed place of business (PE) of the employer.
- A home office is generally not considered to be an "establishment" of the employer for payroll withholding purposes, so that an employee who works full-time from home in a particular province is generally not considered to report for work at an establishment of the employer in that province solely by virtue of the home office. So, the employee is generally deemed to report for work at the establishment of the employer from which their remuneration is paid.
- Having said these things, an employee working from home may cause the corporate employer to be deemed to have a PE in that province if the employee has a general authority to contract on behalf of the corporation. General authority to contract normally exists if the employee, in the ordinary course of business, can bind the corporation, without prior approval. This can create issues for the company's jurisdiction for tax liability and an employee's payroll taxes.

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