

## Theme 2: Fixed establishment

### ***What is the problem?***

Various CJEU and national court decisions in the Member States but also real-life examples from business practice showcase the challenges and legal uncertainty that exist on this topic both for business and tax administrations across the 27 EU Member States.

Questions like

- *can a locally established and formally independent entity constitute a FE of another taxable person established abroad? And if yes, which circumstances are relevant in this respect? (independent entity as an FE of another taxable person)*
- *when does the most appropriate, and thus the primary, point of reference for determining the place of supply of services for tax purposes, which is the place where the taxable person has established his business, not lead to a rational result or when does it create a conflict with another Member State that another establishment may come into consideration? (rationality test)*
- *what type/level of human and/or technical resources are required to constitute an FE – especially taking into account that new models of business activities often do not require any human and/or technical presence in the Member State where the services are supplied and/or received? Can human resources employed by another entity create a FE of the non-established entity? If yes, it is understood that these employees work under direct supervision of the non-established entity. How can this be determined? (human and technical presence' test)*
- *what does the term "sufficient degree of permanence" mean in practice? does a single transaction (even if execution of a contract requires several months) create a sufficient degree of permanence? what if over the time the establishment becomes a FE? Should such an emerging fixed establishment be considered for VAT purposes with retro-active effect (ex tunc) or only from the point in time in which the presence of the VAT payer has crossed the line to a permanent presence (ex nunc)? Both approaches expose the taxpayer to a risk of penalties/sanctions. (permanence test)*

show that in practice the topic fixed establishment causes legal uncertainty, bureaucracy, cash flow issues and ultimately as well VAT costs, particularly in B2B scenarios where VAT should be neutral.

### ***How to resolve?***

To clarify this topic further the VEG did already carry out some work on this topic (Welmory case) a couple of years ago. Since then further court cases came up on the CJEU and national level and also new examples from business practice were collected, which are worthwhile to look at – we captured some of them in the appendix below. We as VEG think a detailed analysis on the topic fixed establishment has to be carried out with a view of laying down positive and practical criteria that reflect the specific nature of the FE for VAT purposes. We are very happy to actively support on such initiative.

### ***Our request:***

As there are different approaches and VAT treatments on this topic across the EU, a discussion in the VAT Committee on this topic leading to guidelines or explanatory notes of the Commission based on an analysis carried out by the VEG (taking the cases and real life examples highlighted in this document as a basis) might be very helpful in order to come to a common approach across the EU, strengthening the EU harmonized VAT system with consistently applied rules on the concept of fixed establishment across the 27 Member States, particularly important for business in the post Covid-19 recovery process.

**Appendix:**

**Examples of tax rulings/tax authorities' positions/national tax courts' verdicts from, , , , Austria, Belgium, Croatia, France, Germany, Poland and The Netherlands**

**Facts of the case:**

The Austrian Company has concluded the consortium agreement. The Company was obliged to supply the metro carriages to Poland. The Company is also obliged to:

- perform the trial run;
- supervise the installation;
- perform the maintenance (36 months guarantee).

The metro carriages were produced in Austria and then transported into Poland.

The Austrian Company is entitled to use client's premises and does not lease any office or other real estate. The only technical resources that Company possess in Poland are the personal equipment of the employees.

All the management activities are performed in Austria. The employees assigned to Poland are not entitled to undertake any decisions or conclude any agreements.

The Company's employees will be present in Poland only for the time of the realization of the contract for the carriages' supply. This time will include the supply of metro carriages and the guarantee period. The Company may make use of the leased employees if necessary.

The parties of consortium agreement and the client seems unrelated.

**Tax ruling:**

The Company is entitled to make use of the client's premises. Thus, there are technical resources that are controlled by the Company.

The Company has engaged the human resources, sufficient for carrying on Company's business activities.

Thus, the Company will have the fixed establishment in Poland.

**Facts of the case:**

Swiss Company was buying and selling cosmetics in Poland and planned to store those goods in Poland. It concluded a warehousing agreement with (independent; non-related) Polish company (Polco). Polco leased a warehouse to the Swiss Company and was also supplying logistic, admin and compliance services.

Dedicated employees of Polco were acting as a point of contact for the supplier and customers of the Swiss Company. There were no own technical and human resources of the Swiss Company in Poland.

**Tax ruling:**

The character and scope of the resources available for Swiss Company in Poland allowed Swiss Company to operate in Poland autonomously.

The fact, that the Swiss Company concluded agreements with the Polish service providers confirms, that the Swiss Company could conduct broad business operations in Poland.

Access to the warehouse and employees of Polco makes Polco a fixed establishment of the Swiss Company. The fact that the decisions are taken in Switzerland is irrelevant.

**Facts of the case:**

The Company (German partnership) will take part in Poland in the project of building the plant. The project will last 2 year and will include Company's support in the area of preparing the plant to use. The above services shall be deemed as the services connected with the real estate for VAT purposes.

The Company does not use outsourcing and engages own employees. Only one employee is assigned to Poland, however, according to the needs, more employees may be engaged in Germany and then assigned to Poland. The personnel will be settled down in the hotel rooms or the apartments will be leased. Employees in Poland will not be entitled to undertake any business decision concerning activity in Poland.

The permissions will be provided by Company's client. The Company will be entitled to use the space shared with Client's employees (and, probably, the employees of other companies). The Company will not receive the keys to the rooms.

All equipment (tools, laptops etc.) will be provided by the Client.

It seems from the description that Company and the Client are unrelated.

**Tax ruling:**

The place of business in Poland will be characterized by a sufficient degree of permanence as the project's realization will last for 2 years.

The Company will possess the human and some technical resources. Although the Company formally will not own the premises and equipment, in the economical meaning the Company will be entitled to use them and have a control over them. Employees will also be present.

Summarizing, the Company's activity in Poland will be characterized by a sufficient degree of permanence and a suitable structure in terms of human and technical resources to carry out the economic activity in Poland.

**Facts of the case:**

British Company carries on business activities in the area of gas trading. Company will enter into an agreement regarding gas storage.

Company's employees will not be permanently present in Poland, however they may appear in Poland for certain time.

The Company may create a branch in Poland for the purpose of meeting the legal requirements (Company's business activity requires a concession). Even if branch is created the management and sale activities will be performed in the UK.

**Court's judgement:**

As based on the Act on Energy branch of the non-resident entity is obliged to have the permanent human and technical resources, sufficient for carrying on the business activity in the area of gas trading – therefore the Company will possess the fixed establishment in Poland.

**Facts of the case:**

Swiss Company produces and sells metal packaging. It concluded agreement for indefinite period of time with Polish Company (toll manufacturing agreement).

Swiss Company ships materials and Polish Company produces finished products.

Upon completion of services, the goods are stored by Swiss Company in the Polish warehouse owned by the Polish company. Then the goods are distributed in Poland and outside Poland. Swiss Company purchases also logistics and administrative services from Polish service providers.

Swiss Company has no employees nor assets in Poland.

**Court's judgement:**

The Swiss Company concluded with its Polish partner an agreement for indefinite period of time, what confirms that Company CH operates on Polish territory on a permanent basis

The Swiss Company has adequate technical resource in PL – as it controls the resources of the Polish Company and Polish Company (acting as a fixed establishment of the Swiss Company) can use the resources of third parties – other service providers, which concluded agreements with Swiss Company.

The fact that both Companies are related is irrelevant. What is important is the fact that Polish Company PL provides services exclusively to the Swiss Company.

Swiss Company has sufficient human resources – as it has economical control over the employees of the Polish Company.

**Facts of the case:**

Maltese company was distributing pharmaceutical products in Poland. Polish (related) company was providing marketing, promotional and distribution services in Poland

The orders were placed via the Polish company. Maltese entity did not have its employees in Poland but a person (Country Manager), member of the board of the Polish company was providing several services to the Maltese principal (advisory, reporting, business planning, representation etc.).

Maltese company did not own any premises nor technical equipment in Poland but entered into a warehousing agreement and some technical support agreement with the Polish company.

**Court's judgement:**

The agreement created a fixed establishment in Poland as the Maltese company did have a "comparable control" over employees and technical resources of the Polish company. The court has emphasized that without a Polish company's resources Maltese company would not be able to distribute goods in Poland.

**Facts of the case:**

German company entered into a toll manufacturing agreement with the Polish entity. The agreement was quite typical toll manufacturing and was concluded for the indefinite period of time.

Polish company provided a toll manufacturing services (using also the machinery and equipment owned by the German principal) and was also storing a manufactured goods. Manufactured goods were not distributed in Poland but were sent back to Germany.

**Court's judgement:**

The court decided that the permanence test is met; the human and technical resources criteria are met as well (part of equipment is owned by the German company and also one employee is present on site but most important argument is that German company controls the human and technical resources even though formally human and (most of) technical resources are owned by the Polish supplier.

In two instances (different EU Member States), a supplier of entity X was forced upon to charge VAT to a non-EU established entity.

One case concerned a contract manufacturer (France), the other case was for domestic transport services (Germany).

The authorities claimed that entity X had a fixed establishment in their country, although following the EU Implementing Regulation, the entity X provided them with a certificate it has no Fixed Establishment in the country concerned.

There was no argumentation by the tax authority why there was an assumption of a Fixed Establishment.

The entity X had no ability to defend itself. In both instances, this has led to a discussion (disruption) of the business relationship with the supplier, since he was forced to charge VAT, which the customer did not want to pay. In one instance, the supplier paid the VAT to the authorities, claimed it back from the customer which the customer did not pay/accept and he was close to bankruptcy.

Similar example on toll manufacturer (Croatia): The tax authorities were of the opinion that local toll manufacturer (a subsidiary of foreign parent company), who was engaged - beside the toll manufacturing contract- by a separate service contract to provide some administrative and advertising services to parent company, creates a fixed establishment for parent company in that member state. Arguing that employees of toll manufacturer also actively participates in the business operations with customers and the supplier of parent company when e.g. organizing delivery of raw material for toll manufacturing or delivery of finished goods to customers after toll manufacturing.

On 22.7.2020 another similar case to that was brought from Romania to the ECJ and is now pending under C-333/20 Berlin Chemie (BC). In a nutshell Berlin Chemie, a German company, sells goods in Romania where it is VAT registered. BCAM, a group company established in Romania, provides BC with marketing, advertising and regulatory support services. These services have been treated as being outside the scope of Romanian VAT and subject to reverse charge VAT in Germany. However, the Romanian tax authorities are of the opinion that, by engaging BCAM with different activities, BC thus has sufficient human and technical resources at its disposal in Romania to create a fixed establishment there with the consequence that BCAM's services to BC are subject to VAT.

In Belgium, there is a recent court case at the Court of First instance, whereby under a typical toll manufacturer - principal commissionaire structure, the tax authorities claimed a Fixed Establishment for the principal in Belgium. The decision did not refer to ECJ cases. The taxpayer concerned will appeal to the decision. Note that the Belgian tax authorities prepare a Circular on this topic which was discussed with the business. Their main (critical) argument/condition is "economic reality", an approach whereunder activities and resources located in a country are attributed to a foreign entity without regard to the legal arrangement whereunder they are being procured. In this way, tax authorities construe a concept of adequate structure consisting human and technical resources from the fact that a foreign entity is able to realise taxable transactions in a country, rather than from its effective presence there. This is pretty worrying as every subsidiary of the same group could be considered as having a FE.

#### Human and technical resources test:

In Austria there is one case pending at the Highest Administrative Court which was also referred to ECJ (C-931/19, Titanium) whether the term fixed establishment acc to Dir 2006/112/EG and Implementing regulation 282/2011 requires both technical and human resources.

The pending case concerns the vatable renting out of an immovable property in Austria by a non-established company where except of the building itself no human resources are present. The authorities are of the opinion that taxable person creates however a fixed establishment (with the consequence that Reverse Charge is not applicable anymore).

Similar cases are pending at lower courts on the question whether the mere renting out an immovable property located in Austria creates a fixed establishment (with the consequence that the special scheme for small entrepreneurs is no more applicable).

#### Sufficient degree of permanence test:

As there is no explicit definition of term "sufficient degree of permanence" same activities of a taxable person lead each time to a different outcome both in local as well as cross border transactions. Some examples: supply of good with installation that last some weeks or month, construction work/project that last some weeks or months, supply of goods or services at a fair/exhibition that lasts 2 weeks etc

Netherlands Supreme Court decision 2019 (comparable to the pending Titanium case)

Two German persons rent a holiday home in the Netherlands through a rental agency. They want to apply the exemption for small businesses. A requirement for the application of this exemption is that the entrepreneur is established in the Netherlands. The Den Bosch court of appeal held that the interested parties do not have a fixed establishment in the Netherlands. According to the Supreme Court, the Court wrongly failed to address the claim of the interested parties that the holiday home forms a fixed establishment in connection with the activities of the office. However, this does not lead to cassation. Interested parties in the Netherlands must have their own staff and a structure with a sufficient degree of permanence to draw up lease contracts and take decisions of day-to-day management. The services of an independent intermediary cannot be taken into account in this respect. Now that the Court of Appeal has ruled that the rental office is an independent intermediary, the holiday home and the activities of the rental office in combination cannot constitute a permanent establishment.