

Taxation of Permanent Establishment

Permanent Establishment or PE is an important concept under Tax treaties. Multi National Corporations & Non- Residents carrying on Business in another country are liable to pay tax on the business profits in that other Country only if the business is carried on through a PE situated in that other Country.

Therefore, MNC's or Non-Residents carrying on business in other Countries it is extremely important to determine the existence of a PE. If the business is not carried out through a PE the MNC's Non Resident would not be liable to taxation in the other Country. If the business is so carried out through a PE, the Source Rule will apply to the business done in the other Country. It would then be immaterial whether the PE has a tax number or tax card or any form of Registration.

Qatar Tax laws 2009 in Article 1 has defined Permanent Establishment – “A fixed place of business through which the business of a taxpayer is wholly or partly carried on, including , for instance, a branch, office, factory, workshop, mine oil or gas well, quarry, a building site, an assembly project or a place of exploration, extraction or exploitation of natural resources. Permanent Establishment also includes the activity carried on by the taxpayer through a person acting on behalf of the taxpayer or in his interest, other than an agent of an independent status” The scope of the definition is Extremely wide and as we will see later the definition of PE in the Tax treaties entered into by Qatar with several Countries is more restricted in its scope. Where Qatar has entered into Tax treaties with Countries the Restricted meaning of PE would prevail .

The definition gives instances of PE namely; a branch, office, factory, workshop, mine or gas well, quarry, a building site, an assembly project or a place of Exploration, extraction or exploitation of natural resources . These are instances of fixed place, envisaged in the definition. These again are as per Article 5 of OECD Model Convention. However, as mentioned earlier these fixed places are given a restricted meaning in Article 5. The last Para of the definition refers to PE being Established where the activity is carried on by the taxpayer through a person acting on behalf of the taxpayer or in his interest other than an agent of independent status. Broadly, a PE would be Established where the activity is carried on through a ‘Dependent agent’ who is not an ‘Independent Agent’ Again, the OECD MC gives a restricted meaning of who would constitute a ‘Dependent Agent’ or a independent Agent’.

Elaborating the definition of Qatar Tax laws “a fixed place of business through which the business of a taxpayer is wholly or partly carried on ...” a PE is said to be formed where:

- there is an enterprise carrying on a *business*.
- There is a *place of business* at the disposal of the enterprise.
- The place of business is *fixed*.
- The *business* of the enterprise is *carried on* wholly or partly *through* this fixed place of business.

The term “business” is not defined in the Tax Treaties and hence the meaning assigned in the respective Tax laws should act as a guide. Qatar Tax Laws 2009 has not defined the word “Business” but has defined the word “activity” as “any profession, vocation, service, trade, industry, speculation, contractual work or any business carried on to derive a profit or an income including the exploitation of a movable or

immovable property”. Business would therefore mean an activity which is carried out to earn profit or income. The question whether the activity constitutes ‘Business’ is a mixed question of law and fact which has to be decided on facts and circumstances of each case.

Again, Place of Business is not defined. It usually means premises of the enterprise used for carrying on the business. Further, the concept ‘place of business’ as commonly understood is undergoing change and in the digital world and the world of mobile and satellite communication it would not necessarily mean a ‘premises’ in the traditional sense.

The place of business must be fixed. A PE fixed place. A place which is temporary or a casual place would not lead to formation of a PE. Again with

controlled and owned by the Enterprise or through a person acting on behalf of the tax payer or in his interests other than a person of independent status. Qatar has adopted the OECD model Articles in its Tax Treaties with Countries with some modifications. We have taken the Qatar UK Double Taxation Avoidance Agreement (DTAA) as a respective Agreement for the purposes of a discussion.

Permanent Establishment – ARTICLE 5.

(1) For the purpose of this Agreement, the term “permanent establishment” means a fixed place of business through which the business of an enterprise is wholly or partly carried on.

(2) The term “permanent establishment” includes especially:

(a) a place of management;

(b) a branch;

(c) an office;

(d) a factory;

(e) a workshop;

(f) a warehouse;

(g) a sales outlet;

(h) a mine, an oil or gas well, a quarry or any other place of exploration, extraction or exploitation of natural resources.

(3) A building site, a construction, assembly or installation project or supervisory activities in connection therewith constitute a permanent establishment only if such site, project or activities last more than six months in any twelve month period commencing or ending in the tax year concerned.

(4) A permanent establishment shall be deemed to exist where:

(a) an enterprise furnishes services through employees or other personnel or other personnel engaged

by the enterprise for such purpose, but only if the activities of that nature continue (for the same or connected project) within a Contracting State for a period or periods aggregating more than 183 days in any twelve month period commencing or ending in the tax year concerned;

(b) an enterprise through an individual resident in a Contracting State performs service in the other Contracting State and the individual's stays in that other Contracting State is for a period aggregating more than 183 days in any twelve month period commencing or ending in the tax year concerned.

(5) 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, displays or delivery of goods or merchandise belonging to 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 carrying on, for the enterprise, any other activity of a preparatory or auxiliary character.

(e) the maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character.

(f) the maintenance of a fixed place of business solely for any combination of activities mentioned in sub-paragraphs (a) to (e) of this paragraph, provided that the overall activity of the fixed place of business resulting from this combination is of a preparatory or auxiliary character.

(6) Notwithstanding the provisions of paragraphs (1) and (2) of this Article, where a person – other than an agent of an independent status to whom paragraph (8) of this Article applies – is acting on behalf of an enterprise and has, and habitually exercises, in a Contracting State an authority to conclude contracts on behalf of the enterprise, that enterprise shall be deemed to have a permanent establishment in that State in respect of any activities of such person are limited to those mentioned in paragraph (5) of this article which, if exercised through a fixed place of business would not make this fixed place of business a permanent under the provisions of that paragraph.

(7) Notwithstanding the preceding provisions of this Article, an insurance company of a Contracting State shall, except in regard to reinsurance, be deemed to have a permanent establishment in the other Contracting State if it collects premiums in the territory of that other Contracting State or insures risks situated therein through a person, other than an agent of an independent status to whom paragraph (8) of this Article applies.

(8) An enterprise shall not be deemed to have a permanent establishment in a Contracting State merely because it carries on business in that State through a broker, general commission agent or any other agent of an independent status, provided that such persons are acting in the ordinary course of their business.

(9) The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other 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.

Clause wise Analysis of Article 5:

Article 5(1) embodies the basic definition of PE which is similar to the definition under the Qatar Tax wholly or partly carried on. Place of Business is not defined. In usually means a premise of the Enterprise used for carry on the business. It may include a machinery or Equipment eg: Teller machine or even

where the place is permanent and Fixed for a reasonable long period. Temporary offices in Business

Id cease to exist when the foreign enterprise disposes the fixed place of business or when the business activities being carried out through it ceases or terminates. However, temporary closure or is defined in the Tax Treaties i e Performance of professional services and

activit
circumstances of the case..

In Article 5 (2), the DTAA especially provides that the term PE includes (a) a place of management (b) a branch (c) an office (d) a factory (e) a workshop (f) a Warehouse (g) a sales outlets (h) a mine, an oil well or gas well, a quarry or any other place of exploration, extraction or exploitation of natural resources. management of an enterprise reside.

Example: A foreign contractor does not have a place of management on an oil rig is a foreign state where it merely provides personnel for manning operations & management of the rig. Article 5 (2) (b)

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where goods are stored. A warehouse which is used for purchasing and selling the goods would place for where the enterprise sells its goods. Article 5 (2) (h) refers to a mine, an oil or gas well, a quarry or any other place of exploration, extraction or exploitation of natural resources as PE. The word mining of any type or onshore/offshore activities of exploiting hydrocarbon or complex materials which are below the sea or below the ground.

Article 5 (3) refers to building site PE, a contractor PE assembly PE, installation PE or Supervisory PE. Each of these has a very wide meaning in the respective fields. Broadly, these activities are linked to

roads, bridges, laying pipelines, building creation & renovations, Excavation & dredging. Installation PE could cover installation of pipelines, machinery installation, laying foundation. Supervisory PE are connected with civil work or Construction or projects which oversee work. But not all supervision work would give rise to a supervisory PE. Where only personnel are supplied by an enterprise no Supervisory PE may arise.

in any 12 months commencing or ending in the tax year concerned. Tax year as per Qatar Tax laws is generally a period of 12 months from 1st January to 31st December but could be a period of 12 months from a different date which is linked to the accounting period.

A question would arise whether a PE would arise where the period exceeds six months in totality spread over two tax years but does not exceed six months in each tax year. In the opinion of the author no PE would arise in such a situation as the criteria of 6 months in each tax year is not satisfied. More questions arise on the date of commencement of PE and date of creation of the PE. The PE would commence when the work commences after receipt of the contract but care should be taken to ascertain the date after excluding the period of formation of PE or where only incidental work is done.

guided by the facts of each case.

SERVICE PE [Article5 (4)]

A service PE is formed where an enterprises provides services with a contracting state through its employees or personnel employed by it if the activities continue for a period or periods aggregating more than 183 days in any 12 months period commencing or ending in the tax year concerned. Where the enterprise through an individual who is a resident in a contracting state performs service in the other contracting state and the individual stays in other Contracting State is for a period aggregating more than 183 days in any 12 month period commencing or ending in the tax year concerned a PE would come to exist. The most common example of a service PE would be deputing employees to projects in the other contracting state.

SPECIFIC EXCLUSIONS FORM PREVIEW OF A PE [ARTICLE 5 (5)]

Article 5(5) gives exclusions from those considered to be a PE. Mere use of facilities solely for the purpose of storage, display or delivery of goods belonging to the enterprise will not make such a facility as a PE in terms of Article 5 (5) (a). Maintenance of stock of goods belonging to the enterprise solely for the purpose of storage, display or delivery will not lead to the creation of a PE in terms of Articles 5 (5) (b) .Similarly, maintenance of stock of goods belonging to the enterprise solely for the purpose of processing will not lead to the creation of a PE in terms of Article 5 (5) (c) .While generally a fixed place leads to the creation of a PE provided in Article 5 (1), a fixed place of business solely for the purposes of purchasing goods or for collecting information for an enterprise would not lead to creation of a PE in terms of Article 5(5)(d). Similarly, a fixed place of business solely for the purpose of carrying on any other Character will not lead to creation of a PE in terms of Article 5(5)(e).

circumstances of the case would have to be examined to ascertain whether the activities have a . Broadly, if the activity of the Fixed Place forms an indispensable and significant part of the activity of the enterprise as a whole or are similar to the activities of the . It is also provided in Article

5(5)(f) that where a fixed place of business combines any of the activities mentioned in clauses (a) to (e) of Article 5(5), then, as long as the combined activity of such fixed place of business is preparatory or auxiliary, a PE should not be deemed to exist. This Article should be considered in the light of the facts and circumstances of each case.

AGENCY PE [Article 5 (6), 5 (7) & 5 (8)]

Generally, a dependent agent constitutes a PE and an independent agent will not result in a PE. The performing business activity itself through a Fixed Place then it would invariably lead to a Fixed Place PE. However, where the Foreign Enterprise chooses to carry out the business activity through an agent whose activities are integrated to the business of the foreign Enterprise to a large extent such an agent would then be a dependent agent this will lead to a creation of an Agency PE. Else, it would lead to circumvention of the Basic Rule of PE taxation and deny the source country of its share of Revenue.

Article 5 (6) & 5 (8) deems formation of an Agency PE where the agent is acting on behalf of the Foreign Enterprise and habitually exercises an authority to conclude contracts on behalf of the Foreign Enterprise. However, no PE would be formed where only non-binding orders are secured by the agent & where the Foreign Enterprise takes final decision on accepting or rejecting the order or contracts. Therefore the role of the agent is quite important and the functions he performs quite critical. Where the agent concludes the contract and binds the Foreign Enterprise habitually or regularly, an Agency PE can be said to be formed.

At the same time an agent who acts for a number of Foreign Enterprises and who secures orders as part of his ordinary business would not create an agency PE. However, even such an agent could become a dependent agent viz- a viz a particular Foreign Enterprise where the facts and circumstances are taken into account. A complete analysis would need to be done on the relationship between the Foreign status.

Article 5 (7) pertains specific to insurance Company and conveys that a PE is deemed to be formed where it collects premium in the territory of that other Contracting State.

Subsidiary PE [ARTICLE 5 (9)]

This article clarifies that a Foreign Enterprise is not deemed to have a PE in the other state merely because it controls or is controlled by a Company that is a Resident of the other State. The other Articles would have to be referred to so as to determine the Existence of a PE. Mere Existence of a Controlled Enterprise in the other Contracting State will not lead automatically to the creation of a PE. What is subsidiary company did no work for Foreign Enterprise and the Foreign Enterprise dealt directly with the Entities in the other Contracting State subsidiary no PE would exist.

TAXATION of PE

The tax treatment of income generated by a PE would depend upon the nature of income i.e. whether it is a Business income or Capital gain or income from shipping and Air transport, dividend, Royalty, fees for Technical Services etc. There are separate Articles for each type of income. However, the taxation of Business Profits in the hands of PE covered by ARTICLE 7 are frequently referred to and therefore taken up separately.