SCENTIA INTERNATIONAL ECONOMIC REVIEW Volume 1 - Issue 1 - 2021

Requirements for assuming a permanent establishment under Art. 5 OECD Model Tax Convention -

in accordance with the German Federal Fiscal Court's considering a locker as a fixed place of business

Mandy Witt, Mendel University, Brno, Czech Republic

Abstract

In January 2019, the German Federal Finance Court defined the legally binding requirements with respect to a fixed place of business being a matter of a permanent establishment according to German law, thus the revenue generated being subject to the German taxation.

This article addresses the research question 'Which criteria have to be met by a permanent establishment to be effective for tax purposes?'

Regarding the methods, the article reviews relevant literature and case law to identify the prevailing and dissenting opinions on the requirements for assuming a fixed place of business under Art. 5(5) OECD-Model Tax Convention. As to the question whether one can refer to a fixed place of business as a permanent establishment, the courts use to differentiate between Civil Jurisdiction and Common Law. For the sake of clarity, the coined the article 5 of the $OECD^1$ Model Tax In accordance to the abovementioned Model Tax Convention, binding provisions were defined on the international level for both, countries using the Common Law as well as for those using the Civil Law, with respect to the requirements as to a permanent establishment and the resulting country of taxation be In doing so, the question arose whether for instance a lockbox would represent a permanent establishment or not.

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¹ The Organisation for Economic Co-operation and Development

However, the contracting states did not succeed in determining clear requirements as to the existence of the establishment in question. In fact, they left it to the state in question to define their respective double-tax agreements according to their own needs.

Keywords: OECD, place of business, permanent establishment

JEL codes: G38, K34

1. Introduction

In January 2019, the German Fiscal Court held that the mere existence of a locker may qualify as a fixed place of business under Art. 5(1) OECD Model Tax Convention. In this case, an aircraft-engineer conducted technical maintenance services as a subcontractor at a hangar in Germany; according to the court, his locker provided by the contractor for the storage of the maintenance equipment constituted a permanent establishment, and thus subjected the English Limited (Ltd.) on behalf of which he was acting to German income tax.2

This paper will outline the requirements under Art. 5 OECD Model Tax Convention which need to be satisfied for constituting a permanent establishment and then critically discuss the assumptions made by the Federal Fiscal Court.

2. Methods

This article addresses the research question 'Which criteria have to be met by a permanent establishment to be effective for tax purposes?'

Regarding the methods, the article reviews relevant literature and case law to identify the prevailing and dissenting opinions on the requirements for assuming a fixed place of business under Art. 5(5) OECD-Model Tax Convention. For so doing, it is also necessary to discuss the legal perspectives underlying Art. 5(5) and (6) as well as the differences of the law of agency in civil and common law jurisdictions. Given the theoretical background, the article can then contrast the opinion concerning Art. 5 with the understanding of a permanent place of business under German law and conclude in how far the Federal Fiscal Court's decision can be reconciled with it.

² Federal Fiscal Court, judgment of January 1, 2019, IB 138/17.

3. Results

3.1. Understanding of "agency" in civil and common law jurisdictions

Civil and common law jurisdictions differ in a wide range of dogmatic perspectives, including the law of agency. Civil law jurisdictions understand the term "agency" in different ways. For instance, as a technical legal term, "agency" describes a specific way of contracting where a third person can agree on a contract for someone else with a legally binding effect; in a broader sense, "agency" can also mean the particular relationship between a principal and his "agent"; in this sense, agency thus refers to the legal relationship between the principal and the agent who acts on his behalf.

For an agency to be established in the technical meaning, the agent first needs to be vested with special authority by the person on whose behalf he is assigned to conclude legally binding contracts (under German law referred to as *Vollmacht*). Second, the legally binding conclusion of a contract by an agent requires that he discloses to the other party the person of the principal.³ In the civil law perspective, the disclosure requirement is assumed to protect the third party from entering into contracts without knowing his contractual partner;⁴ accordingly, if the agent fails to disclose his principal he is deemed as not properly exercising the *Vollmacht* and the contract has no legally binding effect.⁵

Civil law jurisdictions further distinguish the commissionaire (*Kommissionär*) who – in contrast to the agent – concludes contracts in his own name but on behalf of a principal.⁶ That is, the agent and *Kommissionär*, under civil law, differ on the "in his own name" prong, and thus exempt *Kommissionärs* from contracting with a legal effect for the principal unless it is not specifically mentioned.

As civil law jurisdictions, common law also relies on two differing meanings of agency. In a legal understanding, "agency" means that a person can represent a third party with a legal effect, including the change of the principal's legal status. In practice, however, the term is often applied in a wider non-legal meaning which is also used in this article. That is because in common law jurisdictions, "agency" in no sense refers to a specific agency contract as they do not exist in common law. Rather, common law relies on the concept of freedom of contract and allows the parties broad leeway in formulating their contractual terms unless it is not legally forbidden.

Of course, the difference in the concepts of agency in civil and common law have one fundamental consequence: under common law, and as a result of the rather broad understanding of "agency", contracts made between the agent and the third party legally bind the principal whether he is disclosed to the contractual partner or not and whether or not the agent acts "in the name of" the principal. Precisely, and in contrast to civil law, the addendum "in the name of" is basically unknown to common law jurisdictions in both

³ See Sec. 164(1) German Civil Code.

⁴ Schilken in: Staudinger, BGB, before Sec. 164 et seq., n. 35.

⁵ Schramm in: MüKo, BGB, Sec. 164, n. 48 et seq.

⁶ See Sec. 383(1) German Commercial Code.

⁷ See generally ALI, Restatement (Third) of Agency; Watts, Bowstead & Reynolds on Agency.

⁸ See *Watts*, Bowstead & Reynolds on Agency, n. 12, para. 8-073.

general and tax law. Thus, for the purpose of this article, the term "agent" can be equated with "legally binding" because virtually all contracts concluded by agents are effectively made "on behalf of" or "in the name of". For Common law such as the German jurisdiction, contracts concluded by an agent can only have a legal effect for the principal if the former expressly acts in the name of the principal; consequently, the differentiation between legally binding contracts made by agents for their principal on the one side, and contracts concluded by *Kommissionärs* without a legal affect for the principal on the other side, are fundamental for subjecting a person to taxation under civil law. Essentially, the differentiation between agent and *Kommissionär* on which tax rules in civil law jurisdictions are fundamentally based are irrelevant for taxation in common law unless the contract expressly states the agent shall be liable to the other party; this scenario, indeed, is rather unlikely in practice.

As needs to be captured at this point, the fact of whether a person qualifies as an agent is indispensable for determining whether his principal is legally bound by the contract or not both under civil and common law. And it is exactly this issue on which Art. 5 OECD Model Tax Convention is built because it applies to agency law both in common and civil law countries. Having laid down the theoretical background for agency law and its relevance for taxation, the article can now discuss the requirements for assuming a permanent establishment under Art. 5 Model Tax Convention.

3.2. Requirements for assuming a permanent establishment under Art. 5(5) Model Tax Convention

According to Art. 5(1) OECD Model Tax Convention, a permanent establishment in a Contracting State is generally constituted by a

"fixed place of business through which the business of an enterprise is wholly or partly carried on." ¹¹

3.2.1. Place-of-business-test

This definition basically implies a place-of-business-test which requires that (1) the enterprise is tangible and (2) its operations in the Contracting State can be attributed to it.

For the tangible nature of the place of business, the enterprise needs to hold a physical object which can be deemed as able to conduct commercial activities, e.g. a building. As generally agreed in the literature, automated equipment including pipelines and vending machines can constitute a fixed place of business as well. ¹² In contrast, only software and copyrights are agreed upon to be definitely excluded from being tangible. ¹³

⁹ But see US Internal Revenue Code, para. 864(5)(A) as an exception.

¹⁰ See for common law countries *Teheran-Europe Co. Ltd v. S.T. Belton (Tractors) Ltd.*, 2 Q.B. 545, 533 (CA) (1968); *Weiss, Biheller and Brooks ltd v. Farmer*, 8 TC 381, 406 et seq. (1922); *Watts*, Bowstead & Reynolds on Agency, n. 12, para. 8-073.

¹¹ See Cockfield/Hellerstein/Millar/Waerzeggers, p. 113.

¹² Marti/Wechner-Roth, Betriebsstättendefinition der OECD, p. 348.

¹³ Skaar, Permanent Establishment: Erosion of a Tax Treaty Principle, p. 122.

The attribution-prong requires that the enterprise exercises some degree of power of the place of business, e.g., that it exercises the "right-of-use".

The right-of-use-prong itself is not mentioned in Art. 5(1) OECD Model Tax Convention itself, but, according to the OECD Commentary, necessary to constitute a permanent establishment.¹⁴ Thus, under Art. 5(1) OECD Model Tax Convention, the right-of-use-requirement is fullfilled when the place of business is "at the disposal" of the company in the Contracting State; that is, the company which shall be subjected to taxation needs to have the right of use which itself is constituted when the place of business is at its disposal.¹⁵

Although the at-the-disposal-condition is mentioned forty-eight times in the OECD Commentary, there is little agreement on a positive definition and what exactly it requires. In a negative definition, scholars agreed upon what the at-the-disposal-prong does not require while the OECD's attempts to clarify the issue appear to be in vain. Specifically, the disposal-requirement in the OECD Commentary first referred to the condition that an enterprise needs to have "a certain amount of space at its disposal" in order to assume a permanent establishment in the Contracting State. 19

In this definition, there appear to be no issues as regards the right-of-use-requirement at the first glance. Some scholars, however, argued the OECD's statement, e.g. its at-the-disposal-definition, to mean that the enterprise must hold the legal rights over the permanent establishment.²⁰ The OECD rejected that assumption and clarified that a permanent establishment can indeed be constituted by a company's "mere presence" at the premises of another enterprise, accompanied by examples on the disposal-concept in Art. 5 of the OECD Commentary, paras. 11 f.

Consequently, the right-of-use-prong cannot be ascertained based on a positive definition; rather, its requirements are circled out based on agreements on what it does not require, e.g. the rejection of the argument that "at-the-disposal" equals "to have a legal right over the place of business".

Today's controversies on the right-of-use-prong do not concern obvious places which qualify as a permanent establishment, e.g. buildings when they are evidently at the disposal of the enterprise by, for instance, possessing the keys for it.²¹ But there exist several nuances which can render the right-of-use-condition controversial. For instance, and taking the key example, can an enterprise also be deemed to exercise the right of use

¹⁴ OECD Commentary, Art. 5 para. 38, 44, 64; see also Skaar 1991, pp. 155 et seq.; Sasseville/Skaar, pp. 35 et seq.

¹⁵ Vogelsang, p. 100; *Wassermeyer* in: Wassermeyer/Kaeser/Schwenke/Drüen/Jülicher, Art. 5 para. 42a.

¹⁶ OECD, Interpretation and Application of Article 5 (Permanent Establishment) of the OECD Model Tax Convention, 2012, p. 5; Williams, pp. 31 et seq.; Wassermeyer in: Wassermeyer/Kaeser/Schwenke/Drüen/Jülicher, Art. 5 para. 24.

¹⁷ Vogelsang, pp. 110 et seq.; Skaar 1991.

¹⁸ OECD, Interpretation and Application of Article 5 (Permanent Establishment) of the OECD Model Tax Convention, 2012, p. 10.

¹⁹ OECD Commentary, Art. 5 para. 10.

²⁰ OECD, Issues Arising under Art. 5 (Permanent Establishment) of the Model Tax Convention, 2002 in: OECD. Model Tax Convention on Income and on Capital, 2019, pp. R(19)-11, para. 27; see also OECD Commentary, Art. 5 para. 124; Dürr/Rumo 1999, p. 398.

²¹ Vogelsang, p. 110 with further references.

when it is granted access to a piece of land and/or buildings of a third party? And does this access need to be granted in a specific form; e.g. would only leasing contracts satisfy the right-of-use-requirement for an enterprise which does not hold any buildings itself but has merely access to a third party's premises?²²

Admittedly, the issue of the right-of-use-condition is rather abstract on what renders the control of premises to the enterprise; in any event, and in order to assume a permanent establishment, the premises must qualify as a place of business which – as clarified above under the tangible-nature-prong – can be constituted by any physical or tangible object. In order for subjecting the enterprise to taxation in the Contracting State, the enterprise then needs, secondly, to exercise the right of use over the place of business. As got clear in the previous section, the right of use can be doubtlessly affirmed in cases where the enterprise is the owner of the premises and/or the buildings, while a range of other possible ways to exercise a right of use, for instance granted access to the premises of a third party, may pose controversial issues on whether the at-the-disposal-requirement is satisfied. Unfortunately, in absence of a positive definition of the at-the-disposal-requirement, discussion circles around rather abstract assumptions.

In any event, and as gets clear at this stage, it is primarily the tangible-nature and right-of-use-prong which are at issue when discussing the Federal Fiscal Court's decision to consider a locker as a fixed place of business under Art. 5(1) OECD Model Tax Convention. However, there are several other tests apart from the place-of-business-test which are required for assuming a permanent place of business of an enterprise in order to render it taxable in the Contracting State.

3.2.2. Fixation-test

The wording in Art. 5(1) OECD Model Tax Convention implies that a permanent establishment can be affirmed only where it has a stable geographical location.²³ Indeed, the idea of a stable geographical location is based on conditions of the nineteenth century's industrial revolution and referred to factory buildings which were located in one state and belonged to a (mother) company in another.²⁴

As with the tangible-nature-prong discussed above, there are no issues considering a building as "fixed" in one state. However, the fixation-test is further bound on time-requirements, e.g. under Art. 5(3) OECD Model Tax Convention, a permanent establishment can only be assumed where it persists for at least some months in the Contracting State. Accordingly, the fixation-test can be split into two distinct requirements:

(1) first, the place of business at issue needs to be linked to a geographical location (geographical link),

²² OECD Commentary, Art. 5 para. 11, 15, 17; Skaar 1991, pp. 188 et seq., 185

²³ Skaar 1991, p. 73.

²⁴ Schaffner 2013, p. 5.

(2) second, this link needs to last for a minimum of months (duration).²⁵

The geographical-link-requirement – as the OECD Model Convention falls under the international law – can be interpreted according to its ordinary meaning inferred by Art. 31(1) VCLT.²⁶ Under this interpretation, "fixed" and "place" do not require a place of business to be irremovable or inseparable from a piece of land;²⁷ rather, and on the one hand, the wording of Art. 5(1) OECD merely requires that the place of business persists at the same ground;²⁸ on the other hand, the wording does not per se restrict movements within the place of business.²⁹

As regards the duration-prong, the wording "fixed" implies that the place of business supports a certain period of time;³⁰ in other words, a business which is only carried out temporarily in the Contracting State will not qualify as a permanent establishment.³¹ Precisely, the OECD Commentary suggests some degree of consensus on the minimum amount of months which are necessary to satisfy the duration-prong (six months³²) while the OECD Model Convention itself at no point sets out a precise minimum duration besides Art. 5(3) OECD for building sites, etc. (twelve months).

Primarily, the lack of any precise duration requirement in Art. 5 OECD Model Tax Convention is based on two aspects:

- (1) first, Contracting States could hardly agree on fixing a minimum duration and
- (2) secondly, sought to leave it open for their disposal to shape double taxation conventions according to their needs.³³

As a consequence, it is up to the states to formulate precise duration requirements so as to avoid double taxation; among scholars, the presumption of a minimum duration of six months appears to be settled.³⁴ In contrast, a place of business which is carried out for the purpose of one single transaction can be considered as limited in time and thus temporary, which in turn in no event satisfies the duration-requirement.³⁵

The question then is how to handle interruptions in conducting business in the Contracting State, for instance, if the economic situation makes it more advantageous for a company to leave the Contracting State for some time. Here, scholars agree that interruptions which can be deemed short or insignificant do not hinder a place of business

²⁵ Reimer 2016, Part 2, para. 61.

²⁶ Vienna Convention on the Law of Treaties, concluded in Vienna on May 23, 1969.

²⁷ OECD Commentary, Art. 5 para. 21.

²⁸ Reimer 2016, Part 2, para. 40; also see OECD Commentary, Art. 5 para. 21.

²⁹ Larking, p. 267.

³⁰ Vogelsang, p. 79.

³¹ OECD Commentary, Art. 5 para. 28; Reimer 2016, Part 2, paras. 79 et seq.; but see critically: Sasseville/Skaar, p. 28.

³² OECD Commentary, Art. 5 para. 28.

³³ Reimer 2016, Part 2, para. 65.

³⁴ Meuter, p. 11.

³⁵ Hilty, Art. 5, p. 35.

from fulfilling the duration-requirement;³⁶ however, what interruptions exactly qualify as "short" or "insignificant" are not clarified. The OECD Commentary itself is silent on the issue³⁷ while scholars focus on the intention of the enterprise: if it intends to conduct business in the Contracting State for more than the minimum amount of months it shall be deemed as satisfying the duration-requirement beginning from the first time of recurrent business activity.³⁸

Concluding at this point, the fixation-test requires both a geographical link of the place of business to the Contracting State and a certain persistence of its conducting business, while the concrete circumstances of short and insignificant interruptions have not yet been clarified. Besides the fixation and the place-of-business-tests outlined in the previous section, the wording of Art. 5(1) Model Tax Convention finally suggests another element in order to assume a permanent place of business:

3.2.3. Business-activity-test

Any permanent establishment needs to conduct business which is carried out through this establishment. The conducting business through an establishment is defined in Art. 3(1)(h) OECD and requires an enterprise performs "professional services" or "other activities of an independent character". Primarily, the performance-requirement means that inactive places of business cannot constitute a permanent establishment because at this place, no business is conducted through it; in other words, the mere fact that an enterprise holds property in the Contracting State, gains passive income or interests, rents, royalties, or dividends without any active business activity does not constitute a permanent establishment.³⁹

Specifying the business-activity-requirement, only those activities can be considered as "business" which are carried out in order to achieve the general purpose of the enterprise;⁴⁰ in contrast, the mere leasing of property does not fall under the scope of activity which is necessary for satisfying the performance-requirement.⁴¹ For instance, and referring to the at-the-disposal-prong set out above, a real estate proprietor will not qualify as a permanent establishment unless he retains some degree of authority and has a veto-right to decisions of the tenant, can make managerial decisions, and assumes a minimum of economic risks.⁴²

Generally, and agreed upon in the literature, the performance-requirement needs to be interpreted broadly particularly because Art. 5(4) OECD, in its negative definition, limits the occasions for assuming a business activity.⁴³

³⁶ OECD Commentary, Art. 5 para. 32; Reimer 2016, Part 2, para. 79.

³⁷ Reimer 2016, Part 2, para. 79.

³⁸ Reimer 2016, Part 2, paras 83 et seq.

³⁹ OECD Commentary, Art. 5 para. 35 et seq.; *Görl* in: Vogel/Lehner, Art. 5 para. 25; Vogelsang, p. 89; but see critically: Reimer 2016, Part 2, paras. 20, 122.

⁴⁰ Schreiber/Honold/Jaun in: Zweifel/Beusch/Matteotti, Art. 5 para. 9; Häck in: Flick/Wassermeyer/Kempremann, Art. 5 para. 27; Vogelsang, p. 90.

⁴¹ OECD Commentary, Art. 5 para. 37; Reimer 2016, Part 2, para. 26.

 $^{^{42}}$ Reimer, 2016, Part 2, para. 26; but see critically: De Vries Reilingh 2010, p. 127.

⁴³ Schreiber/Honold/Jaun in: Zweifel/Beusch/Matteotti, Art. 5 para. 9.

Further, the wording in Art. 5(1) Model Tax Convention "through (the permanent establishment)" first indicates a certain degree of functional integration in the enterprise which is to be subjected to taxation in the Contracting State; second, it indicates that the business is conducted by no other person than the enterprise itself, or that the activity carried out by a third party can be attributed to the enterprise. This attribution-prong is exactly the issue when assessing the German Fiscal Court's decisions, where it was a subcontractor who possessed a locker in Germany; in other words, and recalling the initial clarification on the status of an agent, what requirements must be satisfied in order for legitimately attributing a subcontractor's business activity to the taxpayer enterprise?

Firstly, for the functional-integration-prong to be fulfilled, the wording "through" in Art. 5(1) OECD Model Tax Convention implies that the place of business is the instrument through which the business activity is carried out (and not its object). 44 Referring again to the leasing of property example from above, the leasing itself does not qualify as business activity carried out "through" the place of business in the meaning of Art. 3(1)(h) OECD Model Tax Convention when it has the sole purpose of gaining rental income for the enterprise and, consequently, does not constitute a permanent establishment. 45

The OECD Commentary in Art. 5, para. 20 suggest that the term "through which" needs to be interpreted broadly⁴⁶ so that any activities which are controlled by the enterprise's personnel will fall under functional-integration-prong.⁴⁷

The attribution-prong, as indicated above, is highly relevant for discussing the German Fiscal Court's locker-decision. Precisely, the business activity carried out in the Contracting State under Art. 5(1) OECD Model Tax Convention must be able to be legitimately considered as that *of* the enterprise.⁴⁸ With this requirement, Art. 5(1) OECD Model Tax Convention separates whether it is the enterprise which is to be subjected to taxation or the third party who physically conducts the business instead;⁴⁹ in other words, to whom can the business activities carried out be attributed to and who, thus, needs to be taxed?

In the standard case, the business activities in the Contracting State will be performed by the enterprise's personnel, which is then doubtlessly attributable to the enterprise.⁵⁰ According to Art. 5, para. 39 OECD Commentary, "personnel" covers all "persons who are paid in a paid-employment relationship with the enterprise (personnel);" obviously, all employees of the enterprise qualify as personnel as well as all other persons who are instructed by the enterprise; that is, dependent agents under the definition laid out in the first section.

The crucial issue then is whether subcontractors – as in the German Fiscal Court's decision – qualify as dependent agents. According to the OECD, the absence of fixed personnel does not per se prevent a place of business from constituting a permanent

⁴⁴ Reimer 2016, Part 2, paras. 124 et seq.; Vogelsang, p. 96.

⁴⁵ Reimer 2016, Part 2, paras. 26 et seq.; Williams, p. 88.

⁴⁶ Reimer 2016, Part 2, para. 128; Vogelsang, pp. 95 et seq.; but see critically: *Häck* in: Flick/Wassermeyer/Kempremann, Art. 5 para. 31; Sasseville/Skaar, p. 43; Reimer 2016, Part 2, para. 129.

⁴⁷ Reimer 2016, Part 2, paras. 111 et seq.; Vogelsang, pp. 115 et seq.

⁴⁸ Sasseville/Skaar, p. 43.

⁴⁹ Sasseville/Skaar, p. 39.

⁵⁰ OECD Commentary, Art. 5 para. 39; Sasseville/Skaar, p. 39.

establishment⁵¹ because in an economic perspective, agents can be necessary when personnel in a fixed paid-employment relationship is inappropriate for the enterprise to achieve its business aims in the Contracting State. The question then is under which circumstances the activities carried out by third parties other than employees can be deemed attributable to the enterprise.

Basically, subcontractors can be considered as (dependent) agents fulfilling the attribution-requirement if they are either (1) subordinated to the enterprise ("vertical attribution")⁵² or if they are on an equivalent footing with the enterprise ("horizontal attribution").⁵³

Vertical attribution in this sense primarily covers business activities which are carried out by dependent agents, while horizontal attribution refers to joint ventures or partnerships between the third party and the enterprise. As in the case discussed here before the German Fiscal Court, vertical attribution primarily occurs in multinational enterprises which hire agents (and personnel) for their affiliated companies in the Contracting State.⁵⁴

For instance, and taking the situation in the Fiscal Court's case, the aircraft manufacturing enterprise A mandated a third party – subcontractor B – for conducting maintenance activities at a place of business in Germany; B was not in a fixed paid-employment relationship with A and rather had a subcontractor-status, with the questions arising whether B's activities could be attributed to A and thus constitute its permanent establishment in Germany.

Besides the Fiscal Court's decision, the scholarship appears to have two differing views on the issue:

(1) according to one view and in order for attributing the subcontractor's activities to the enterprise, the former must be fully controlled and supervised by the enterprise as the principal.⁵⁵ Only in this case, the subcontractor's activities at the place of business can be attributed to the enterprise and the latter therefore be subjected to taxation in the Contracting State.⁵⁶ This view appears to be supported by the OECD because the OECD Commentary makes it clear – as outlined above – that an enterprise does not need to have

⁵¹ OECD Commentary, Art. 5 para. 36, 39, 127; Robinson, p. 1272.

⁵² Vogelsang, p. 117.

⁵³ Vogelsang, p. 115.

⁵⁴ OECD, Interpretation and Application of Article 5 (Permanent Establishment) of the OECD Model Tax Convention, p. 15.

⁵⁵ OECD, Interpretation and Application of Article 5 (Permanent Establishment) of the OECD Model Tax Convention, p. 19; Reimer 2016, Part 2, para. 115.

⁵⁶ OECD, Are the Current Treaty Rules for Taxing Business Profits Appropriate for E-Commerce?, Final Report of the Technical Advisory Group on Monitoring the Application of Existing Treaty Norms for Taxing Business Profits, June 2004, p. 30; OECD Commentary, Art. 40, para. 40.

personnel in paid-employment relationships for constituting a permanent establishment.⁵⁷

(2) the second view in the literature expresses a more restrictive opinion and suggests that under Art. 5(6) OECD Model Tax Convention, an independent agent's activities cannot be attributed to the enterprise for taxation purposes under Art. 5(1).⁵⁸

As a consequence of the second view, a subcontractor who qualifies as an independent agent within the definition laid out in the first section of this paper would not satisfy the attribution-requirement, and the enterprise's place of business would thus not constitute a permanent establishment in the Contracting State.⁵⁹

Concluding for the fixation-test at this point, business activities at the place of business in the Contracting State do not per se qualify as attributable to the enterprise, particularly when they are carried out by more than one party, e.g. subcontractors. Precisely, in order for an enterprise to be subjected to taxation under Art. 5 OECD Model Tax Convention, a subcontractor must have the status as a dependent agent, which in turn requires that he is supervised by and receives instructions from the enterprise-principal. Here, Art. 5(5) OECD Model Tax Convention makes it explicit that a permanent establishment can also be assumed when

"an agent of an independent status (...) is acting on behalf of an enterprise and has, and habitually exercises, in a Contracting State an authority to conclude contracts in that State in respect of any activities which that person undertakes for the enterprise (...)."

In contrast, Art. 5(7) states that the mere existence of a subsidiary resident does not amount to a permanent establishment so as to subject the parent company to income taxation and the resident state's tax law.⁶⁰

With the theoretical background of what constitutes a permanent establishment under Art. 5(1) OECD Model Tax Convention, it now remains to discuss and assess the German Fiscal Court's considering of a subcontractor's locker as a permanent establishment.

4. Discussion

As indicated above, presented at the German Fiscal Court was the issue of a natural person-subcontractor ("plaintiff") who had the status of an aircraft-engineer and was licensed to maintain aircrafts of the type Airbus A300 and Boing 757. During the years at

⁵⁷ OECD, Preventing the Artificial Avoidance of Permanent Establishment Status, Action 7/2015 Final Report, p. 28; OECD, Addressing the Tax Challenges of the Digital Economy, Action 1/2014, Deliverable, p. 143; OECD Commentary, Art. 5, para. 129.

⁵⁸ Williams, pp. 51 et seq.

⁵⁹ OECD Commentary, Art. 5 para. 103.

⁶⁰ See on this point *Lang*, Bulletin for International Fiscal Documentation (2003), p. 55.

issue (2008 until 2010) he lived in Germany as well as in Great Britain while his main place of residence was Great Britain.

During the years at issue, he maintained aircrafts based on a freelancer contract on behalf of an English company incorporated as a limited ("English Ltd.") at an aircraft hangar in Germany. The English company itself conducted its business on behalf of the English operator of the aircrafts which was also incorporated as a limited ("English operator").

The plaintiff argued that he was an employee of the English operator who itself, according to the plaintiff, had the status of a subcontractor in relation to the English Ltd. The German Federal Central Tax Office ("Bundeszentralamt für Steuern") instead argued that the operator needed to be qualified as an economically inactive phantom company ("Briefkastenfirma"). Accordingly, the respective tax office in Saxony treated the English Ltd.'s income gained from the maintenance work of the plaintiff as unlimitedly taxable in Germany, e.g. as income gained from self-employment. Precisely, the tax office maintained that the plaintiff used the English operator as an excuse where he was the actual contractor to the English Ltd., and that, consequently, Germany was granted the right to tax the income because he maintained the premises rented by the English Ltd. according to Art. XI sec. 1 sentence 1 of the Tax Convention between Germany and Great Britain.⁶¹

The Federal Fiscal Court stated that, generally, Germany has a right for taxation only when an enterprise can be considered to have a permanent establishment in its jurisdiction as described under Art. 5 OECD Model Tax Convention and when the place of business is at its disposal. Such a right of disposal – in accordance with the outlined assumptions of the scholarly opinion in the previous sections – cannot be assumed if the English Ltd. is merely granted access to the premises on behalf of a third party. Rather, for constituting a permanent place of business, there need to exist further circumstances beyond legal entitlements which suggest a certain degree of fixation in the meaning outlined above ("gewisse Verwurzelung").

Here, the Federal Fiscal Court affirmed the plaintiff's status as an independent agent because he had no ties to the English Ltd. whatsoever which could have resembled a paid-employment relationship. Specifically, the plaintiff had to provide his maintenance equipment himself, and for this purpose possessed a locker next to the hangar at his sole disposal and marked with his name. The mere fact that the hangar was rented by the English Ltd. (and not by the plaintiff himself) did not render their relationship a paid-employment relationship.

The court then raised the decisive question whether it can be deemed sufficient for taxation purposes when the subcontractor's main contractor provides a locker-room for the former's equipment and where these premises could also be provided to other subcontractors. This question touches the tangible-nature and right-of-use-prong under the place-of-business-test explained above, and which – with reference to the scholarly opinion – are generally established by any physical or tangible object such as, for instance, a building; under the right-of-use-prong, the company which shall be held taxable in the

⁶¹ BGBl II 1966, 359, BStBl I 1966, 730; BGBl II 1971, 46, BStBl I 1971, 140.

Contracting State then further needs to exercise the right of use over the place of business, e.g. the physical or tangible object at issue.

According to the Federal Fiscal Court, a permanent establishment in accordance with Art. 5(1) Model Tax Convention could be assumed in the plaintiff's case because for the whole duration of the contract, the English Ltd. provided him with a locker at his own disposal and for the sole purpose of the contractual issue – maintenance services on behalf of his contractor. The court thereby effectively rejected the plaintiff's argument that he qualified as an employee because he only stored his equipment in the locker when he conducted maintenance activities for his English Ltd. contractor. Specifically, the Fiscal Court argued that the locker had the purpose of safely storing the maintenance equipment in both times where the plaintiff conducted maintenance services for the contractor and when he did not.

Further, the court made it clear that the use of premises provided to a subcontractor neither require a minimum scope nor do they need to be of a certain relevance for the contractor; that is, even premises of minor relevance, e.g. secondary services, can satisfy the fixed-place-of-business-requirement. Consequently, the locker-room, according to the Court, could be considered a physical object which also was at the English Ltd.'s disposal because it could further rent it to other subcontractors besides the plaintiff. Overall, the English Ltd. appeared to thus have a permanent establishment in Germany in the sense of Art. 5 Model Tax Convention which made it taxable according to German Tax law.

The research question of this article 'Which criteria have to be met by a permanent establishment to be effective for tax purposes?' could therefore be fully answered.

5. Conclusion

As needs to be concluded from the German Federal Fiscal Court's decision, a permanent place of business can only be assumed where it has a physical or tangible object at its disposal in the Contracting State. Importantly, and as the distinctive issue in this case, a permanent place of business can be assumed even when the premises are of no obvious relevance to the contractor-principal; precisely, and as decided by the Fiscal Court, a fixed place of business can be established even through a locker-room which does not directly support the company's business activity, but is provided for the storage of their subcontractors' items.

As concluded by the German Fiscal Court, it is then sufficient for assuming a permanent establishment of an enterprise under Art. 5 Model Tax Conventions where the subcontractor-agent can be considered as being provided with premises, even though it may be as tiny as locker, and accordingly be subjected to income taxation under German law.

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