

Danish Tax Authority rules subcontracting of services by foreign company to non-related foreign entity creates a permanent establishment in Denmark

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Executive summary

In a binding ruling published 23 August 2017 (SKM2017.509.SR), the Danish Tax Board ruled that a foreign company would create a permanent establishment in Denmark based on a service contract with a Danish company, under which the foreign company would subcontract services to a foreign non-related entity. The Danish Tax Board ruled that the subcontractor would be carrying out the foreign company's business through a fixed place of business in Denmark, since the subcontractor's work in Denmark would be part of the foreign company's overall business activity.

Detailed discussion

Facts

An Austrian company requested a binding ruling on the exposure of creating a permanent establishment (PE) in Denmark as a consequence of entering into a service contract with a foreign non-related subcontractor for services to be performed in Denmark.

The Austrian company completed a construction project in 2016 for the construction of a building for a Danish company in Denmark. The income generated in connection with this project was subject to taxation in Denmark. The Austrian company and the Danish company are planning to enter into a new contract regarding servicing of the building.

For the purpose of the service contract, the Austrian company is in the process of hiring a foreign non-related subcontractor. The services comprised by the contract will be assistance with the daily operations as well as cleaning and maintenance of the building facade. The expected duration of the contract is 10 years. The Austrian company will not carry out any of these activities in Denmark. Any meetings regarding the service contract would be held outside Denmark. The Austrian company would not have an office at their disposal in Denmark and would not have any employees working in Denmark for the purpose of the service contract. Any questions that the Danish client would have would be discussed with the subcontractor.

Decision

With reference to the Danish Corporate Tax Law, the Danish Tax Board stated that a foreign company that is carrying out business in Denmark is subject to limited tax liability in Denmark. The PE determination should be interpreted in accordance with Article (Art.) 5 of the Organisation for Economic Co-operation and Development Model Tax Convention (OECD MTC) including the commentaries.

In the case at hand, the double tax treaty between Austria and Denmark should be applied, which has the same wording as Art. 5 as the OECD MTC.

The Danish Tax Board referred to the contract between the Austrian company and the Danish company, according to which the Danish company would make offices and storage facilities available to the Austrian company. The Danish Tax Board was informed that the premises would be used by the subcontractor only. The Danish Tax Board ruled that according to the wording of the contract between the Austrian company and the Danish company, the Austrian company would have a place of business in Denmark at its disposal regardless of the fact that the services would be outsourced to a subcontractor.

Furthermore, according to the contract between the Austrian company and the Danish company, the Austrian company would only be able to transfer its rights and/or obligations to a third party if a preceding written acceptance had been

obtained. Furthermore, the Austrian company could only use subcontractors for the performance of the contract, if a preceding written acceptance had been obtained. As no final contract had been signed between the Austrian company and the Danish company or between the Austrian company and the subcontractor, such written acceptance by the Danish company for the use of a subcontractor was not available.

Based on the Danish Tax Board's understanding, the Austrian company would remain liable for the execution of the work. This meant that the rights and obligations towards the Danish company were not transferred to the subcontractor. According to the recommendations prepared by OECD Committee on Fiscal Affairs on the interpretation and application of Art. 5, item 8, a foreign company that performs business in another country through a subcontractor can create a PE if the other requirements for creating a PE according to the OECD MTC Art. 5 are met.

The Danish Tax Board ruled that a fixed place of business would be at the Austrian company's disposal due to the contract with the Danish company. Furthermore, the subcontractor would be carrying out the Austrian company's business in Denmark through the fixed place of business, as the activities performed by the subcontractor in Denmark would be part of the Austrian company's overall business.

The Danish Tax Board took into account that the Austrian company would have offices and storage facilities at their disposal in Denmark, that they would have rights and obligations towards the Danish company, and that the activities performed by the subcontractor would be part of their overall business.

Based on this, the Danish Tax Board ruled that the Austrian company would have a PE in Denmark according to the proposed service contract, even though they would outsource the work to be performed in Denmark.

Implications

This ruling is generally in line with the interpretation of the fixed place requirements set forth by the Danish tax authorities.

This ruling establishes that the risk for creating a fixed place PE in Denmark for nonresident companies should be considered when there is: (i) a possibility that the foreign company has a place at their disposal in Denmark simply via contractual terms; and (ii) outsourcing of core business activities carried out in Denmark to subcontractors.

For additional information with respect to this Alert, please contact the following:

Ernst & Young P/S, Copenhagen

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|------------------------|---------------|---------------------------------|
| ▶ Vicki From Jørgensen | +45 5158 6232 | vicki.from.joergensen@dk.ey.com |
| ▶ Maja Gelineck | +45 2529 5904 | maja.gelineck@dk.ey.com |
| ▶ Emilie L Stentoft | +45 2529 3835 | emilie.l.stentoft@dk.ey.com |

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