European Union:  
CJEU rules on VAT fixed establishments

The Court of Justice of the European Union (CJEU) issued a decision on 16 October 2014 on the issue of whether a customer that receives an intra-EU supply of services should be treated as having a “fixed establishment” for VAT purposes in the member state of the supplier. The Welmory sp. z o.o. case involved an internet auction site operated by a Cypriot company using infrastructure located in Poland. The key issue was whether the Cypriot company had a fixed establishment in Poland where the services were received for VAT purposes, which would result in the Polish supplier having to account for Polish VAT. The CJEU confirmed the requirements for creating a fixed establishment and remanded the case to the referring Polish court to determine whether a fixed establishment existed.

The concept of “fixed establishment” for VAT purposes initially was developed by CJEU case law and then was defined in EU VAT law. It means an establishment other than an organization’s business establishment (i.e. its head office, or main seat of power) from which its activities are carried out and that involves the permanent presence of both human and technical resources necessary for making or receiving supplies. Services may be deemed to be supplied or received by a fixed establishment only where it is inappropriate to deem that the supplies in question have been provided at or from the place where the entity has its business establishment.

Background

Welmory Poland entered into a cooperation agreement with Welmory Cyprus, under which Welmory Cyprus operated an auction website in Poland. Welmory Poland then supplied the auctioned goods to customers under its own name and for its own account. Welmory Cyprus used Welmory Poland’s employees and technical equipment, located at Welmory Poland’s offices in Poland, to run and manage the website. Welmory Cyprus’ own core infrastructure was located outside of Poland.

On the basis of the cooperation agreement, Welmory Poland billed Welmory Cyprus for its services without charging Polish VAT, believing that Welmory Cyprus should account for VAT in Cyprus under the reverse charge mechanism that applies to general business-to-business supplies (that is, a service is subject to VAT in the place where the recipient is established). The Polish tax authorities disagreed, concluding that Welmory Cyprus had a fixed establishment in Poland because it was using Welmory Poland’s infrastructure and, therefore, Welmory Poland should have charged Polish VAT on the services. The case eventually went before a Polish court that referred the case to the CJEU.

Advocate General (AG) Kokott issued her opinion in the Welmory case on 15 May 2014, stating that it is up to the national courts to determine whether a company has a fixed establishment. For a fixed establishment to exist, she stated that the company must have a certain degree of permanence in the relevant member state, as well as the human and technical resources to supply/receive the relevant services. However, AG Kokott also opined that it is not necessary that the human and technical resources be the company’s own resources – it is sufficient that the company have access to third-party resources in the relevant member state in a way that is “comparable” to the access it would have to its own
resources. This opinion, if followed by the CJEU, could have had far-reaching VAT implications for many businesses operating across Europe that share or utilize third-party resources.

CJEU decision

The CJEU did not follow the AG’s interpretation that would have taken third-party resources into consideration in defining a company’s “human and technical resources,” which could have broadened the circumstances under which a fixed establishment would be considered to exist. Instead, the court reconfirmed the earlier two-pronged test for ascertaining whether a fixed establishment exists, and stated that it is up to the national courts (the Polish court, in this case) to determine, based on the facts, whether the relevant characteristics are present in a specific case, in light of the following principles:

- The starting point for determining the place of supply of services is the place where the taxable person has a business establishment, and only if that place of business leads to an “irrational result” for VAT purposes may another (fixed) establishment be considered; and
- A fixed establishment is characterized by a sufficient degree of permanence and a suitable structure in terms of human and technical resources to enable the taxable person to receive the services supplied to it and use them for its business, and this is an issue for the national courts to decide.

The CJEU also noted the following points:

- In terms of the human and technical resources required to create a fixed establishment, it is necessary to consider what is appropriate for the business in question. Relevant factors may include the presence of equipment, such as computer equipment and servers, and associated human resources (e.g. for maintaining and servicing equipment) and the place where contracts are concluded.
- The fact that the economic activities of two companies are linked by a cooperation agreement and form an economic whole is not material for determining the existence of a fixed establishment.
- The decision confirms that the case law on the interpretation of fixed establishments is still relevant after the introduction of the EU VAT package on 1 January 2010 that updated the place of supply rules for the provision of services within the EU.

Comments

While the CJEU’s decision reconfirms the application of existing EU case law, it does highlight the importance of considering the specific facts of each case. In particular, this should include determination of the following:

- The nature of the services being provided;
- The contractual position between the parties;
- The location of the business establishments involved; and
- Whether an irrational result is created by following the corresponding VAT treatment.
Businesses operating in Europe with a presence in multiple countries (e.g. through branches, subsidiaries or human and technical resources such as employees, contractors, servers, manufacturing equipment, etc.) should consider reviewing their arrangements to identify potential risk areas and prepare for potential challenges from the tax authorities (which could result in additional VAT registration obligations, or in overseas VAT being incurred).

— Benno Tamminga (New York)  
Director  
Deloitte Tax LLP  
btamminga@deloitte.com

Phil Walton (Chicago)  
Manager  
Deloitte Tax LLP  
phwalton@deloitte.com

Steve Butler (Los Angeles)  
Manager  
Deloitte Tax LLP  
stebutler@deloitte.com

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