

PE Watch: Latest developments and trends, August 2020

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PE case law developments

India

On 22 July 2020, the Supreme Court of India rendered its decision in the case of *Director of Income Tax-II (International Taxation) New Delhi & Anr. & M/S Samsung Heavy Industries Co. Ltd (Civil Appeal No. 12183 of 2016)*. In this case, the taxpayer, a company incorporated in South Korea, was a party to a consortium being awarded a turnkey contract by an Oil and Gas company. The taxpayer set up a project office (PO) in India to act as a "communication channel" between the taxpayer and its customer. The activities undertaken by the PO comprised coordinating and executing the delivery of documents in connection with the construction of an offshore platform modification. The PO was not involved in the coordination or execution of the entire project itself and had just two employees, neither of whom was qualified to perform any core activities of the taxpayer. The main issue in dispute was whether the PO constituted a permanent establishment (PE) of the taxpayer in India and whether the profits arising from the commissioning of the turnkey project, if any, was attributable to such PE.

The Supreme Court ruled in favor of the taxpayer that the activities performed by the PO did not give rise to a fixed place PE and were of a preparatory or auxiliary character. The Supreme Court reasoned that the PO was not a fixed

place of business through which the core business of the taxpayer was wholly or partly carried on; the PO was an auxiliary office meant to act as a liaison office between the taxpayer and its customer, and hence falling within the scope of specified exempt activities under Article 5(4)(e) of the India-South Korea tax treaty.

While the Supreme Court did not specifically address this aspect, it has cited certain past Supreme Court rulings holding that offshore profits are not taxable in India where such profits are independent to the PE.

South Korea

On 25 June 2020, the Supreme Court of South Korea rendered its decision in the case [2017Du72935](#) dealing with the attribution of profits to a PE in South Korea.

In this case, the taxpayer is a Philippines tax resident company (i.e., junket operator) which was engaged by a South Korea casino operator to bring in overseas high rollers to play at the casino. Some employees of the Philippines company provided guidance to the high rollers and exchanged casino tokens in an office forming part of the casino. The Korean tax authorities considered that the activities performed by the Philippines company at the casino would create a PE, and consequently, the tax authorities imposed corporate income tax and value-added tax (VAT) on the basis that all income should be attributable to the PE.

The Supreme Court ruled in favor of the taxpayer and upheld that although the business activities of the Philippines company can constitute a PE in South Korea, the amount of profits attributable to the PE should be assessed under a functional analysis. The Korean tax authorities failed to prove through an objective analysis that the main activities performed by the Philippines company, were performed in South Korea. Therefore, the Supreme Court ordered annulment of the tax authorities' assessment in its entirety.

PE tax rulings

Turkey

The Turkish Revenue Administration (TRA) recently published [Tax Ruling No. 22927](#), dated 20 April 2020. This tax ruling was requested by a Turkish individual to determine if he would have a taxable presence in Turkey for the provision of digital services to his Turkey customers. The TRA responded that the activities carried out on a continuous basis by the individual may potentially earn income, and therefore, the individual

would be considered to be engaged in commercial activities in Turkey. Further, the TRA clarified that the domestic definition of a place of business is not exhaustive and a website could also be a place for the purposes of performing commercial activities. In light of this, the TRA concluded that the individual has a taxable presence in Turkey and would be subject to tax in accordance with the provisions applicable to commercial earnings included in the Income Tax Law.

Ukraine

On 1 July 2020, the State Fiscal Service (SFS) of Ukraine published a tax ruling whereby it considered how to calculate profits of a PE following the 2020 tax reform. In this ruling, a company with a PE in Ukraine determined the profits of the PE under the so called "indirect method" (whereby the taxable profits of a PE are deemed to be 30% of its income regardless of actual expenses). The company asked the SFS whether it could continue applying the same method for calculating the profits of the PE or should it apply the general procedure applicable to Ukraine resident companies using the arm's-length principle. In that respect, the SFS confirmed that following the 2020 tax reform, a PE needs to calculate its profits following the general procedure applicable to Ukraine resident companies.

This change to the tax base calculation in the middle of the 2020 reporting year was caused by the enactment of the Law No.466-IX that reformed numerous tax matters, including the PE definition and taxation. Therefore, all PEs of nonresident companies which used the "indirect method" to determine taxable profits should now follow the general procedure applicable to Ukraine resident companies using the arm's-length principle.

PE developments in response to COVID-19

Austria

On 20 July 2020, the Austrian Ministry of Finance published [guidance](#) on various international tax issues. This guidance replaces the guidance that was previously issued on 22 May 2020 regarding the same issues. With respect to PEs, the main difference under the updated guidance is the removal of a reference to a consultation agreement between Germany and Austria regarding the application and interpretation of the time threshold for a Construction PE under the applicable tax treaty.

Greece

On 22 July 2020, Greece published a [circular](#) on some of the international tax issues arising as a consequence of COVID-19. Among other topics, the circular provides that employees will not constitute a home office PE unless the home office becomes the new norm. Likewise, the risk of creating an Agency PE would be low as long as the agent's activity is temporary and would not have been performed in Greece but for the travel restrictions. However, the tax authorities may take a different approach if the agent was habitually concluding contracts on behalf of the nonresident enterprise in his home country before COVID-19. Further, if a construction project is interrupted due to COVID-19, the interruption period should be included when calculating time threshold.

Although the circular is generally applicable from 18 March 2020 until 15 June 2020, it may also apply retroactively or for a longer period depending on the travel restrictions imposed by other jurisdictions. To this end, interested taxpayers must request the guidance to be applicable to a different period and submit relevant documentation.

Domestic law PE developments

Recently, a number of countries amended their domestic laws to modify certain regulations on PEs, including Cape Verde, Fiji and Pakistan. **Fiji** amended its [Income Tax Law](#), with effect from 1 August 2020, and updated its PE definition by removing the general exception of the definition to Governments and persons in which the Government has an interest. The **Cape Verde** Government published [Law n. 86/IX/2020](#), dated 28 April 2020, that *inter-alia* modifies the PE definition to include some of the elements suggested by the Base Erosion and Profit Shifting (BEPS) Action 7 final report, including: an anti-fragmentation clause, the new wording of agency PE, and the definition of closely-related enterprise. These changes are applicable as from 29 April 2020.

See EY Global Tax Alert, [Cape Verde amends certain tax regimes and introduces Country-by-Country Reporting](#), dated 10 July 2020.

Pakistan

On 30 June 2020, Pakistan published the [Finance Act 2020](#) that, among other things, modifies the taxation of a PE of nonresident companies as from 1 July 2020. Prior to the *Finance Act 2020*, the minimum tax rules were only applicable to Pakistani tax resident companies and foreign companies with a PE in Pakistan were not subject to the minimum tax. The *Finance Act* has now extended the application of the minimum tax rules to nonresident companies with a PE in Pakistan (including a branch). However, the *Finance Act* provides that the tax withheld from payments made to a PE of a nonresident shall be subject to a minimum tax, except where payments are received for the sale of goods by a company being a manufacturer of such goods. This amendment aims to level the playing field between resident companies and PEs of nonresidents.

Tax treaty developments

Kenya

On 13 July 2020, the National Treasury and Planning issued a [public notice](#) requesting public comments on the draft tax treaties with [Barbados](#) and [Singapore](#). In relation to the PE provisions in these tax treaties, the agreement with Barbados contains the BEPS Action 7 suggested language (namely, the contract splitting rule, the specific activity exemptions, an anti-fragmentation clause, the new wording of agency PE, and the definition of "closely related enterprise"). In contrast, the tax treaty with Singapore follows the PE provision language in the OECD Model Tax Convention prior to the 2017 update and also includes a service PE provision. Comments on these Tax Treaties should be forwarded in writing to the Cabinet Secretary by 17 August 2020.

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

Ernst & Young Belastingadviseurs LLP, Rotterdam

- ▶ Ronald van den Brekel ronald.van.den.brekel@nl.ey.com
- ▶ Roberto Aviles Gutierrez roberto.aviles.gutierrez@nl.ey.com

Ernst & Young Belastingadviseurs LLP, Amsterdam

- ▶ David Corredor-Velásquez david.corredor.velasquez@nl.ey.com

Ernst & Young Solutions LLP, Singapore

- ▶ Chester Wee chester.wee@sg.ey.com

Ernst & Young LLP (United States), Global Tax Desk Network, New York

- ▶ Jose A. (Jano) Bustos joseantonio.bustos@ey.com

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