UPDATE

Fixed establishment in VAT

Entrepreneurs with a branch in another country may have a fixed establishment for VAT purposes. This can have consequences for services they supply themselves as well as for services purchased by the entrepreneur. There are also consequences for the liability for VAT, administrative, invoicing and declaratioin obligations, the deduction of input tax and some special schemes. In December 2020, the State Secretary of Finance published new policy on fixes establishments for VAT purposes. We will discuss this policy in this update.

VAT consequences of services to third parties

For entrepreneurs who supply services to parties other than entrepreneurs (e.g. private individuals), the main rule is that a service is taxed in the country where the entrepreneur providing the service is established. Exceptions may apply. In principle, the services are taxed where the entrepreneur has his/her main establishment. If a service is provided by a branch that can be regarded as a fixed establishment for VAT purposes, the service is taxed in the country of that fixed establishment.

In this situation, a fixed establishment is deemed to exist when the branch is sufficiently permanent and the entrepreneur has personnel and technical resources at his disposal to provide services to third parties. This interpretation of the concept of a fixed establishment is relevant for all VAT rules in which the fixed establishment plays a role, except for the determination of where a service is taxed in the case of services between entrepreneurs (see below).

When you provide services to an entrepreneur, it may also be important to determine whether there is a fixed establishment for VAT purposes. However, this concerns the fixed establishment of the customer and not the fixed establishment of the entrepreneur himself. In the case of services between entrepreneurs, the main rule is that services are taxed in the country where the customer is established. When the service is provided to a fixed establishment of the entrepreneur, the service is taxed where the fixed establishment is located. For this purpose, a broader interpretation of the concept of fixed establishment is applied. We will discuss this below under the VAT consequences for the purchase of services.

VAT consequences when procuring services from third parties

When services are purchased from third parties, it is important to determine whether there is a fixed establishment. Here too, the rule applies that the branch must be sufficiently permanent.

The entrepreneur must have personnel and technical means at his disposal that enable him to purchase and use the services on site. It is therefore not required that supplies of goods or services are also provided to third parties by the branch. A branch that performs ancillary or preparatory work can also be considered a fixed establishment in this respect. This is also referred to as a purchase-fixed establishment. This interpretation of the fixed establishment only applies for the application of the principal rule for the place of supply of services between entrepreneurs.

If your customer has a fixed establishment in another country, it is important to determine whether the service is taxed in the country of the head office or the country of the fixed establishment. For this purpose, the VAT legislation contains a step-by-step plan.

Step 1: Firstly, you must consider whether you can establish from the nature or the use of the service that it is intended for the fixed establishment. We can imagine that this would be possible, for example, if you were to provide training for staff at the fixed establishment's location. But there are many cases where it is not possible to establish who uses the service. You may then go to step 2.
Step 2: You determine from the contract, the order, the VAT identification number of the customer and the payment whether the fixed establishment is the one that has purchased the service. If this is also not successful, go to step 3.
Step 3: Step 3 is a catch-all clause. If, on the basis of step 1 and step 2, you do not succeed in attributing the service to the fixed establishment, you may assume that the service has been provided to the head office.

Please note! This step-by-step plan only applies to the service provider who must determine to which establishment the service is provided. The recipient may not use it himself. It is advisable to properly communicate to the service provider which establishment is the recipient of the service in order to avoid double taxation.

Liability for payment of VAT

The main rule is that the VAT is due from the entrepreneur who performs the service. If the entrepreneur is not established in the Netherlands, but the supply is taxed in the Netherlands and the customer is a Dutch entrepreneur, the reverse-charge mechanism applies. This means that the VAT is owed by the recipient who states the VAT owed in the tax return and also deducts this if and insofar as he is entitled to deduct input VAT. A foreign entrepreneur can also shift the VAT to a Dutch fixed establishment. This applies both in the case of a fixed establishment that supplies goods or services to third parties and in the case of a purchasing fixed establishment as described above.

It may also be the case that a foreign establishment of an entrepreneur performs a service for a Dutch customer, whereby that latter entrepreneur has a fixed establishment in the Netherlands. The question then arises whether the reverse charge mechanism can still be applied when the service is taxed in the Netherlands. The reverse charge mechanism can still be applied if the permanent establishment in the Netherlands does not intervene in the service provided. A fixed establishment intervens when the personnel and the technical means of the fixed establishment are used for the supply of goods or services before or during that supply. Intervention does not apply to accounting or administrative support tasks. If the VAT identification number of the fixed establishment is stated on the invoice, then intervention is presumed and the entrepreneur must prove that there is no intervention of the fixed establishment. A purchasing fixed establishment, that does not itself supply services to third parties, cannot be an intervening fixed establishment. The presence of a purchasing fixed establishment in the Netherlands does not preclude the application of the reverse charge mechanism.

The recent decree by the State Secretary contains an example of an intervening fixed establishment. According to the decree, this concerns the situation in which a foreign entrepreneur transfers goods from his principal place of business to his fixed establishment in the Netherlands. The goods are then delivered from his fixed establishment to an entrepreneur in the Netherlands. In that case, the reverse charge mechanism cannot be applied because the fixed establishment has intervened.

If an entrepreneur has his principal place of business in the Netherlands, the reverse charge mechanism cannot be applied, even if that principal place of business is not involved in the supply and the supply is made by a foreign permanent establishment.

Declaration, administrative and invoicing obligations

An entrepreneur who has a fixed establishment through which he supplies goods or services to third parties, will have to register in the Netherlands with the Tax Authorities at the local office in the area where the permanent establishment is situated. He will file a tax return just like a Dutch entrepreneur and will have to comply with the administrative and invoicing obligations in the Netherlands.

If a foreign entrepreneur only has a purchasing fixed establishment in the Netherlands, a fixed establishment that does not provide services to third parties, two situations may occur.

1. The fixed establishment only buys services from Dutch entrepreneurs. In that case, the Dutch entrepreneurs will charge VAT to the fixed establishment. The foreign entrepreneur will have to reclaim this VAT by submitting

an electronic application for the refund of foreign VAT to his own tax authority. If the entrepreneur has no establishments in the EU, the refund application must be submitted in writing to the Dutch Tax Authorities, kantoor Buitenland.

2. The fixed establishment purchases services from entrepreneurs who are not established in the Netherlands. In that case the fixed establishment owes the VAT on these services based on the reverse charge rule. The fixed establishment then registers for VAT with the Dutch Tax Authorities, kantoor Buitenland. Here, the entrepreneur will declare the reverse-charged VAT and deduct it via the same return if and insofar as the entrepreneur is entitled to deduct input tax. In this case, the administrative obligations as they apply under Dutch VAT legislation will also have to be met, too.

Deduction of input tax

When a foreign entrepreneur has a fixed establishment in the Netherlands, he must submit a VAT return in the Netherlands and can also deduct input VAT. The starting point here is that it must be examined whether the activities of the fixed establishment itself give rise to a right of deduction. However, if the fixed establishment performs activities for the foreign head office or if goods or services purchased by the fixed establishment are also used by the foreign head office, the activities of the head office must also be considered. A double test applies here. Both the VAT legislation of the EU Member State of the fixed establishment and the VAT legislation of the EU Member State of the foreign head office must be considered. Only if the VAT legislation of both EU Member States entitles to deduction, the VAT can be deducted (see table below).

Deduction in case of Dutch fixed establishment that incurs expenses that also relate to activities of a foreign head office:

	VAT deductible in case supplies were subject to VAT in the EU Member State of the head office	VAT not deductible in case supplies were subject to VAT in the EU Member State of the head office
VAT deductible in case supplies are subject to VAT in the Netherlands	Deduction	No deduction
VAT not deductible in case supplies are subject to VAT in the Netherlands	No deduction	No deduction

It is not yet clear how to deal with the situation where the foreign head office is located outside the EU. Questions about this are still pending before the European Court of Justice. In our opinion, it can only be tested whether the activities in the Netherlands, where the fixed establishment is located, give rise to a right to deduction.

If costs are made for both activities for which there is a right of deduction and costs for which there is no right of deduction then the VAT is only partly deductible. We call this deductible proportion. The deductible proportion is calculated by dividing the turnover for which VAT can be deducted by the total turnover. It follows from the State Secretary's decree that in this situation all turnover generated by the foreign head office and fixed establishment must be included in the calculation of the deductible proportion. It could be deducted from the Morgan Stanley judgment that only the turnover generated for which the goods and services were used needs to be included.

Obviously, what has been discussed above also applies when a Dutch head office wishes to deduct VAT on costs that also relate to the activities of a foreign fixed establishment.

An entrepreneur who provides exempt financial services is, in principle, not entitled to deduct input VAT. This right does exist when he provides services to customers located outside the EU. If he supplies his services to a fixed establishment located outside the EU, this right to deduction also exists. For the manner in which services can be attributed to a fixed establishment of the customer, we refer to what is stated under the heading 'VAT consequences when procuring services from third parties'.

Fixed establishment and international trade in goods

In respect of international trade in goods, it is also important whether there is a fixed establishment in the Netherlands. If a foreign entrepreneur has a fixed establishment in the Netherlands, he can apply for a VAT deferment license with which he can declare the import VAT in the periodical VAT returns instead of directly when the goods enter the Netherlands. The advantage of this is that he does not have to pre-finance the import VAT. He declares it in the periodical VAT return and deducts it immediately if and insofar as he is entitled to deduct input VAT.

A foreign entrepreneur with a fixed establishment in the Netherlands can also apply for a permit for a VAT warehouse. This allows certain goods to be supplied at zero rate/exemption with a right to deduct VAT.

A fixed establishment in the Netherlands may also have consequences for the application of the simplification for call-off stock. This simplification can no longer be applied in the Netherlands if the supplier has a fixed establishment in the Netherlands. In another recently published decree, the State Secretary made it clear that a warehouse or depot is not auto-

matically a fixed establishment. What is important is whether that warehouse or depot has staff and resources that supply goods to third parties. However, other EU countries may take a different view. We refer to our perspective and update on the quick fixes.

More clarity

The Decree on fixed establishments was in dire need of an update due to case law of the European Court of Justice and a change in the rules for the place of supply. It is good that this update is now available and that entrepreneurs can find the consequences of having or not having a fixed establishment in one place. The necessary clarity has also been provided about the judgments in Skandia America Corporation and Morgan Stanley.

More information?

It is important to check whether the decree will affect your situation. Naturally, we will be happy to help you with this. Please contact one of our VAT specialists at btw@bdo.nl.

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