

Taxation of Permanent Establishments in Qatar

OECD Model Convention has laid down that profits of a business carried on by an enterprise of another State cannot be taxed in a state unless such enterprise conducts its operations in that state through a permanent establishment.

A foreign company's business profits in another State are only taxable to the extent they are attributable to such Permanent Establishment.

Various Types of Permanent Establishment:

(1) **Fixed place PE** i.e. a fixed place of business through which the company or an enterprise is wholly or partly carried on.

(2) Following are specifically included in the definition of Permanent Establishment:

- a. A place of management;
- b. A branch;
- c. An office;
- d. A factory;
- e. A workshop;
- f. A mine, an oil or gas well, a quarry or any other area to extract natural resources.

(3) Building site / Construction / Installation project if it lasts for more than a year

(4) Following activities, even if done at a fixed place of business, do not constitute a Permanent Establishment:

- a. The use of facilities solely for the storage, display or delivery of the enterprise's goods or merchandise;
- b. The maintenance of a stock of the enterprise's goods or merchandise solely for storage, display, or delivery;
- c. The maintenance of a stock of the enterprise's goods or merchandise solely for processing by another enterprise;
- d. The maintenance of a fixed place of business solely for purchasing the merchandise or goods or for collecting information for the enterprise;
- e. The maintenance of a fixed place of business solely for carrying out any other activity of the enterprise;
- f. The maintenance of a fixed place of business is solely for the combination of any of the activities above-mentioned.

However, these exceptions apply only if the overall activities are of preparatory or auxiliary in nature.

(5) Agency Permanent Establishment

A business would be considered to have a permanent place of business in another State, if a person is working on behalf of the business, under certain conditions specified. In such a case, even if the business does not have a fixed place of business in that State, it would have a PE in the form of a dependent agent of the enterprise.

A dependent agent is a person, acting in a Contracting State on behalf of a foreign enterprise and, in acting as such, routinely signs contracts or routinely plays the main role in concluding contracts that are routinely signed without any significant changes by the enterprise.

(6) Independent Agent

If an enterprise of a Contracting State carries on business dealings through an independent agent, then such an enterprise cannot be taxed in the other Contracting as it is deemed that it does not have a PE in the foreign country. This provision only applies if the agent is acting for the enterprise in the ordinary course of that business.

However, a person will not be considered as an independent agent of the enterprise if he works exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related.

(7) Subsidiary Permanent Establishment

Merely because a parent company has a subsidiary company in a foreign State, it would not imply that the subsidiary company is a permanent establishment of the parent company. A subsidiary company will be considered a separate legal entity regarding taxes. Even if the parent company manages the business or trade of the subsidiary company, that doesn't make the subsidiary company a permanent location of the parent company.

Definition of a permanent establishment as per Qatari regulations:

Taxation of permanent establishments in Qatar is governed by the Qatar Income Tax Law, particularly **Law No. 24 of 2018** on Income Tax (the "Tax Law") and its associated executive regulations.

These executive regulations define a Permanent Establishment as a Fixed place of business through which the business of a taxpayer is wholly or partly executed. This will include a branch, an office, a factory, a workshop, a mine, an oil or gas well, a quarry, a building site, an assembly project or a place of exploration and extraction or exploitation of natural resources. Permanent establishment will also include an activity carried on by the taxpayer through a person acting on behalf of the taxpayer or in his interest other than an agent of an independent status.

Corporate Income Tax on PEs

PEs are subject to corporate income tax at a standard rate of 10% on taxable income derived from activities carried out in Qatar. Taxable income includes all Qatar-source income, minus allowable deductions.

Withholding Tax

Non-resident entities without a PE are subject to withholding tax on Qatar-source income. However, for a PE, profits are directly taxed under the corporate income tax framework.

Deductions and Allowances

PEs can deduct business-related expenses incurred to generate taxable income. These may include operating costs, salaries, and depreciation of assets etc. However, certain expenses, such as payments made to head offices or affiliates in excess of a specified limit may be disallowed.

Transfer Pricing

PEs are required to maintain arm's length pricing for transactions with related entities, including their head office. Transfer pricing documentation, such as a local file, master file, or Country-by-Country Report (CbCR), may be required based on the size and nature of operations.

Subsidiary as a Permanent Establishment (PE) in Qatar

Foreign enterprises doing business with other countries may set up a subsidiary company in the source country. Now, since the subsidiary in the source country is controlled by the parent company, many may consider the subsidiary as a PE of the parent company. However, it is a settled position that the existence of a subsidiary company does not, of itself, constitute a PE of its parent company. This is clear from Article 5(7) of the OECD model convention reproduced below:

“The fact that a company which is a resident of a Contracting State controls or is controlled by a company which is a resident of the other Contracting State, or which carries on business in that other State (whether through a permanent establishment or otherwise), shall not of itself constitute either company a permanent establishment of the other.”

The commentary to OECD model convention at para 115 states that:

“It is generally accepted that the existence of a subsidiary company does not, of itself, constitute that subsidiary company a permanent establishment of its parent company. This follows from the principle that, for the purpose of taxation, such a subsidiary company constitutes an independent legal entity. Even the fact that the trade or business carried on by the subsidiary company is managed by the parent company does not constitute the subsidiary company a permanent establishment of the parent company”.

Therefore, mere factum of existence of a controlled subsidiary in another state does not automatically make itself a PE of the parent unless it satisfies other parameters for constitution of PE laid down under the article 5 of the OECD model convention.

As per the article 5 of the OECD model convention, following activities, even if done at a fixed place of business, do not constitute a Permanent Establishment:

- a) The use of facilities solely for the storage, display or delivery of the enterprise's goods or merchandise;
- b) The maintenance of a stock of the enterprise's goods or merchandise solely for storage, display, or delivery;
- c) The maintenance of a stock of the enterprise's goods or merchandise solely for processing by another enterprise;
- d) The maintenance of a fixed place of business solely for purchasing the merchandise or goods or for collecting information for the enterprise;
- e) The maintenance of a fixed place of business solely for carrying out any other activity of the enterprise;
- f) The maintenance of a fixed place of business is solely for the combination of any of the activities above-mentioned.

However, above exceptions apply only if the overall activities are of preparatory or auxiliary in nature.

Further, there may be circumstances where subsidiary could become a PE. There may be situations or transactions between the holding company & the subsidiary which could result in a PE. In this article, we have examined certain transactions namely of secondment & deputation.

Secondment & deputation arrangements

Within a multinational group, it is a common practice for employees of one company to be seconded to another affiliate company of the group and to perform business activities that clearly belong to the business of that affiliate. Seconded employees typically work under the direction, control and supervision of the affiliate during their secondment. However, many a times, seconded employees

retain their rights to participate in the overseas entities retirement and social security plans and other benefits. In such cases, administrative reasons (e.g. the need to preserve seniority or pension rights etc.) often prevent a change in the employment contract. The foreign company pays the salary of the employees seconded to the associate abroad to continue the social security contribution and for convenience purposes. The said salary is then recovered from affiliate on a cost-to-cost basis.

In general, secondment/deputation arrangements with subsidiaries could be broadly classified into two categories: (a) where the employment, direction, control of the personnel as well as risk arising out of work performed by the personnel remains with foreign parent and (b) where economic employment rests with the subsidiary. The analysis described in paragraphs 8.13 to 8.15 of the OECD Model Convention Commentary on Article 15 on Income from employment is relevant here for the purposes of distinguishing cases where business of the other company is performed from those cases where employees of a foreign enterprise perform that enterprise's own business activities. This analysis is reproduced below:

“8.13 The nature of the services rendered by the individual will be an important factor since it is logical to assume that an employee provides services which are an integral part of the business activities carried on by his employer. It will therefore be important to determine whether the services rendered by the individual constitute an integral part of the business of the enterprise to which these services are provided. For that purpose, a key consideration will be which enterprise bears the responsibility or risk for the results produced by the individual's work. Clearly, however, this analysis will only be relevant if the services of an individual are rendered directly to an enterprise. Where, for example, an individual provides services to a contract manufacturer or to an enterprise to which business is outsourced, the services of that individual are not rendered to enterprises that will obtain the products or services in question.

8.14 Where a comparison of the nature of the services rendered by the individual with the business activities carried on by his formal employer and by the enterprise to which the services are provided points to an employment relationship that is different from the formal contractual relationship, the following additional factors may be relevant to determine whether this is really the case:

- *who has the authority to instruct the individual regarding the manner in which the work has to be performed;*
- *who controls and has responsibility for the place at which the work is performed;*
- *the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided (see paragraph 8.15 below);*
- *who puts the tools and materials necessary for the work at the individual's disposal;*
- *who determines the number and qualifications of the individuals performing the work;*
- *who has the right to select the individual who will perform the work and to terminate the contractual arrangements entered into with that individual for that purpose;*
- *who has the right to impose disciplinary sanctions related to the work of that individual;*
- *who determines the holidays and work schedule of that individual.*

8.15 Where an individual who is formally an employee of one enterprise, provides services to another enterprise, the financial arrangements made between the two enterprises will clearly be relevant, although not necessarily conclusive, for the purposes of determining whether the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided. For instance, if the fees charged by the enterprise that formally employs the individual represent the remuneration, employment benefits and other employment costs of that individual for the services that he provided to the other enterprise, with no profit element or with a profit element that is computed as a percentage of that remuneration, benefits and other employment costs, this

would be indicative that the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided. That should not be considered to be the case, however, if the fee charged for the services bears no relationship to the remuneration of the individual or if that remuneration is only one of many factors taken into account in the fee charged for what is really a contract for services (e.g. where a consulting firm charges a client on the basis of an hourly fee for the time spent by one of its employees to perform a particular contract and that fee takes account of the various costs of the enterprise), provided that this is in conformity with the arm's length principle if the two enterprises are associated. It is important to note, however, that the question of whether the remuneration of the individual is directly charged by the formal employer to the enterprise to which the services are provided is only one of the subsidiary factors that are relevant in determining whether services rendered by that individual may properly be regarded by a State as rendered in an employment relationship rather than as under a contract for services concluded between two enterprises."

Secondment/deputation arrangements could give rise to fixed place PE exposure as well as service PE exposure (in cases where foreign parent is located in a country with which a tax treaty containing service PE provision has been signed). **In such a case, it is not the legally incorporated subsidiary but the physical space at its premises, which is available at the disposal of the foreign enterprise, that can create a fixed place of business PE of the foreign enterprise, if the necessary tests of permanency are satisfied, namely if the expatriates of the foreign enterprise occupy such space for such duration, as satisfying the generally accepted threshold of permanency.**

It is through the presence of such expatriates that the foreign enterprise may be said to carry on business at such fixed place available at its disposal.

Fixed Place Permanent Establishment (PE) in Qatar:

Does secondment of employees to wholly owned subsidiary constitute a Fixed Place PE?

In today's globalized economy, businesses frequently expand beyond their home countries, establishing offices, factories and warehouses worldwide. But when does a foreign company's presence in another country create a taxable obligation? The answer lies in the concept of Permanent Establishment (PE) - a crucial principle in international tax law.

A Fixed Place Permanent Establishment (PE) arises when a business maintains a physical location in a foreign country where it conducts core operations. This status can have significant tax implications, as it subjects the company to local corporate income tax on profits generated in that country. For multinational companies, understanding what constitutes a Fixed Place PE is essential to ensure compliance with tax regulations and avoid unexpected liabilities.

The basic requirement of the fixed place is that the business of an enterprise is wholly or partly *carried on* through the fixed place of the business in the other contracting State. Therefore, in cases where the economic employment of the personnel seconded/deputed lies with the subsidiary and the role of foreign parent is limited to provision of employees to the subsidiary, then the possibility of constitution of a Fixed Place PE in such type of situations is very remote.

If the parent company makes personnel available to the subsidiary for remuneration, then the activity of this 'hired labour' is to be attributed to the subsidiary and does not constitute a PE of the parent doing the hiring-out.

Whereas, in cases where economic employment remains with the foreign parent and the employees perform business of the parent as well from the premise of the subsidiary, it becomes imperative to

examine whether the premise of the subsidiary, is at the disposal of the foreign parent. This 'right to use' test has been further elaborated under Para 12 and by way of an illustration in Para 15 of the OECD Model Convention Commentary on Article 5 wherein the premises of subsidiary constitute a fixed place PE for the parent when employees of parent who, for a long period of time, are allowed to use an office in the headquarters of its subsidiary in order to ensure that subsidiary complies with its obligations under the contracts concluded with the parent.

In such cases, there is a possibility of attribution of profits to the subsidiary which should be worked out on ALP basis.

Therefore, care needs to be taken when a subsidiary provides office space to seconded/deputed employees of the parent carrying on business of the parent company as well from such premises such that particular office space is not reserved for such employees and also to limit the amount of time spent by employees of the parent at the premises of the subsidiary, not only on an individual trip basis or on a continuous basis if the trips are recurrent.

Service PE:

Service PE could arise in cases where legal/economic employment remains with the parent and the parent renders services, through its employees to its AEs, provided the services are rendered for specified time duration as stipulated under respective treaties.

Contract manufacturing:

In many industries, rather than outsourcing parts of its business, a company could outsource its entire business process (e.g. production/manufacturing/processing) to another company due to advantage of cost savings amongst others. In contract manufacturing, the manufacturing process is the proprietary property of the entity hiring the contract manufacturer and the contract manufacturer has to undertake the process as per the specifications and raw materials provided by such entity. In the case of parent appointing its subsidiary as a contract manufacturer, can the premises (e.g.: factory) of the subsidiary constitute a fixed place PE of the parent?

The pre-requisites of Article 5(1) of the OECD Model Convention would have to be examined in this case too. Under these arrangements, factory owned and used exclusively by an independent subsidiary cannot be said to be at the disposal of the parent that will receive manufactured goods merely because these goods will be used in the business of the parent. An independent subsidiary carries on its own business of manufacturing products for the parent as it would have done under similar market conditions for any other company that did not form part of the same business group. Therefore, under such circumstances, the factory of the contract manufacturer (i.e. subsidiary) should not become a Fixed Place PE for the parent.

Sub-contracting arrangements

Often the parent company bids for the contract as a whole and then sub-contracts a part of the contract to its subsidiary (incidentally incorporated for performance of part of the contract). An important question which arises in such situations is whether the subsidiary becomes a dependent agent PE of the parent?

Para 105 of the OECD Model Convention Commentary on Article 5 states that in relation to the test of legal dependence, it should be noted that the control which a parent company exercises over its subsidiary in its capacity as shareholder is not relevant in a consideration of the dependence or otherwise of the subsidiary in its capacity as an agent for the parent. The independence of the subsidiary under company law also remains authoritative for tax purposes if it sub-contracts entirely

or partially to associated enterprises or it acquires the means required for the contract's execution from associated enterprises.

Further, an agent is to be distinguished on the one hand from a servant and on the other from an independent contractor. A servant acts under direct control and supervision of his master and is bound to conform to all reasonable orders given to him in the course of his work; an independent contractor, on the other hand, is entirely independent of any control or interference and merely undertakes to produce a specified result, employing his own means to produce that result. An agent, though bound to exercise his authority in accordance with all lawful instructions which may be given to him from time to time by his principal, is not subject in its exercise to the direct control or supervision of the principal.

The relationship between a contractor and his sub-contractor is similar to that between one principal and another. Irrespective of whether the subsidiary is considered to act as an independent contractor or as an agent, for it to become an Agency PE of its parent under Article 5(5) of the OECD Model convention, it needs to have an authority to conclude contract in the name of its parent and habitually exercise it too. Negotiation of contracts by a subsidiary is a relevant though not a conclusive factor in determining whether the subsidiary has an authority to conclude contracts in the name of the parent. The mere fact that a person has attended or participated in negotiations in a State between an enterprise and a client, can in certain circumstances, be sufficient, by itself, to conclude that the person has exercised in that State an authority to conclude contracts in the name of the enterprise. Further, a person who is authorised to negotiate the essential elements of the contract, and not necessarily all the elements and details of the contract, on behalf of a foreign resident, can be said to exercise the authority to conclude contracts.