Changes in Spanish interpretation of the VAT permanent establishment

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The Spanish VAT authorities have recently published some public rulings concerning different questions related to the interpretation of the criteria for creating a permanent establishment for VAT purposes (hereinafter: "p/e") in Spain. The new interpretation seems to be a complete change from the previous Spanish legal position.

I. Interpretation until the end of 2009

Until the end of 2009, it was - according to the Spanish VAT law - possible to have a "VAT only p/e" in Spain. To create such a p/e for VAT purposes, it was for example sufficient for a business to rent warehouse space in Spain. Neither an intervention in the operations nor human resources were required for being an "established" operator.

Furthermore, the Spanish VAT law incorporated at that time a so-called "force of attraction" rule. This rule stated that all supplies of goods made by the company having such a warehouse were automatically attributed to the p/e for VAT purposes, even if the p/e was not actually involved in these supplies, e.g. because the business had no employees in Spain. Therefore, it was quite simple avoiding the "reverse charge" scheme generally applied to non-established entities in Spain.

A non-resident business renting a warehouse in Spain was thus treated as established in Spain for VAT purposes and consequently the business was obliged to charge VAT on domestic supplies of goods in Spain instead of issuing invoices under the reverse-charge mechanism. With this set-up, it was possible to avoid VAT cash-flow issues in Spain, because Spanish input VAT incurred could be offset against the Spanish VAT liability.

II. Interpretation from 2010 onwards

A. Changes in the VAT law

In 2010, several changes to the Spanish VAT law entered into force due to the introduction of the "EU VAT package" implementation as well as relevant case law from the European Court of Justice (ECJ). We may remember that the new EU rules were based on two principles: the so called reinforced p/e and the need of a relevant intervention of the p/e in the operations, but the concept of a p/e itself was not introduced as it was previously developed by the ECJ.

The implementation of such new rules by Spanish internal law may be considered not complete: the wording of the VAT p/e was not changed in the VAT law, but the "force of attraction" principle was removed from the Spanish VAT rules. Thus, in case a p/e is not involved in the supply of goods by using own human or technical resources, the p/e does not carry out the supply.

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For example: If a foreign company with a rented warehouse supplied goods in Spain, it was still considered to be established for VAT purposes, but the supply was not automatically attributed to the Spanish p/e. Hence this supply considered to be made by the foreign head office and was therefore subject to the reverse charge mechanism. Please note that for warehouses owned by a foreign taxable person and staffed with its own personnel the situation might have been treated differently.

B. Clarification through public consultation

At the beginning of 2010, the VAT implications of the new rule in practice were still somewhat unclear. During the year 2010, the Spanish VAT authorities published the result of two public consultations confirming that rented warehouses could be seen as a VAT p/e under Spanish VAT law if certain requirements were met. The first publication highlighted that the current ECJ case law also needed to be considered for the interpretation of the p/e. Therefore, according to this first published public consultation, the following four criteria needed to be fulfilled to create a p/e in Spain:

1. Minimum degree of stability.
2. Sufficient structure to supply the services on an independent basis.
3. Permanent presence of both human and technical resources necessary for the provision of those services.
4. Sufficient degree of permanence in time.

The second publication of 2010 stated that even if a rented warehouse is a VAT p/e this is not sufficient to create a VAT liability for the foreign company, i.e. the reverse charge mechanism applies to the supplies of goods made in Spain. This legal opinion was confirmed by the EU VAT Implementing Regulation becoming effective on 1 July 2011.

Taking these arguments into account, from the Spanish VAT perspective a supply of goods made by a foreign entity should come under the reverse charge mechanism even if the foreign business had rented warehouse space in Spain.

C. New position in 2011

The EU Regulation 282/2011 was approved and defines quite precisely the concept of intervention of a p/e with the aim of clarifying the determination of the relevant tax payer in any operation, but the Spanish law did not introduce any changes in its former wording. One could consider that it was because the "direct effect" of such Regulation but instead, unexpectedly, what followed was a change in the interpretation of the law.

Between July and November 2011, the Spanish VAT authorities dealt with four new public consultations concerning several questions with regard to the p/e from a VAT point of view. These consultations were published in late 2011 and at the beginning of 2012 and seem to include another complete change of position. All documents argue – in line with the situation before 2010 – that it is sufficient to rent a warehouse in Spain in order to create a p/e for VAT purposes and even if the intervention was minimal (logistics, packaging, subcontracted works, etc.) said p/e may be considered to be automatically involved in the supplies of goods in Spain. As a result, the supplier needs to be VAT registered and to charge Spanish VAT on domestic supplies of goods in Spain in any case as he will be treated as established in Spain and therefore the reverse charge mechanism cannot be applied.

III. Conclusion

In cases where that a business rents a warehouse from a third party warehouse provider and has no other presence in Spain, but does distribute its own goods from such warehouse, then it does not meet the criteria of a VAT p/e under the EU VAT Directive / ECJ case law, not having neither local intervention nor human resources. A foreign business might therefore consider continuing to make its supplies under the reverse-charge mechanism. Should the Spanish tax authority – based on the 2011 public consultations – argue that the foreign business is established and therefore should charge VAT there should be sufficient legal ground to expect that such a case should most likely be defendable successfully in court. However, this can be a drawn out process and hence a business taking this position should evaluate its situation carefully.

In contrast, if a business can benefit from being able to charge VAT on its supplies of goods in Spain, the four public consultations provide an argumentation base which allows the business to do so. Nevertheless, the risk that the situation might change again in the future cannot be ruled out entirely.

Where a company owns a warehouse (instead of renting it) the situation should in theory be the same. In practice, though, this might give the Spanish tax authorities even stronger grounds to claim that the warehouse creates a p/e. In this set-up it will be much harder to defend a company not charging VAT on its supplies of goods in Spain.

Furthermore, in cases where a company is treated as being established from a VAT point of view, the tax authorities might use this to argue that the company is also established for direct tax purposes, as the operator is recognising that he has at least certain resources that intervene in the operations. Even if on basis of the OECD model treaty and to a somewhat more limited extend the Swiss-Spanish double tax treaty, there should not be a p/e for direct tax purposes, in case the warehouse is only used for storage or for some limited ancillary purposes for the business, the tax authorities are quite aggressive with the approach to try to establish a p/e in Spain, in order to be able to tax the allocated profit with 30% corporate income tax.

A. Recommendation

We would highly recommend that companies with (rented or owned) warehouses in Spain review their current situation in Spain very carefully in order to eliminate a potential risk, both from a VAT and direct tax point of view.

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