



## ECJ: EU subsidiary as fixed establishment of its foreign parent company

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### 1 Facts

The Polish company Dong Yang Electronics sp. z o. o. ("Dong Yang") entered into an agreement with LG Display Co. ("LG Korea") seated in Korea for the assembly of printed circuit boards. LG Korea provided Dong Yang with the materials necessary for the assembly. The materials were provided to Dong Yang by the Polish subsidiary of LG Korea ("LG Poland"). After assembly by Dong Yang, LG Poland processed the finished printed circuit boards on behalf of LG Korea. LG Korea then sold the finished products to another subsidiary based in Germany. Dong Yang was not aware of the service relationship between LG Korea and its Polish subsidiary. LG Korea assured Dong Yang that it did not have a fixed establishment in Poland. As a result, Dong Yang issued invoices to LG Korea for the supply of assembly services without showing VAT. The Polish tax authorities, however, found that the supply of services were subject to Polish VAT because LG Poland was a fixed establishment of LG Korea. As a result, the supplies of services were not rendered at the seat of LG Korea in Korea, but rather at the place of its fixed establishment in Poland.

Dong Yang filed an appeal against the tax assessment. The Polish court asked the ECJ whether it could be inferred that a third country parent company had a fixed establishment in an EU member State, from the mere fact that the parent company had a subsidiary in the EU Member State. In addition, the Polish court wanted to know whether a third party is obliged to examine the contractual relations between the parent company and the subsidiary in order to determine whether the subsidiary is a fixed establishment of the parent company.



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## 2 Grounds

In its judgment of 7 May 2020 (C-547/18 - Dong Yang), the ECJ answered the two questions referred by the Polish court in the negative. The ECJ found that the mere holding of a subsidiary on the territory of an EU Member State would not necessarily indicate the existence of a fixed establishment of a parent company established on the territory of a third country. Although the ECJ is of the opinion that it is, in principle, possible for a subsidiary to constitute the fixed establishment of its parent company. However, this depends to a large extent on the material requirements of Art. 11 of the Council Implementing Regulation (EU) (personnel and technical equipment), which must be examined on the basis of the actual circumstances. The ECJ thus confirmed its previous case law (ECJ, judgment of 20 February 1997 - Case C-260/95, DFDS). The ECJ justified its decision by taking into account the economic and commercial reality. In this regard, the ECJ first states that the place of supply of services to a taxable person is primarily determined by the place where the recipient of the supply has established his business (Art. 44, first sentence of the VAT Directive). An exception to this rule only exists if the service is supplied to a fixed establishment of the taxable person (Art. 44 sentence 2 of the VAT Directive). In this case, the supply of service is deemed to be rendered at the place of the fixed establishment. The fixed establishment primarily serves the proper functioning of the VAT law, provided that the link to the place of establishment does not lead to a fiscally reasonable solution. In addition, the ECJ clarifies that the subsidiary's legal form is irrelevant as regards the classification as a fixed establishment. In this respect, the ECJ refers to the Free Trade Agreement concluded between the EU and the Republic of Korea. This agreement allows Korean investors to carry out economic activities in Poland only by way of certain company forms. However, this restriction has no effect on the interpretation of the concept of a fixed establishment.

Furthermore, the ECJ ruled that it was not for the third party, e.g. a contractual partner, to examine the contractual and factual relationships between the parent company and the subsidiary. A third party was not obliged to determine whether the subsidiary constitutes a fixed establishment of the parent company. According to the ECJ, such an obligation cannot be derived from Art. 22 of the Council Implementing Regulation (EU). Finally, no obligations should be imposed on the supplier that would have to be carried out by the tax authorities.

## 3 Opinion

With its most recent decision, the ECJ confirms its previous case law. An independent subsidiary can, in principle, be a fixed establishment of its parent company. Already in 1997, the ECJ held that a wholly owned subsidiary may constitute a fixed establishment if it merely acts as an auxiliary organ of the parent company on the basis of contractual agreements (ECJ, judgment of 20 February 1997 - Case C-260/95, DFDS). In its decision, the ECJ contradicted the opinion of the Advocate General. She argued that the subsidiary of a foreign company could not, in principle, be its fixed establishment. In its judgment, the ECJ left the most important question open: When is an independent subsidiary the fixed establishment of its parent company? And what are the VAT consequences for a parent company and its subsidiary if the subsidiary is also the parent company's fixed establishment? In particular for subsidiaries, the decision creates considerable legal uncertainty with regard to the invoicing of supplies of services to parent companies. If a subsidiary is not a fixed establishment of the parent company, supplies rendered by the subsidiary to its parent company are, in principle, taxable at the place where the parent company is established. If the subsidiary is also a fixed establishment of the parent company, it is left open to question whether the subsidiary must invoice with or without showing VAT.