

2009 IFA CONGRESS

Canadian Branch Report: Subject 1 – Is there a Permanent Establishment?

Summary and Conclusions

The concept of PE is used in Canadian tax treaties and for domestic income and value-added tax (GST) purposes, to allocate income among the provinces and to establish residence for GST purposes. The concept of PE as a "fixed place of business" and the "agency establishment" concept are contained in the domestic provisions.

For both treaty and domestic purposes, Canadian courts and tax authorities use the OECD Model and Commentary. Consequently, Canadian jurisprudence and administrative policy are closely aligned with the OECD Commentary. The Technical Explanations ("TE") of the Canada-United States Tax Treaty and Protocols thereto are also a source of guidance.

Canadian authorities have not generally analyzed whether a "place of business" exists apart from the elements of fixity and permanence associated with the PE concept. The existence of a specific physical location or "habitation" is necessary rather than only a network of agents or other similar sales organization. Thus, a ship or other vehicle cannot, under the general definition, be a PE because it is not a "place".

In determining whether a particular place of business is that of a taxpayer, recourse will be had to:

- (a) identification of the premises (for example, signage) with the business of the enterprise,
- (b) payment of expenses of the premises by the enterprise,
- (c) whether contracts were concluded there, and
- (d) keeping goods for sale or delivery on the premises,

as well as the degree of control exercised over the premises (or an agent if the premises are those of an agent). Where an enterprise carries on more than one business, the place must be identified with the particular business. The business of renting real estate will constitute the real estate a place of business.

Canadian tax authorities have taken the position that premises leased by an enterprise for use by employees of an unrelated service provider to service Canadian customers (but not conclude contracts) would be a place of business of the enterprise.

"Place of business" implies a degree of fixity which, as noted, would not be possessed by a ship. The use by a sports team of locker room facilities at the stadiums of other teams does not have sufficient fixity or permanence to constitute a PE.

The use by an enterprise of a fixed place for short periods of time will generally not have the degree of permanence to constitute a PE (use of a booth at a fixed location for three weeks in each year over a 15-year period has been found to constitute a PE).

For a place of business to be a PE, the enterprise must have the right to use it for carrying on the business, not merely, for example, of providing services to a particular customer or client – both physical control and exclusive or unlimited access and right of use are required.

Use of a client's premises is unlikely to constitute a PE.

There are no judicial or administrative statements on other aspects of carrying on business "through" a place of business.

There are no judicial or administrative statements on the listed examples in paragraph 2 of Article 5.

An installation project is distinct from, and need not be related to, a construction site or project. Installation of machinery or equipment will be an installation project which will commence with the first activity in Canada and continue until all aspects of the project, including start-up, testing and staff training, have been completed. This will also be the case where contractors carry out all or part of the project. Installation of machinery is distinct from its fabrication where the contract encompasses both.

The combination of two or more enumerated activities will not by itself constitute a PE.

A dependent agent's authority to conclude contracts in Canada must extend to contracts relating to operations constituting the business of the enterprise rather than the agent's business.

To be an agent of independent status, the agent must be independent both legally and economically. Legal independence is evidenced by intention of the agents, lack of control or ownership by the enterprise of their business, absence of reimbursement for cost of assets and responsibility of agents for their own employees. Economic independence is evidenced by compensation based on commission with no minimum or maximum levels, freedom to solicit business from others, absence of a requirement to act exclusively for the enterprise and economic risk borne by the agents. Exclusive dealing with, or the supply of product by, the enterprise is not determinative.

A Canadian subsidiary habitually exercising authority to conclude contracts in the name of its parent may constitute a PE depending on the terms of the agency agreement and the operations of the subsidiary.

The concept of fixed base is similar to that of PE. The TE to the Fifth Protocol suggests that both geographical and commercial coherence will be required to deem projects to be the same or connected.

There are no judicial or administrative statements on the rules relating to insurance activities in the UN Model.

The mere use of leased railway rolling stock will not constitute a PE of the lessor.

Machinery or equipment need not be owned by the enterprise for it to be a PE. Whether it is substantial will be determined by its size, value and its contribution to gross income.