Federal Ministry of Finance Issues Guidance on Austrian Permanent Establishments

On 5 August 2013, the Federal Ministry of Finance issued unexpected guidance on permanent establishments under the German/Austrian Double Taxation Treaty.

The double taxation treaty between Germany and Austria defines a permanent establishment as "a fixed place of business through which the business of an enterprise is wholly or partly carried on". The term "permanent establishment" shall, inter alia, not include the maintenance of a fixed place of business "solely for the purpose of carrying on, for the enterprise, any other activity of a preparatory or auxiliary character". This is generally in line with the OECD Model Convention.

In the case assessed by the Austrian Federal Ministry of Finance a German cleaning company worked on the premises of an Austrian customer on six days per week for two to three hours per day. The cleaning company used a small room in the customer's building for storing its cleaning equipment.

Despite the auxiliary character exception to the definition of a permanent establishment under the double taxation treaty between Germany and Austria, the Austrian Federal Ministry of Finance ruled (BMF 5.8.2013, EAS 3333) that this small room ("broom closet") constituted a permanent establishment for the German cleaning company in Austria because it was essential for the cleaning contract to be economically reasonable. Consequently the German cleaning company has to pay taxes in Austria on a part of its profit.

Alternative Investment Funds Manager Act

On 21 July 2013 the Alternative Investment Funds Manager Act entered into force in Austria and will have major tax implications for investors.

Under Austrian tax law, investors are not only taxed on actual distributions by investment funds but also on deemed distributions ("ausschüttungsgleiche Erträge"). This - roughly speaking - means that an investment fund is treated as a tax transparent entity for Austrian tax purposes.

The recently enacted the Alternative Investment Funds Manager Act ("AIFMG") broadened the definitions of domestic and foreign investment funds: Foreign entities, which are in their country of residence either treated as tax transparent or lowly taxed now also may qualify as foreign investment funds. Also alternative investment funds pursuant to the AIFMG are generally covered. However, even though the AIFMG
provides a definition for the term “alternative investment fund”, many details in this respect remain unclear and often render the applicability of the new provisions uncertain.

Investors should therefore be aware that more investment structures than before will be considered to be tax-transparent in Austria with the crucial implication of deemed distributions by such structures also being subject to income tax.

Capital Duty on Grandparent Contributions

In several decisions the Independent Tax Senate recently ruled on Capital Duty on Grandparent Contributions in connection with reorganizations.

Austria levies a capital duty of 1% on contributions to Austrian corporations by their direct shareholders. Generally, this duty may be avoided by using a “grandparent contribution” where an indirect shareholder, such as the grandparent company, effects the contribution to the Austrian corporation rather than the direct shareholder.

Since the Austrian tax authorities apply a substance over form approach they, however, base their assessment on an economic point of view as to which company is contributing the capital and which company is the recipient thereof. They argue that if a grandparent contribution was effected right before a reorganization during which the entities involved then change their respective shareholder-level, the contribution is to be assessed based on the corporate structure after the reorganization because it correlates closer to the true economic circumstances.

More specifically, the Independent Tax Senate for example ruled that a grandparent contribution may be subject to capital duty if it is granted by the grandparent to the indirect subsidiary only to facilitate a merger between the indirect subsidiary and its parent company.

Austria/Liechtenstein Treaty Ratified by Liechtenstein Parliament

On 6 September 2013 the Liechtenstein Parliament voted in favor of the tax agreement on the regularization of undeclared assets between Liechtenstein and Austria.

As reported in our Newsletters No. 2/2013 and 3/2013, Liechtenstein and Austria have signed a tax agreement on the regularization of undeclared assets, effective 1 January
2014 ("Tax Agreement"). Despite substantial concerns by trustees in Liechtenstein, it was now ratified by the Liechtenstein parliament. The Austrian parliament had already approved the Tax Agreement in March 2013.

Together with the Tax Agreement also the double taxation treaty between Liechtenstein and Austria was amended (effective 1 January 2014, please see our Newsletter No. 3/2013). These changes will extend treaty benefits to certain Liechtenstein resident entities, which did not fall under the scope of the double taxation treaty before. It is worth noting that according to the Federal Ministry of Finance (BMF 19.2.2013, EAS 3315) entering into the benefits of the Liechtenstein/Austria double taxation treaty might trigger exit taxation in Austria, particularly if such Liechtenstein entity held participations in Austrian corporations.

Supreme Administrative Court on Cross-Border Personnel Leasing

On 15 August 2013 the Austrian Supreme Administrative Court rendered a surprising decision on cross-border personnel leasing expressing an opinion deviating from the tax administration’s position.

The residence state of an employee is generally entitled to tax any employment remuneration unless the employment is exercised in the other state. If the employment is exercised in the other state, such remuneration may be taxed in that other state.

However, under most double taxation treaties, the remuneration shall remain taxable in the residence state if a) the recipient is present in the other state for a period or periods not exceeding in the aggregate 183 days in any twelve month period commencing or ending in the fiscal year concerned, and b) the remuneration is paid by, or on behalf of, an employer who is not a resident of the other state, and c) the remuneration is not borne by a permanent establishment which the employer has in the other state.

In a cross-border personnel leasing situation it is crucial to assess who is the employer for purposes of criterion b). If the personnel leasing company is the employer, the residence state would have the taxation right on the employment income. If the customer (the lessee) is the employer, the source state would be entitled to tax the income as long as the employment was exercised there. This question is answered based on an economic approach rather than from a formal perspective.

Contrary to the view expressed by the Austrian Federal Ministry of Finance (BMF 24.1.2011, EAS 3201; 9.3.2012, EAS 3271), the Austrian Supreme Administrative Court now ruled that the customer (lessee) shall be regarded as the employer if he economically bears the employment costs and deducts such costs for tax purposes in the source state. This opinion matches the interpretation by many other OECD countries.
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About WOLF THEISS Tax Practice

WOLF THEISS was one of the first Austrian law firms to advise on tax law and we like to think we’ve been setting the standards ever since. Our experience covers a wide range of disciplines, from corporate tax advice for reorganizations and M&A to tax disputes and litigation, financial products, holding companies, fiscal criminal law and private clients. For many years now we have successfully expanded the tax practice also to our other offices. We are known for offering clear solutions for challenging cases in a very efficient manner, which has been recognized by the international legal community many times.

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If you would like to know more about the topics covered in this memorandum or our services in general, please get in touch with the contacts listed above.

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