

Rödl & Partner

# Permanent establishments



## International taxation

The international taxation practice group of Rödl & Partner Czech Republic advises our clients in all matters associated with the taxation of cross-border transactions, focusing mostly on:

- review of tax consequences of international transactions;
- taxation of permanent establishments;
- corporate transformations, including cross-border transactions;
- cooperation of Rödl & Partner's tax experts across more than fifty countries.

## Taxation of dependent agent permanent establishments

Many foreign companies maintain their presence on the Czech market through sales representatives (whether own employees or independent contractors) who are tasked with finding and recruiting new customers or negotiating contracts on the local market. A sales representative used by a company to serve a foreign market is called a dependent agent.

Recently, the definition of the so-called dependent agent permanent establishment and its interpretation in the context of international taxation, as used in double taxation avoidance agreements, has been broadened by the OECD in its commentaries on the model DTA agreement to include a situation in which the dependent agent habitually plays the principal role leading to the conclusions of contracts that are then routinely entered into by the company without material modification. This shift in the definition of permanent establishments has made it more important than ever to approach the topic of permanent establishment formation with caution and after a comprehensive review of the tasks and the activities performed by the agent in the Czech Republic, focusing on the economic reality instead of the formal approach on who signed the contract and where.

The economic reality should also be prioritized with regard to the recent developments in the employment relations, particularly with a view to the increasingly popular practice of foreign companies to allow their employees perform their tasks from a home office.

## Calculating Permanent Establishment's Tax Base

According to the OECD methodology, in calculating the tax base, the permanent establishment should be treated as an independent entity, i.e. in accordance with standard transfer pricing rules. Regrettably, the correct calculation of tax base of permanent establishment tends to be more complicated than for regular business corporations, largely due to difficulties inherent in the proper identification of the transactions that generate taxable income. The correct calculation of the taxable income on the part of permanent establishments is therefore predicated on the completion of proper functional and risk analysis for transfer pricing purposes, and on the analysis of assets and human resources in particular, which constitutes an additional complication of the whole process.

## Comprehensive Solution for the Review and Taxation of Permanent Establishments

To outline the process involved in the taxation of permanent establishments in the Czech Republic, we briefly sum up the basic steps required:

- Review of the facts and circumstances leading up to the formation of permanent establishment in the Czech Republic;
- Registration of the permanent establishment to the corporate income tax;
- Allocation of revenues and costs in compliance with internationally recognized transfer pricing rules;
- Calculation of the taxable income and the tax liability;
- Completion and filing of the corporate income tax return form.

## Methodological Inquiries and Advanced Pricing Agreements

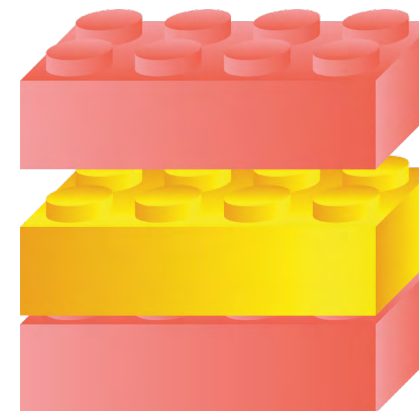
Since 2018, tax authorities may be asked to review the facts and the law for a specific set of circumstances, and to present their official opinion in an Advanced Pricing Agreement covering the permanent establishment's tax base calculation in the Czech Republic.

The Advanced Pricing Agreement, if properly exercised, gives taxpayers an assurance that the tax authorities will not challenge the method used to assess their tax.

Alternatively, a more general methodological inquiry may be raised with the General Financial Directorate. This type of inquiry gives a lower degree of assurance, but represents a less administratively demanding process for the resolution of certain methodological uncertainties.

## and that's not all ...

The statutory regulation of permanent establishments is not limited to the matter of their taxation. The regulatory framework also covers a broad range of employment law, corporate law or accounting matters. Since permanent establishments are by their nature closely integrated with their foreign owners, we cooperate with our colleagues from other Rödl & Partner branches that span all over more than fifty countries. This allows us, for example, to draw comparisons between the tax burden of foreign companies operating in the Czech Republic via permanent establishments and subsidiaries, and prepare case reports that analyze the tax burden in the event of permanent establishment formation in the Czech Republic compared to the taxation of revenue in the tax residence of their foreign owner.



## Our team

- our experts on taxation of permanent establishments of foreign entities

## Your contact persons



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As attorneys, tax advisers, auditors, accountants and management and IT consultants, we are present with 106 own offices in 48 countries. Worldwide, our clients trust our 5,130 colleagues.

In the Czech Republic, we have been offering our services since 1991. Today, we provide our legal, tax, audit, business process outsourcing and management & business consulting services through more than 320 professionals operating in our offices in Prague and Brno.

Rödl & Partner holds the prestigious title of the Czech Law Firm of the Year in the field of tax law in years 2012 to 2020.

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