



## PERMANENT ESTABLISHMENT IN AUSTRALIA: BRANCH OR SUBSIDIARY?

### DEFINITION OF A PERMANENT ESTABLISHMENT

Broadly, a **Permanent Establishment (PE)** exists where: Business operations are carried on by a foreign resident entity at or through a fixed place of business in Australia.

Australia's more recent double tax agreements (DTAs), including the French treaty, provides greater clarity in respect of various treaty articles, including the definition of what constitutes a 'permanent establishment' (PE).

The business must have a clear operating base which is a physical address. Location can be a rented business premises, warehouse or even a residence used by the managing director. This highlights that consideration of the PE issue needs specific attention to each situation.

One of the more traditional tests in determining if a PE is in existence is the ability for an entity to sign and finalise contracts in Australia.

The mere presence of employees on the ground doesn't necessarily create a PE. For example, researching the local market or providing sales leads to the head office doesn't necessarily imply a PE exists. Once there are a significant number of employees or where continuous sales commissions are paid, it becomes somewhat a difficult to argue that there is no PE.

Broadly speaking, Australia has traditionally based its definition on the OECD model with some minor changes depending on the specific treaty. In recent times the OECD has issued a draft paper which includes an expansion of the PE concept. Australian Integrity measures which are to commence in January 2016 have some differences to the OECD proposals and as such, businesses with cross border activity should consider the impact of the measures.

### DEFINITION AND MAIN DIFFERENCES BETWEEN A BRANCH AND A SUBSIDIARY

#### Subsidiary

An Australian subsidiary company is a separate legal entity with limited liability and has its own identity for tax and legal purposes. The Australian subsidiary must have at least one resident director in Australia but the company can be wholly owned by a foreign shareholder.

- Registration: A (private) company can usually occur on a same day basis (business ready) and post incorporation documents within a few working days.
- Reporting: A branch is required to lodge either parent company accounts or the local branch accounts with ASIC as a matter of public record.

#### Branch

A foreign company branch carrying on business in Australia is subject to Australian legislation. A branch office does not have limited liability and is not recognised as having a separate legal identity in the country. Registration for a branch office is more complex and time consuming than for a subsidiary company with the company required to disclose both corporate information and supporting documentation to ASIC. The registration of a branch office can take up to 28 days. Using an experienced provider can generally expedite the process.



## DOING BUSINESS IN AUSTRALIA

- Tax: The entities of corporations are taxed at standard company tax rates currently being 30% regardless of whether it is a branch or subsidiary.
- Liability: A company, as either a Pty. Ltd. or Ltd. is limited to the value of the company's assets unless of course the directors trade when they know, or should have known the company is no longer able to meet its debts when they fall due. This could leave the directors personally liable under certain circumstances. As a branch is not a separate legal entity, the whole assets of a parent are exposed. The local agent may also be personally liable for the company's ASIC and ATO liabilities.
- Thin Capitalisation: Rules govern the amount of tax deductible debt used to finance an entity's Australian operations. These rules limit interest claimed as a tax deduction. Broadly speaking, a company should be able to fund approximately 75% of its investment in an Australian project by way of debt.

The rules which also apply to a branch operation or a subsidiary are quite detailed and care needs to be taken if the safe harbour rules do not apply.

Safe Harbour (De Minimis Rule) allows entities with 'debt deductions' being interest and other debt costs of less than \$250,000 per annum to claim a tax deduction without applying the Thin Cap rules.

### TAX AND ACCOUNTING OBLIGATIONS

Company tax is calculated by the taxpayer under self-assessment and paid on lodgement. In addition, the entity must account for Goods and Services Tax (GST) on a monthly and/or quarterly basis and Pay As You Go (PAYG) tax deducted from employee earnings. The GST and PAYG payments are made on a monthly basis or quarterly Business Activity Statements (BAS) which may also include quarterly pre-payments of income tax and Fringe Benefits Tax (FBT).

Entities will be liable to pay FBT. The year-end reporting date for FBT is 31 March. The benefits subject to FBT may include:

- Motor vehicle
- Entertainment
- Rent and housing payments
- Health Insurance
- And any other benefits paid in lieu of salary payment

### REGISTRATION FORMALITIES

- Consider 'Know Your Client' rules as Proof of Identity documentation rules are strict. Incorrect documentation will result in delays.
- Federal Income Tax & Australian Business Number (ABN) registration must be made.
- Australia does not have state based income tax but other levies such as payroll taxes, insurances, stamp duty and various others may apply, requiring registration

### STANDARD LEGAL OBLIGATIONS AND FORMALITIES FOR A BRANCH

- Reports of the foreign company's annual accounts must be filed.