Applying tax conventions to employees not resident in the Netherlands who carry out temporary work in the Netherlands via a foreign employment agency

Directorate-General for Fiscal Matters; International Fiscal Matters Department

Decision dated 10 March 2004, no. IFZ2004/113M

On behalf of the State Secretary for Finance, the Director-General for Fiscal Matters has decided upon the following.

1. Introduction

According to article 15, first paragraph, of the OECD model convention, the income generated by work carried out in one country (the work country) by someone living in another country, may be taxed in the work country. The second paragraph makes an exception to this where the presence of the employee in the work country during the relevant period does not exceed 183 days. One of the conditions to applying the so-called 183-day regulation is that the remuneration for the activities is paid by or on behalf of an *employer* who is *not* resident in the work country.
Up till now, in interpreting the above-stated concept of employer in the conventions – which agree on this point with the OECD model convention – the Netherlands has taken as starting point the formal concept of employer (this being under the premise that the formal employer is usually also the material employer). In principle, the criterion in a formal approach is with whom a civil law employment contract has been negotiated. In fact, a purely material approach is only applied in the Netherlands in situations of abuse, as referred to in point 8 of the comments to article 15 of the OECD model convention. On 28 February 2003, the Supreme Court of the Netherlands rendered a judgement that raises the question as to what extent this is still tenable (Supreme Court of the Netherlands, 28 February 2003, no. 37 224, United Nations 2003/15.12).

2. Supreme Court ruling

In its ruling dated 28 February 2003, the Supreme Court indicates that for interpreting the concept of employer from the so-called 183-day regulation of the tax convention, it is not possible to adhere to the conclusion as to who is considered the employer (liable to deduct tax) for the Wages and Salaries Tax Act 1964. Furthermore, according to the Supreme Court, neither is the person with whom the employment contract was negotiated decisive. The capacity of employer in relation to the convention requires at least a relationship of authority with the employee involved for the relevant activities in the work state.
In my opinion, the above-mentioned considerations relating to the interpretation of article 15, paragraph 2, of the tax convention with Poland are also important for the other tax conventions entered into by the Netherlands which apply a similar concept of employer as in the OECD model convention. In the above-mentioned case, it was established that the interested party *did not* have a relationship of authority with the Polish corporation for his employment activities in Poland. As a result the Supreme Court did not need to go into further detail about the exact contents of the relationship of authority requirement. Neither did the Supreme Court indicate which other criteria (might) also play a role in addition to the relationship of authority.

3. An employment agency loaning out an employee with a temporary employment contract

In practice it is often the case that persons not resident in the Netherlands carry out activities temporarily in the Netherlands via a foreign employment agency. In such cases the employee is employed by the foreign employment agency for the duration of the activities in the Netherlands. If the employee's stay in the Netherlands does not exceed 183 days, and the foreign employment agency does not have a permanent branch or permanent representative in the Netherlands, what is important for determining the Dutch right to levy tax under the tax conventions (in conformity with the OECD) is whether in this situation one can say that the remuneration is paid by or on behalf of an employer in the Netherlands. In other words: what is important is whether whoever is borrowing the employees (the recipient) can be regarded as employer for application of the convention. If this is the case, then the Netherlands has the right – as long as the remuneration is paid by or on behalf of that employer – to levy tax over the income earned from the work carried out in the Netherlands.

Assuming a formal approach, the employment agency with which the employment contract was entered into will generally be regarded as employer in the sense of the convention. However, what follows from the above-mentioned ruling dated 28 February 2003, is that in such cases it will not be sufficient to simply apply a mere test of formality. The material relationship between the foreign employment agency, the Dutch recipient and the employee will also have to be taken into consideration.

Testing for a material relationship

As the occasion arises, the relationship between a foreign employment agency, a Dutch recipient and an employee takes shape such that as soon as the activities for the Dutch recipient have ended, the employment contract with the foreign employment agency will also end. The recipient has the authority to determine at any given moment that he no longer requires the employee. In fact, the authority to dismiss and the assessment of the employee rest upon the recipient. Furthermore, the recipient determines the number of employees he requires and their qualifications. Determining the actual authority over (carrying out) the activities also rests entirely upon the recipient. There is usually a direct link between the payment of the employee and the reimbursement paid by the recipient to the employment agency for the loan, so that the employment agency hardly runs any risks at all on this point. In this way, the foreign employment agency hardly exercises any employer's functions at all from a material point of view.

New line of policy

On the basis of the ruling dated 28 February 2003, in the above-described situation whereby the foreign employment agency hardly fulfils any actual employer's functions at all, in future the recipient will be regarded as the employer for application of the so-called 183-day regulation of tax conventions (which agree with the OECD on this matter). Furthermore, the requirement that the remuneration must have been paid by or on behalf of a Dutch employer is fulfilled due to the link between the remuneration for the loan and the payment of the employee.
In practice it is not always easy to determine whether a person working in the Netherlands has been employed by a foreign employment agency as described above. In many instances this will be the case. For this reason the point of departure adopted when taxing non-residents who have carried out activities in the Netherlands via a foreign employment agency will be that the recipient must be regarded as employer in the sense of the convention. This means that the Netherlands has the right to levy tax under the tax conventions (in conformity with OECD) over income generated by those activities, even in the situation that the employee's stay in the Netherlands did not last longer than 183 days.
Persons involved (employment agency, employee and/or recipient) can subsequently make plausible that in a concrete case the employer's function of the employment agency was of more substantial importance than described above. This is the case, for example, if the employee's employment with the foreign employment agency is such that the latter is running a real risk of continued payment of wages over periods in which the employee cannot be loaned out due to a lack of work. In such a case the employment agency will usually fulfil a real independent function with respect to determining the place of activities (loaning out), assessing the employee and determining his conditions of employment. Obviously, when in doubt, certainty can be obtained in advance from the competent inspector.

Liability to deduct tax

The above-described qualification for convention purposes is, for the rest, unrelated to the question as to who must be regarded as the withholding agent (employer) for income tax. If the recipient has to be regarded as employer for convention purposes, without the relationship between the recipient and the employee being considered as employment in the sense of the Wages and Salaries Tax 1964, it is still the foreign employment agency, as the withholding agent in the sense of that law, that is responsible for deducting the wage tax (see article 6, first paragraph, section *a*, second paragraph and third paragraph, section *b*). In situations in which the Netherlands has the right to levy tax under the applicable tax convention, the employment agency is obliged to deduct and hand over the wage tax. In addition, article 34, first paragraph, of the Collection of State Taxes Act 1990 stipulates that the recipient is responsible for the tax owed.

Only for the levying of tax

Furthermore, we must point out, perhaps unnecessarily, that the present decision covers the application of tax conventions, so that (as a result) it is only relevant to the levying of tax. Separate allocation rules apply for the levying of national insurance contributions.

Residents with work activities abroad

The above-described explanation of the concept of employer for tax conventions will also be the point of departure in the reverse situation of a resident in the Netherlands who carries out work activities abroad for a foreign recipient via an employment agency. It will then be up to the tax-payer to plausibly demonstrate that the situation is such that the employment agency does not fulfil any notable employer's functions, and that the foreign recipient can therefore be considered as employer in the sense of the convention.

4. Other situations, current procedures and determining a definitive position

Subsequent to the ruling dated 28 February 2003, the Supreme Court is currently dealing with a number of other actions about the interpretation of the concept of employer in various conventions. These cover various situations of loaning employees out within the same group of companies, whereby not only the recipient, but also the loaning company, fulfil actual employer's functions. For example, I have appealed against the decisions of the court of appeal in The Hague dated 29 April 2003, nos. 01/1970 and 01/1971.
On the basis of the judgement of the Supreme Court in the current procedures, greater clarification is expected about the interpretation of the concept of employer in the conventions, also for other situations than that described above under point 3. This decision will be adjusted if warranted by the judgement of the Supreme Court.

5. Entry into force

The current decision is applicable as of 1 January 2004.
In situations in which the line taken up till now did not require the deduction of income tax by the foreign employment agency, it has been approved that the foreign employment agency only needs to apply the new policy on wages received by employees from 1 April 2004 on.