



WHY PERMANENT ESTABLISHMENTS HAVE NO GUIDANCE AND MECHANISM IN GUATEMALA?

MONTHLY NEWSLETTER THE LAW FIRM OF CENTRAL AMERICA

Permanent Establishments (hereinafter "PE") are regulated in Article 7, of Decree No. 10-2012 of the Congress. Although its regulation dates to 2013, the Tax Administration Office (hereinafter "SAT") has not shown interest in developing a criterion and internal regulations so that a non-resident can effectively constitute a PE in Guatemala.

In simple terms, a PE is considered as an extension of a non-resident person, it is not a different legal person, therefore it does not have legal personality and is considered internationally as a passthrough entity.

PE is used exclusively in tax matters and international taxation for the purpose that the countries, considered as Source States (which are the jurisdictions where the income is generated and do not necessarily correspond to the residence State, which seeks to tax the same income) may, under its tax sovereignty, levy said income by constituting a PE to which the profits or income generated can be attributed.

The concept of PE under Decree 10-2012, considers that there are 3 different types of PE that could be constituted in Guatemala by a non-resident, as follows:

- i. Physical PE.
- ii. Construction PE.
- iii. Agency PE.

The physical PE is considered the traditional type of PE, under which multinational companies can carry on business activities, commerce or perform income generating activities in other States. In Guatemala, to constitute this type of PE it's necessary that a non-resident person (individuals, legal entities, international organizations, entity or patrimony) maintain in Guatemala in a continuous or habitual manner a fixed place of business, facilities or workplaces of any kind, in which it performs all or part of its lucrative activities.

It is considered as the traditional PE, since it is necessary to have a fixed place of business, this being understood as any geographically specific point in Guatemala, with a certain degree of permanence where a person carries on business activities, commerce or income generating activities, thus, a fixed place of business is not limited to: place of management, branches, offices, factories, workshops, warehouses, stores or other establishments, agricultural, forestry or livestock exploitations, mines, oil or gas wells, a quarry or any other place of extraction or exploitation of natural resources.

A construction PE is deemed to exist when a non-resident person carries on construction or installation projects and even supervision activities that are related to such projects, if these projects or constructions exceed the 6 months threshold. Said definition of Construction PE is based under the PE concept in the Model Convention (hereinafter "MC") of the United Nations Organization (hereinafter "UN"), rightly based on the UN Model by the legislator, as this was developed to be negotiated and subscribed for developing countries, protecting taxable income generated in the Source States, unlike the MC, which was developed by The Organization for Economic Co-operation and Development (hereinafter "OECD"), which gave rise to taxation in the Residence State.

Regarding the Agency PE, a PE is deemed to exist when the non-resident performs through a dependent agent, (third party) activities that are related to its activity and:

- Holds and habitually exercises in Guatemala powers to conclude contracts on its behalf, or,
- It does not hold powers, but habitually keeps in Guatemala goods to be delivered on its behalf to the recipient.

Notwithstanding the above, an agency PE will exist in the following circumstances:

ii. If an insurance company collects premiums in the national territory or insures risks located therein through a person resident^[1] in Guatemala.

i. A financial entity has a PE when it has in Guatemala a fixed place of business, facilities or places of work of any kind in which it carries out operations as collection of liabilities or placement of assets in the national territory through a person^[2], without prejudice to the regulations on Banks and Financial Groups.

Considering the above mentioned elements for the types of PE under our legislation and knowing that a PE is not a legal person, if a non-resident wishes to constitute a PE in Guatemala, for the reasons applicable to each specific case, SAT will request that the registration process is done as a branch of a foreign company, which denaturalizes a PE, since it is constituted for tax purposes and does not have the formal characteristics of a branch, based on the scope of the limitations that Article 220 of the Code of Commerce establishes to exercise activities without the need to register a branch, which are quite limited.

Nonetheless, it must be considered that the PE arises from a need to collect and facilitate the taxation in order to balance international tax burdens and eventually allow the taxation of digital services used by Guatemalans. SAT's current criterion and the lack of implementation of mechanisms and guidance to register a PE, results in a higher tax collection and perhaps this is the reason for the lack of interest in regulating it. A branch, besides incurring in registration and withdrawal costs, would be registered in the corporate income tax regime or in the optional simplified regime income tax, which taxes income at a rate of 25% on net income, in the first case, and 7% on gross income, in the second case. These same regimes would apply to a non-resident with PE.

Non-residents without a PE, on the other hand, are subject to withholding tax according to tax rates ranging from specific rates such as 3%, and for general business activity at a tax rate of 25%, which are generally applied on gross income or the accredited amount. This being in many cases a higher effective tax rate paid than if the non-resident constituted a PE in Guatemala under the corporate income tax regime on net income, since this regime allows them to deduct costs and expenses from their income. This is a more attractive tax collection scenario for SAT, rather than developing an effective criteria, mechanism, and guidelines for the constitution of PE in Guatemala.

[1] Article 6 of Book I, Income Tax, Ley de Actualización Tributaria, Decree 10-2012

[2] Article 6, Governmental Agreement 213-2013 Regulation book i of the Tax Update Law, Decree 10-2012.

Written by:



Ximena Tercero
Partner
Ximena.Tercero@ariaslaw.com



Estaymer Mendoza
Associate
Estaymer.Mendoza@ariaslaw.com