1. - INTRODUCTION.

The analysis of no matter which legal problem related to a permanent establishment forces us to use as points of reference, at least, these two aspects:

1) The foundations of the institution and the goals and objectives pursued with her. Specifically, balancing tax revenues from countries that impose tax on worldwide income and tax revenues from source States, where the income is earned.

2) The rigorous application of legal techniques with which to delimit, specify and set the keynotes of a permanent establishment.

Even more, if the work is based on the analysis of court decisions, not only this analysis is determinant. We should pay special attention to the facts underlying the case solved.

The distinction between "facts" and "law" is not always easy. It might even affect the decision-making body's sphere of competence. This is quite usual in the Continental European legal system. It is frequent, for instance, in the Spanish appeal, where the jurisdictional competence is restricted, on one hand, to points of law (factual issues are excluded) and, on the other, to the motives invoked by the appellant on the appeal.

2. - THE DECISION OF THE SPANISH SUPREME COURT OF 12TH JANUARY 2012

In this particular case, the decision taken by the Spanish Supreme Court aims to answer if there was a fixed place of business permanent establishment.

Well, the answer requires a careful exam of the factual situation raised before the Supreme Court. However, it is also important to underline the implications that the facts, as described, have for the Court. In this regard, it is worth mentioning that, according to a Spanish classical legal expression, "things are what they are and not what the parties involved say they are".

It follows that, in the situation solved by the Supreme Court, we should bear in mind that, as from 1st of July 1999, Roche Vitamins Europe bound to the Spanish limited company Roche Vitaminas under two contracts: a manufacturing agreement and a promotional agreement.

Under the first of those contracts, Roche Vitamins Europe, licensee of certain formulas, know-how, patents and trademarks in the pharmaceutical, cosmetic and animal food sectors,

contracted Roche Vitaminas, the owner in our country, Spain, specifically in San Fernando de Henares, Madrid, of facilities used to manufacture products of those sectors for their subsequent sale. Roche Vitaminas undertook to prepare and package the products and to sell them to the Swiss company, pursuant to the instructions given by the latter, which undertook to acquire those products. The price was determined for each year according to the production costs, to which there was added a margin specified according to market criteria. Roche Vitaminas accepted liability for defects due to incorrect application of quality parameters, while Roche Vitamins Europe would bear those arising from improper specification of those parameters or from their modification after the goods were manufactured.

In the second contract, Roche Vitaminas undertook to promote in Spain the merchandise, while Roche Vitamins Europe purchased from her, as well as those others which the Swiss company acquired in intra-community transactions. In addition, by virtue of this business, the former leased to the latter a warehouse of 22 square meters for deposit of the products prior to their distribution to the clients. In any event, the price of sale to third parties was set by Roche Vitamins Europe, which issued and sent the relevant invoices, although the purchase orders could be managed by either of the two companies indistinctly, without, however, the Spanish company being able to alter or negotiate the terms of sale or accept any contract for the account of the Swiss Company. The compensation consisted of 2% of the sales in Spain, which would be added to the costs incurred by Roche Vitaminas, plus 750 pesetas for each square meter of the leased warehouse.

Both contracts, as is emphasized in the claim, entailed a change in strategy, whereby Roche Vitaminas, theretofore manufacturer, importer and seller of the products, began to produce them for a single client, Roche Vitamins Europe, who then proceeded to introduce them in the market. The aim was to reduce costs, by centralizing them in a single country: Switzerland.

The Spanish Supreme Courts sets out its conclusions on the existence of a permanent establishment in the following terms: “The Spanish company, during the term of the contracts, only existed to serve the Swiss company and, without running any risk whatsoever, to manufacture its products according to its strict instructions, promoting them and participating in the performance of the sales agreements. It had no other mission. This chamber is mindful that production-to-order constitutes a normal practice in the market. Nor are we unaware that it is possible to establish a price for the manufacture as a function of the costs, plus a remunerative percentage for financing the production. And we can admit that the existence of companies with only one client is not outlandish. But the conjunction of the three factors supports the deduction that the case at issue here fulfils the defining characteristics of a dependent agent permanent

establishment for purposes of the Spanish-Swiss treaty for the avoidance of double taxation, as follows from the interpretation expounded above".

From this strict perspective, it may be concluded that Roche Vitaminas is not operating in Spain as agent of Roche Vitamins Europe, because, as adduced in the claim, under the second of the contracts signed, the promotional agreement, it did not have authority to conclude contracts in the name of the principal, not even to negotiate them, with its authority being confined to the management of purchase orders. Such information gives rise to the following comment: "Now, it must not be overlooked that the said contract also obliged it to promote the products that Roche Vitamins Europe purchased from it and stored in the leased premises, along with those acquired in intra-community transactions. This task introduces a point of greater intensity in the relations between the two companies, as the Spanish was not confining itself to processing the purchase orders received from Switzerland, signing the contracts with no capacity for innovation, but, due to its promotional authority, it had to do everything needed to enforce the qualities of the products offered by Roche Vitamins Europe. To this we must add the existence of the manufacturing agreement, which we will now take up when considering the negative perspective of the concept of dependent agent".

Accordingly: "The location of the business risks is a salient factor for measuring the degree of independence. Now, in the case at issue here, it was borne by the foreign company, as the negative consequences for Roche Vitaminas's net worth of improper execution of the orders received do not go beyond the effects that might be suffered by an employee who does not comply with the orders of his principal adequately. It must be borne in mind that the more a principal/agent relationship resembles that of an employer/employee, the more likely that the agent will not be considered legally independent. In addition, given the price paid by Roche Vitamins Europe to the Spanish company for the goods it produced (cost of production plus a percentage), it is plausible to deduce that the latter did not assume economic or financial risk. In short, "it is one thing to manufacture according to a customer's instructions and even accept price ceilings […] and quite another one to manufacture for only one customer, at his orders and pursuant to his instructions […] at price equal to cost plus a simple commission […]" (fourth paragraph of foundation 4 of the assessment order dictated on 23rd of April 2003 by the head of the inspectorate technical office).

In summary, from the standpoint of interest here, Roche Vitamins Europe produced in Spain through a dependent agent, Roche Vitaminas, the goods that it later marketed, assuming the contingencies proper to all business activity. It cannot be argued that the said manufacturing activity was of an auxiliary, secondary or preparatory nature for its principal business. This should be excluded under article 5 (3) of the treaty, which, intended to delimit the notion of

fixed place of business, can be applied by analogy for an analysis of the position of dependent agent. In the first place, because, in fact, it was a basic condition without which the business object could not have been achieved. And, second, because it did not fit any of the auxiliary or preparatory operations set down in that provision, which, given that it lays down an exception, should be construed restrictively".

Within this context, I find extremely interesting the considerations put forward by the Spanish Supreme Court by stating that: "Having established the foregoing, it bears emphasis that the OECD Committee on Fiscal Affairs advocates a strict interpretation and application of this provision and, therefore, of the concept in question, because a broad interpretation would lead to finding permanent establishments exist in all cases where one enterprise engages in crossborder operations through a "dependent person", and the resulting tax burden would hamper the interests of international economic relations (paragraph 32 of the commentary on article 5 of the Model Convention). Consequently, this classification should be limited to those persons who, given their power to contract, involve the non-resident enterprise in the business activities of the state of taxation. So it is a matter of evaluating the agent's capacity to effectively bind the principal enterprise to third parties. Needless to say that capacity must refer to the contracts entered into within the scope of the business proper to the foreign enterprise".

It has been already said that the decision of the Spanish Supreme Court notably provides a dynamic interpretation of the wording of the Convention. But this is not true. On the contrary, it provides that regarding the contracts between the Swiss company and the Spanish company, the former concluded contracts binding on the latter.

3.- <u>THE DECISIONS TAKEN BY OTHER SUPREME COURTS</u>.

It is interesting to note that other countries have rejected the existence of permanent establishment. Examples include the Zimmer decision of the French Conseil d'État and the Dell Products decision of the Norwegian Supreme Court.

From my point of view, these decisions offer different results, rather than contradictory solutions, because they start from widely divergent positions and facts. Indeed, the contracts concluded in the Zimmer and in the Dell Products cases were not as complex as the ones in which the Swiss company, Roche Vitamins Europe, entered.

4. - <u>CONCLUSION</u>.

In my opinion, the three judgements mentioned are different, but not contradictory, because the facts upon which the Supreme Courts decided were not the same.