KÜFFNER MAUNZ LANGER ZUGMAIER

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KMLZ VAT NEWSLETTER

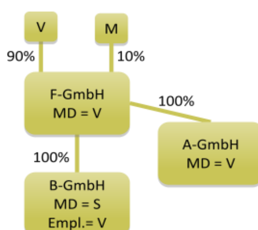
New hope for VAT groups

Federal Fiscal Court reduces requirements for an organizational incorporation

Large groups of companies find it difficult to establish the organizational incorporation for a VAT group. Most recently, the V. Senate interpreted this requirement very strictly. Now, the XI. Senate has deviated from that. An organizational incorporation can also exist without the managing director being both managing director of the parent company and the subsidiary. Thus, in particular, the general meeting's rights to instruct, as well as the parent company's managing director's right to instruct vis-à-vis the subsidiary's managing director, might be sufficient.

1. Facts – Federal Fiscal Court, decision of 12.10.2016 – XI R 30/14

During the relevant years, a married couple, were the sole shareholders of a company, namely F-GmbH. The husband/father (V) held 90% of the shares and the wife/mother (M) held 10%. V was the managing director of F-GmbH. F-GmbH itself held a 100% stake in A-GmbH. V was also the managing director of A-GmbH. F-GmbH also held a 100% stake in the plaintiff. The plaintiff's sole managing director was V and M's son (S). S's position was based on a service agreement without a fixed monthly salary. V was employed by B-GmbH, and received remuneration from it. The company set up is depicted below:



S was required to comply with the instructions issued by the shareholders' general meeting as well as the managing director of A-GmbH (= V). He required prior consent from the shareholders for actions which were beyond the plaintiff's normal commercial operations. As it transpired, S did not actually take care of the family's business. He allowed V to manage things without restriction. Thus, V factually conducted B-GmbH's business. It was left open to question, whether B-GmbH formed a VAT group with F-GmbH.

2. Legal opinion of the Federal Fiscal Court

Justifying a VAT group requires the financial, economic as well as organizational incorporation of the subsidiary into the parent company. In the present case, the Federal Fiscal Court, recognized the organizational incorporation. First, it considered V's factual management of B-GmbH to be insufficient. Otherwise, the legal requirement that the same persons govern both bodies of F-GmbH and B-GmbH would have to be considered as having been fulfilled. This would have justified the organizational incorporation.

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Both Senates of the Federal Fiscal Court, as well as the fiscal authorities insofar, agree on this point (sec. 2.8 para. 8 sentence 2 of the German Circular).

In its decision, the Federal Fiscal Court still assumes that any institutionally approved direct intervention options into the core business of the controlled company's current management are deemed to justify an organizational incorporation. Both Senates of the Federal Fiscal Court and the fiscal authority also agree on this (sec 2.8 para. 10 sentence 2 of the German VAT Circular).

The Federal Fiscal Court deemed such intervention options to be present in the case due to V's status. It justified this stance by means of the general meeting's managerial authority as well as V's authority as managing director of A-GmbH vis-à-vis S. In doing so, the XI. Senate objects the V. Senate's caselaw – without justification. Only recently, the V. Senate has held that, intervention options into the core business of the current management, such as the right to instruct, reporting obligations or a right to reserve approval in favor of the general meeting or in favor of the majority shareholder, should be deemed inadequate (see Newsletter 03/2016).

The Federal Fiscal Court referred the proceedings back to the tax court on the basis of another issue. According to both Federal Fiscal Court Senates' case-law and the fiscal authority's view (sec. 2.8 para. 2 sentence 2, 6 of the German VAT Circular), only one taxable person can be the parent company. As in its last decision, the XI. Senate of the Federal Fiscal Court refers once again to its (seemingly existing) doubts as regards conformity with EU law with respect to this requirement. The V. Senate of the Federal Fiscal Court, however, assumes the German regulation to be explicitly in line with EU law.

3. Consequences for the practice

In its decision, the XI. Senate, disagrees with the V. Senate, in particular, as regards one substantial part of the caselaw for larger groups of companies. The V. Senate's strict requirements are often not practicable in multilevel group structures. The parent company's managing director cannot really conduct the day-to-day management in all the subsidiaries. Due to limitations of liability and e.g. participation rights, this is often also impossible or not intended. Based on the same grounds, a controlling agreement, which would be appropriate to justify institutional intervention options in accordance with sec. 2.8 para. 10 sentence 4 of the German VAT Circular, cannot be concluded.

The right to issue instructions exercised by a general meeting or one of the parent company's managing directors, is, according to the Federal Fiscal Court XI. Senate possible. The XI. Senate expressly confirms the German VAT Circular's view according to which it would also be sufficient if the parent company is in a position to prove its power to make decisions vis-à-vis third parties through written agreements (e.g. managing director policy, corporate guidelines) and to hold responsible the parent company's managing director if the parent company's instructions are not observed. In doing so, the Federal Fiscal Court comes closer to reality: Because, a managing director of a subsidiary who does not comply with the instructions of the group board will soon no longer be managing director.

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