KÜFFNER MAUNZ LANGER ZUGMAIER

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KMLZ VAT NEWSLETTER

Tax benefits for cost sharing associations – the small VAT group?

VAT exemption for cost sharing associations

In its judgment of 4 May 2017 – C 274/15 – C*ommission/Luxemburg*, the ECJ gave its opinion on the independence of associations and immediacy of the use of transactions within the meaning of Art. 132 para. 1 lit. f of the VAT Directive. This judgment is the first of a series of ECJ judgments on the interpretation of this regulation. Opinions on various aspects of further proceedings currently pending before the ECJ have already been published. The ECJ's case law will have a significant impact on German law, as Germany has only implemented the Union tax exemption regulation for cost sharing associations to a very limited extent.

1. Background

The ECJ judgment of 4 May 2017 – C 274/15 – is the first of a series of expected ECJ judgments, which deal with the interpretation of the tax exemption regulation of Art. 132 para. 1 lit. f of the VAT Directive (C-616/15, C*ommission/Deutschland*; C-605/15, *Aviva*; C-326/15, *DNB Banka*). These ECJ judgments will have a significant impact on German law.

Germany has implemented the Union VAT exemption regulation for cost sharing associations in sec. 4 no. 14 lit. d German VAT Act but only to a very limited extent. Infringement proceedings are currently pending. Advocate General *Wathelet* stated, in his Opinion of 5 April 2017 – C-616/15, *Commission/Deutschlan*d, that Germany infringed Art. 132 para. 1 lit. f of the VAT Directive by restricting the VAT exemption to the "*associations whose members exercise a limited number of professions*". The Advocate General even considers that the VAT exemption is not only limited to acts of common interest under Art. 132 of the VAT Directive, but also to other VAT-exempt activities pursuant to Art. 135 of the VAT Directive. Such a broad interpretation of Art. 132 para. 1 lit. f of the VAT Directive would have a serious impact on the German legal situation. If a definite tax burden is to be avoided for cooperation between companies, which are not entitled to VAT deduction, only the legal institution of the VAT group is eligible. However, the requirements of sec. 2 para. 2 no. 2 German VAT Act are narrow, since VAT groups require financial, economic and organizational integration. In addition, only a controlled company can be integrated in the controlling company. The case law does not acknowledge multiple parent VAT groups (see German Federal Fiscal Court of 3 December 2015, V R 36/13). The association of several companies, by means of a VAT group, in order to render IT services free of VAT to their members, which are not entitled to deduct VAT (e.g. banks, insurance companies), is therefore impracticable.

One way out of this tax dilemma will probably be the VAT-free cost sharing association within the meaning of Art. 132 lit. f of the VAT Directive – the so-called "small VAT group".

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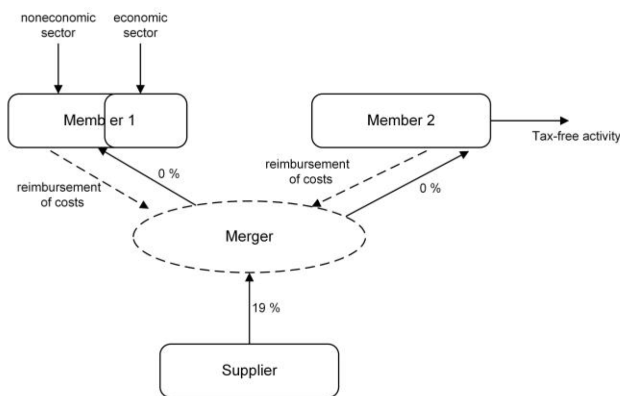

2. Facts

In case C-274/15, *Commission/Luxemburg*, the ECJ had to deal, inter alia, with the question of whether it is compatible with Art. 132 para. 1 lit. f of the VAT Directive, that services rendered to the members of a cost sharing association are exempt from VAT if the members of this association, which also carries out taxable supplies, are likely to generate sales before taxes not exceeding 30% of their total turnover before tax.

3. Decision by the ECJ

The ECJ issued its opinion on the question of the independence of the association and the immediacy of the use of the transactions. Accordingly, the association must be an independent taxable person separate from its members. It therefore follows that transparent groups without their own legal personality should not be permissible.

The ECJ considers it to be harmless if the members of the association exercise taxable activities, that is mixed output turnover. However, the merger will only benefit from VAT exemption if it provides services directly for the purposes of the activities of those members who are exempted from taxation or for members who are not taxpayers.

The ECJ does not explicitly define the term "immediacy". It merely points to the fact that the criterion of immediacy is to be strictly interpreted in accordance with national law. Moreover, there is no direct link between the debiting of overheads and the VAT-free activity.

4. Impact on the practice

What does "immediate" mean? In practice, this is the core problem. According to the present national understanding, this requirement is interpreted strictly. According to the case law of the Federal Fiscal Court, general administrative acts, which only prepare and support medical treatment in general, are not VAT-free according to sec. 4 no. 14 lit. d of the German VAT Act. The fiscal authorities agree (see sec. 4.14.8. para. 3 sentence. 2 German VAT Circular). However, VAT exemption would only become interesting if general administrative acts were also exempt from VAT. This could lead to debiting personnel costs to the members of the association without VAT. The differentiation between overheads and individual costs is unlikely to be helpful. The independent association must be able to determine, with legal certainty, whether its output turnover is VAT-exempt or taxable. However, the association cannot know how individual members of the association will use this service. It may, at best, presume how the services will be used.

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