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VAT NEWSLETTER

German Federal Fiscal Court on bonuses for centralised settlement – clarity and need for action at the same time

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1 Background

Where goods are bought and sold in large volumes, centralized settlement providers often come into play. Member companies become affiliated with a provider in the hope of obtaining better terms when purchasing goods from suppliers by bundling their demand. The centralized settlement business is based on numerous different legal relationships. Among other things, the central clearing agent receives bonuses from suppliers, which it passes on, in whole or in part, to its affiliated companies. In 2014, the ECJ (*Ibero Tours* – ref. C-300/12) and the Federal Fiscal Court (ref. V R 3/12) ruled that the passing on of these bonuses is not subject to VAT. Previously, central settlement agents had reduced the VAT liability on their intermediary services due to the passing on of these bonuses. Their members had, correspondingly, reduced the input VAT on the goods purchased from the suppliers. In practice, the changed case law required enormous adjustments.

2 Facts of the case

The decision is based on a typical case of centralised settlement. In this particular case, the goods were sold in a transaction carried out directly between the supplier and the member company. The central settlement agent negotiated with the suppliers in the absence of any influence exerted on behalf of the member companies. The agreed terms included bonuses to which the member companies were entitled (so-called house bonuses), as well as bonuses, which the settlement agent collected in its own name (so-called group bonuses). The latter payments were made by the suppliers to the central settlement agent for economic advantages, such as bundling functions, condition negotiations, demand promotion, etc. The central settlement agent passed on all bonuses to its member companies.

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The dispute, in the present case, concerns the group bonuses collected by the central clearing agency in its own name. In accordance with the original legal situation in the disputed year 2012, the central clearing agency reduced the tax base when the group bonuses were passed on to the member companies. These members reduced the input VAT from the purchased goods in accordance with sec. 17 para 1 sentence 2 German VAT Act, although this is a separate supply. On the basis of the changed case law, the member company later applied for the reversal of the input VAT adjustment. The Fiscal Court dismissed the appeal. In a break with the case law, it held that an economic assessment had to be made, deviating from the civil law agreements. According to this assessment, the group bonuses were economically directly related to the sales of goods to the member companies. In essence, they were reductions in the purchase price.

3 Decision of the German Federal Fiscal Court

The appeal against the decision of the court of first instance has been successful. The Federal Fiscal Court clearly and stringently presents the development of case law and emphasizes that, for VAT purposes, the decisive factor is whether a discount is granted within or outside a chain of supplies. In the present case, there is no chain of supplies. This is because the contractual supplier directly supplies the central regulator's connected company. The central coordinator, on the other hand, provides a service to the contractual supplier. According to the *Ibero-Tours* ruling of the ECJ, this excludes any reduction of the tax base.

Fortunately, the Federal Fiscal Court also examined the reasoning of the Münster Fiscal Court. It is correct that the group bonuses, which were passed on, are related to the purchases of goods. However, this does not distinguish the case from the case law, but rather is common practice when intermediaries pass on discounts. After all, the passing on of discounts always has something to do with the turnover generated by the intermediary. The more recent ECJ rulings, on legally prescribed discounts in the pharmaceutical sector, did not preclude this conclusion, as there was no legal obligation to grant the discounts in the present case. The differences to the Federal Fiscal Court proceedings (Ref.: V R 20/23), in which a central settlement agent took legal action, were also not relevant to the decision. In this case, the Federal Fiscal Court also ruled that group bonuses, which have been passed on, are not subject to VAT and that the central regulator cannot reduce its VAT on services to suppliers. It now remains for the Münster Fiscal Court to clarify, in the further proceedings, a number of questions that did not arise due to its legal opinion.

4 Consequences for the practice

Member companies: They can be happy about the decision. It is now settled case law that they are not required to reduce the input VAT deduction on purchases of goods due to group bonuses. After the change in case law in 2014, many refund applications were filed. Several of these cases are still pending. With this decision, the pendulum is clearly swinging in favour of the member companies' refund claims.

Central settlement agencies: Some central settlement agencies have not implemented the change in case law, for example because they believed – like the Münster Fiscal Court – that they were in a different situation. This decision makes the air thinner and the risk significantly higher. This is because these central settlement organisations are still reducing their VAT, possibly unlawfully. They must immediately review the VAT treatment of their service relationships and, if necessary, adjust their invoices. This applies both in relation to the member companies and to the contractual suppliers.

Supplier of goods: The decision also clarifies that the group bonuses constitute remuneration for a service provided by the central settlement agent to the supplier. Suppliers therefore require an invoice from the central settlement agent in order to deduct input VAT. However, there is no reduction in remuneration whereby VAT is reduced when payment is made.

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