KPMG

Tax Matters Digest

March 2017

DNB Banka (C-326/15) and *Aviva* (C-605/15) Advocate General Opinions

The same Advocate General (AG) has delivered Opinions in these two cases concerning the cost sharing exemption under Article 132(1)(f) of the VAT Directive. This requires Member States to exempt:

> 'the supply of services by independent groups of persons, who are carrying on an activity which is exempt from VAT or in relation to which they are not taxable persons, for the purpose of rendering their members the services directly necessary for the exercise of that activity, where those groups merely claim from their members exact reimbursement of their share of the joint expenses, provided that such exemption is not likely to cause distortion of competition.'

DNB Banka was a Latvian referral and *Aviva* was from Poland.

DNB Banka (C-326/15)

DNB Banka (DNB) provided exempt financial services. The supplies in dispute were those DNB received from other companies within the corporate group. These were:

- Financial services from its parent company DNB Nord AS (in Denmark);
- IT services from a sister company, DNB Nord IT AS (Denmark); and
- A cost allocation from a sister company, DNB Bank ASA (in Norway), for software licenses purchased from a third party.

DNB was invoiced by the Danish companies at cost plus 5 percent. The background was not explicit and only states that the Danish Tax Authorities took the view that the supply of services is not exempt. The AG looked at the following issues:

Definition of an independent group – The AG considered that the referring court was asking whether an independent group of persons must be a separate entity or, can it, as in the current case, consist of a group of related undertakings. The AG was of the view that the Article 132(1)(f) group has to be a taxable person but does not need to be a legal person. The AG noted the existing case law regarding the criterion of independence under Article 9(1), which defines a taxable person. Whilst noting that a company with several shareholders within a group could be regarded as an independent group, it can only exempt supplies to its shareholders (who are its only members). However, the AG was of the view that in the current case, where the group consists of related companies, there is no independent group. An independent person has to be able to own its own property. Property probably means more than immoveable property here.

Scope of the exemption – The AG was of the opinion that the cost sharing exemption only applies to supplies to members whose activities are covered by the public interest exemptions under Article 132(1) and therefore does not cover supplies to members in the financial services sector. The AG's reasoning, based on the drafting and the history of that part of the Directive, is not included in this Opinion but cross references to the same AG's Opinion (AGO) in *Aviva* (C-605/15) which was delivered on the same day (see below).

Cross border groups – Again, cross referring to the *Aviva* AGO, the AG was of the view that the cost sharing exemption does not apply to cross border supplies.

Uplift – One specific question referred to the Court of Justice of the European Union (CJEU) related to where costs are uplifted. In the current case direct taxation rules required expenses to include an uplift of 5 percent. Based on the wording of the exemption, which refers to 'groups merely claim from their members exact reimbursement of their share of the joint expenses', the AG was of the opinion that the exemption would not apply.

To access the AGO click here.

Aviva (C-605/15)

The Aviva Group is an insurance provider that is considering setting up shared services in a number of Member States under a European Economic Interest Group (EEIG). All members are within the Aviva corporate group. The centres will provide services such as HR, financial and accounting services, IT services, administrative services, customer service facilities or new product development services. The Polish tax authorities challenged the potential application of the exemption on the basis that the absence of a reverse charge by service recipients in Poland would distort competition. The reference to the CJEU focused very much on distortion of competition. However, the AG opined on a wider range of issues.

Scope of the exemption – The AG noted the issues with the wording of the exemption and therefore considered the purpose of this exemption. Referring to the AGO in *Taksatorringen* (C-08/01), the AG was of the view that the purpose is to ensure that an undertaking which must buy in services is not placed at a competitive disadvantage by comparison with an undertaking which is able to have the services supplied by its own employees or as part of a VAT group. An exemption intended to offset a competitive disadvantage should not give rise to a distortion of competition. The AG added that if Article 132(1)(f) is to extend to other exemptions, the question as to which groups are intended to be included must be answered by reference to the purpose of the group members' activity to which the cost sharing exemption is to be extended. The AG noted insurance services are exempted to avoid double taxation (VAT on top of insurance tax) and the purpose of the banking services exemption is based on the difficulties in determining the taxable amount and recoverable VAT. However, such purposes do not extend to the services made by the EEIG. The AG went on to support her view based on the structure and the history of the legislation. The AG is therefore of the Opinion that the Article 132 (1)(f) exemption only applies to the public interest exemptions in Article 132(1). Note that this would not include social housing, where the exempt supply is one of rent. It also ignores the relief for supplies to members carrying on an activity in relation to which they are not taxable persons.

Cross border groups – The AG was of the view that the exemption does not apply cross border. The AG supported this on the basis that:

- In the Sixth Directive Article 13, the equivalent Article, was under the heading which stated 'exemptions within the territory of the country' (though the default place of supply rule then was where the supplier belonged and 132 has no such heading);
- Only chapters 4 to 8 and 10 in the VAT Directive contain special exemptions for cross border transactions; and
- A broader interpretation would:
    - be inconsistent with Article 11 on VAT groups, which is restricted to persons established in the territory of the Member State;
    - make the tax authorities' task of evaluating distortion of competition and the correct and straight forward application of exemption effectively impossible; and
    - lead to VAT avoidance through the use of countries with no VAT or even rate shopping within the EU.

Distortion of Competition – The AG then turned to the focus of the referral. The AG effectively said that the exemption and distortion are mutually exclusive. This on the basis that the purpose of the exemption is to avoid distortion of competition. If there is distortion of competition, this would suggest the exemption has been applied inappropriately. The indicators that this has happened are:

- the group supplies the same services for consideration to non-members;
- the primary purpose of the group's formation is simply to optimise the input VAT burden; and
- the group does not supply any services tailored to the specific needs of its members, with the result that its services could just as easily be offered by others too.

To access the Opinion click here. The Judgments are expected in the summer

Importance? The AG's Opinion that the cost sharing exemption only applies to supplies to members with activities covered by the public interest exemption has come as a bit of a surprise with neither the Commission nor a number of Member States, including the UK, being of that view. The CJEU has previously given judgment in *Taksatorringen* (C-08/01) which concerned a group of insurers. Whilst the specific question around scope of the exemption was not asked, the CJEU would normally note or at least comment that the exemption may not apply as that would be a crucial factor in answering the questions posed (since it would make them irrelevant). Reference to the unsuccessful proposal on the treatment of insurance and financial services also appears to have been a key factor for the AG's conclusion on the limited scope of the cost sharing exemption.

However, the proposal was more around clarification of the cost sharing exemption due to the lack of its harmonised application by those Member States that have implemented it, as opposed to an explicit widening of the exemption to include finance and insurance because it did not previously include them. This is only the AGO and we will wait and see what the CJEU says. However, if it is followed by the CJEU, an already narrow exemption will be restricted even further.

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