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VAT grouping and the Cost-Sharing Exemption: Similarities, Differences, and their Interaction

by

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HARN60 Master Thesis

Master's Programme in European and International Tax Law

2017/2018

Spring semester 2018

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Summary

The present thesis deals with two different provisions in the VAT Directive, the VAT grouping, provided in Article 11 of the VAT Directive, and the cost-sharing exemption, provided in Article 132(1)(f) of the VAT Directive. Both provisions are utilised by businesses in order to alleviate the undesirable consequences of the irrecoverable input VAT. The former establishes the VAT group whose intra-group transactions are not taxable for VAT purposes, while the latter provides for an exemption for services provided by an independent group of persons, the cost-sharing group to its members under certain conditions.

The brief wording of both provisions leads to interpretation difficulties, regarding the different aspects of the scope of the latter, which the CJEU and the European Commission try to resolve. In the present thesis, following the legal-dogmatic method, the fundamental aspects of the two concepts are analysed. The research question and the aim of the thesis are, after such an analysis of the two schemes, their similarities, and their differences, as well as their interaction to be presented in a comprehensive way.

Preface

The past academic year was a lifetime experience for me. The Master's Programme in European and International Tax Law exceeded my expectations.

I would like to thank all my professors and lecturers for sharing with me their knowledge in the field of tax law and in particular my supervisor, Marta Papis-Almansa for her help and insight for concluding this thesis. I would also like to express my gratitude for having as my professor, Oskar Henkow. I consider myself lucky for this and I will never forget him.

In addition, I would like to thank my classmates for their help and support. Finally, I would like to thank my family and especially my partner, because without their daily support and endorsement, I would have not been able to come to Sweden and accomplish my goals.

Abbreviation list

CJEU	Court of Justice of the European Union
EU	European Union
IBFD	International Bureau of Fiscal Documentation
p.	page
para.	paragraph
Sixth Directive	Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the member states relating to turnover taxes – Common System of value added tax: uniform basis of assessment [1977] OJ L145/1
TFEU	Treaty on the Functioning of the European Union
The Court	Court of Justice of the European Union
VAT Directive	Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax [2006]
v.	Versus
VAT	Value Added Tax
VAT Directive	Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax [2006] OJ L347/1
VEG	VAT Expert Group

Chapter 1: Introduction

1.1. Background

Article 9(1) of the VAT Directive provides that “*every person who carries out independently an economic activity is a taxable person for VAT purposes*”. This provision leads to the assumption that every person who carries out independently an economic activity is a distinct taxable person from a VAT perspective¹. Moreover, all transactions between related businesses are subject to VAT². That may not be the case if one of the “*group arrangements*”, stipulated in the VAT Directive, is applicable³. Two of these “*group arrangements*” in the VAT Directive are the VAT grouping scheme of Article 11 and the so-called cost sharing exemption of Article 132(1)(f).

Article 11(1) of the VAT Directive provides that any persons established in the territory of a single Member State who, while are legally independent, are closely bound to one another by financial, economic and organisational links can be considered and treated as a single taxable person for VAT purposes. According to paragraph 2 of the abovementioned Article, a Member State exercising the option provided for in the first paragraph⁴, may adopt any measures needed to prevent tax evasion or avoidance through the use of this provision. Article 132(1)(f) of the VAT Directive exempts 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 to 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 not be likely to cause distortion of competition.

Legal scholars⁵, as well as the Commission⁶, mention the relationship and the interaction of the schemes that the two provisions employ. The Advocate General Kokott also provides for the relationship between the two articles regarding personal scope⁷ and their territorial scope⁸. Furthermore, the importance of the VAT grouping option in comparison with the cost-sharing exemption has increased in the light of the recent developments in case-law, regarding the exclusion of the latter in the financial

¹ Lang M. and Lejeune I., *Improving VAT/GST Designing a simple and Fraud-Proof Tax System*, (IBFD 2014), p. 485.

² Ibid. See also Article 2 of the VAT Directive.

³ Ibid.

⁴ VAT grouping regime is an optional provision for the Member States. According to the VAT Expert Group in VEG No 070 REV 1, 16 Member States have already implemented VAT grouping schemes, with Italy following from 2019 and Luxembourg expected to introduce a VAT grouping system soon.

⁵ Vyncke K., ‘Cost Sharing Associations as an Alternative to VAT Grouping in Belgium’; Zuidgeest R.N.F., ‘Cross-Border VAT Grouping’, 21(1) International VAT Monitor (2010), Journals IBFD, p. 26.

⁶ European Commission, Working Paper No 856 and European Commission Working Paper 883.

⁷ Opinion of Advocate General Kokott delivered on 1 March 2017, *Aviva*, C- 605/15, EU:C:2017:150 paras 41.

⁸ Opinion of Advocate General Kokott delivered on 1 March 2017, *DNB Banka*, C-326/15, EU:C:2017:145 paras. 46 to 49.

and insurance sectors⁹. *Aviva*¹⁰, *DNB Banka*¹¹, and *Commission v Germany*¹² signalled the end of the cost-sharing exemption, as implemented by the Member States until now¹³. In this context, the present thesis is developed.

1.2. Aim

This thesis has the purpose to research and compare the two abovementioned provisions, and their interpretation by the CJEU and the European Commission. The research question is formulated in the following way: What are the similarities, and the differences between VAT groups and cost-sharing groups? How do these two VAT concepts interact?

1.3. Method and Material

The legal-dogmatic method in combination with a comparative analysis of the two relevant provisions of the VAT Directive will be applied in order to answer the above-stated question¹⁴. A conceptual analysis of the provisions is conducted. The material used includes the provisions of the VAT Directive, which constitutes secondary EU law, introduced on the basis of Article 113 of TFEU. Other sources include case law from the CJEU and material of doctrinal value, such as Advocate Generals' opinions, case commentaries, European Commission's papers, journal articles, and books. The case law's main focus has been restricted to cases that explicitly refer to Articles 11 and 132(1)(f) of the VAT Directive. The research has been conducted until the 14 of May.

1.4. Delimitation

In the present thesis, the problematic situations regarding the territorial scope and the cross-border situations of both articles will not be discussed in detail. The aim is to present the basic elements, the fundamental aspects of both provisions in order to compare them and present their interaction. Furthermore, the analysis of both provisions is at the EU level, so aspects of the manner how the Member States implement them is not included in the present thesis.

1.5. Outline

In chapter 2, the fundamental aspects of VAT grouping will be presented. Accordingly, in chapter 3, the fundamental aspects of the cost-sharing exemption will be analysed. In chapter 4, the similarities and the differences between the two provisions will be exhibited. In chapter 5, the interaction of the two concepts will be examined. Chapter 6 has as its content final and conclusive remarks on the topic.

⁹ European Commission, VAT Expert Group, VEG No 075, Implications of the CJEU judgements on cost-sharing for the financial and insurance sectors, taxud.c.1(2018)1016383, Brussels, 16 February 2018, p. 2.

¹⁰ Judgement of 21 September 2017, *Aviva*, C-605/15, EU:C:2017:718.

¹¹ Judgement of 21 September 2017, *DNB Banka*, C-326/15, EU:C:2017:719.

¹² Judgement of 21 September 2017, *Commission v Germany*, C-616/15, EU:C:2017:721.

¹³ *Supra* n. 9.

¹⁴ Douma S., *Legal Research in International and EU Tax Law*, (Wolters Kluwer 2014) p. 17.

Chapter 2: Fundamental aspects of VAT grouping

2.1. Introduction

Article 11(1) of the VAT Directive provides Member States with the option of introducing VAT grouping schemes into their national legislation, after consulting the VAT Committee¹⁵. Two or more persons, established within a Member State who, while legally independent, are closely bound to one another by financial, economic and organisational links, may be treated as a single taxable person for VAT purposes¹⁶. The second paragraph of Article 11 of the VAT Directive permits Member States to adopt any measures needed to prevent tax evasion or avoidance, through the use of VAT grouping schemes. The scope of Article 11 can be divided into three main elements, the personal scope, the substantive scope and the territorial scope¹⁷.

The EU VAT grouping was introduced into the EU legislation in 1967¹⁸. Article 4 of the Second Directive¹⁹ stated that a taxpayer is *any person independently engaging in transactions pertaining to the activities of producers, traders or persons providing services, whether or not for gain*'. Paragraph 2 of the Annex A of the Second Directive²⁰ confirmed the term "independently" and provided that "*Member State(s) not to consider as separate taxable persons, but as one single taxable person, persons who, although independent from the legal point of view, are however, organically linked to one another by economic, financial or organisational relationships*". From the Explanatory Memorandum to the Second Directive²¹, it can be inferred that the EU VAT grouping originates from the German system of Organschaft²². In *Van Paasen*²³, the European Commission expressly acknowledged that the VAT grouping concept is based on the Organschaft concept²⁴.

In the Sixth Directive, VAT grouping was officially introduced²⁵. Art. 4(4) of the Sixth Directive provided that, subject to a consultation procedure, each Member State may

¹⁵ Article 398 of the VAT Directive. See Appendix Figure 1.

¹⁶ European Commission, Communication on the VAT Group option provided for in Article 11 of council Directive 2006/112/EC on the common system of VAT, COM(2009)325 final, p. 2.

¹⁷ Pfeiffer S., 'Written Comment to the keynote paper taxable persons' in Lang M., Pistone P., Schuch J., Staringer C. and Raponi D. (eds) ECJ- Recent Developments in Value Added Tax (Linde Verlag 2014), p. 96.

¹⁸ Pfeiffer S., *VAT Grouping from a European Perspective*, Vol. 34 (IBFD Doctoral Thesis 2015), pp. 11-20; See also Swinkels J.J.P., 'The Phenomenon of VAT Groups under EU Law and Their VAT-Saving Aspects', 2010 21(1) International VAT Monitor, IBFD Journals, p. 36-42.

¹⁹ Second Council Directive 67/228/EEC of 11 April 1967 on the harmonization of legislation of Member States concerning turnover taxes Structure and procedures for application of the common system of VAT.

²⁰ Ibid.

²¹ European Commission, Proposal for a Second Council Directive for the harmonisation among Member States of turnover tax legislation, concerning the form and the methods of application of the common system of taxation on value added, p. 20.

²² Swinkels J.J.P., 'The Phenomenon of VAT Groups under EU Law and Their VAT-Saving Aspects', 2010 21(1) International VAT Monitor, IBFD Journals, p. 37.

²³ Judgement of 12 June 1979, *Van Paasen and Denkvit Dienstbetoen*, Joined Cases C-181/78 and C-22/78, EU:C:1979:151

²⁴ Doesum Ad van and others, *The Fundamentals of EU VAT Law* (Kluwer 2016) p. 83; Supra n. 17 at p. 97.

²⁵ Supra n. 22, at p. 36.

treat, as a single taxable person, persons established in the territory of the country who, while legally independent, are closely bound to one another by financial, economic and organizational links. According to the Explanatory Memorandum²⁶, the aim of the provision on VAT grouping is now “to allow Member States, for the purposes of administrative simplification or combating abusive practices, e.g. when a business is split into several taxable persons so that each may benefit from a special scheme, to not regard as separate taxable persons those whose “independence is purely a legal technicality”²⁷.

Article 4(4) of the Sixth Directive was amended by the Council Directive 2006/69/EC and a second paragraph was added. Following the recast of the Sixth Directive, no changes occurred and now, Article 11 of the VAT Directive provides the VAT grouping provisions.

The main purpose of the VAT grouping notion is that closely-linked persons are merged into a new single taxable person for VAT purposes²⁸. That is confirmed in *Ampliscientifica*²⁹. In *Ampliscientifica*, the CJEU concluded that the treatment as a single taxable person precludes persons who are thus closely linked from continuing to submit VAT declarations separately and from continuing to be identified, within and outside their group, as individual taxable persons, since the single taxable person alone is authorised to submit such declarations³⁰. The use of a single VAT identification number is dictated by the need for legal certainty, both for the economic operators and the tax authorities of the Member States, to identify those effecting transactions subject to VAT³¹. Finally, the most important consequence of the formation of a VAT group for its members is that the transactions between the latter are considered as “out-of-the-scope” transactions and are not subject to VAT³².

The wording of Article 11 of the VAT Directive has led Member States to implement VAT grouping systems in their national legislation in different ways. The CJEU, as well as the VAT Committee, have provided some guidance on the elements consisting the scope of the latter provision. The VAT Committee performs a consulting role and its decisions and interpretations of the VAT Directive are not legally binding³³. Nevertheless, the former has expressed its legal opinion on basic aspects of VAT grouping notion.

²⁶ European Commission, Proposal for a Sixth Council Directive on the harmonisation of the laws of the Member States relating to turnover taxes- Common system of VAT: uniform basis of assessment, OJ L 145, 13.6.1977, p. 1.

²⁷ Supra n. 16, p. 3; Judgement 9 April 2013, *Commission v. Ireland*, C-85/11, EU:C:2013:217 para. 47.

²⁸ Supra n. 16, at pp. 4-5.

²⁹ Judgement of 22 May 2008, *Ampliscientifica and Amplifin*, C-162/07, EU:C:2008:301.

³⁰ Ibid para. 19.

³¹ Ibid para. 20.

³² Supra n. 16, at p. 10.

³³ Supra n. 24, at p. 19

2.2. The personal scope

Article 11 of the VAT Directive merely refers to “persons”. The personal scope of the VAT grouping includes the question of how to interpret the term “person”³⁴. Some elements of this scope have been subject of the CJEU case-law.

The first aspect of the personal scope that is examined is whether both taxable and non-taxable persons can be members of a VAT group. The Commission initially was of the opinion that only taxable persons can be members of a VAT group³⁵. For this reason, the Commission initiated a number of infringement procedures against several Member States, who included non-taxable persons as members of a VAT group in their national provisions for VAT grouping system³⁶. In these cases, the CJEU dealt with the question whether Article 11 of the VAT Directive precludes Member States that implement VAT grouping schemes in their national legislation from permitting non-taxable persons to join or form a VAT group. The Commission’s procedures were dismissed, and the CJEU judged that non-taxable persons are also eligible to join or form a VAT group.

More specifically, in *Commission v Ireland*, which is a landmark case³⁷, the Court, following Advocate General Jääskinen’s opinion³⁸, concluded that the Member states may include non-taxable persons in their national provisions for VAT grouping³⁹. The Court also pointed out that, if such a possibility gives rise to abuse, the second paragraph of Article 11 of the VAT Directive permits Member States to adopt any measures needed to prevent tax evasion or avoidance through the use of the first paragraph of Article 11⁴⁰.

First of all, the CJEU gave a broader interpretation to the term “person” in a comparison with the Commission’s view, based on the wording and the drafting history of the provision⁴¹. The provision refers to “persons” and not to “taxable persons”. From a literal interpretation of the latter, it cannot be concluded that the VAT Directive provides the VAT grouping scheme only to taxable persons⁴².

Secondly, the CJEU examined the context of the provision and concluded that it did not support the Commission’s claim⁴³. The Court held that Article 9(1) of the VAT Directive contains a general definition of the concept of a “taxable person”. Article

³⁴ Pfeiffer S., ‘Current questions of EU VAT grouping’, World Journal of VAT/GST Law, 4:1, p. 28.

³⁵ Supra n. 16, p. 5.

³⁶ Judgement 9 April 2013, *Commission v. Ireland*, C-85/11, EU:C:2013:217; CJEU, Judgement of 25 April 2013, *Commission v. United Kingdom*, C-86/11, EU:C:2013:267; CJEU, Judgement of 25 April 2013, *Commission v. the Netherlands*, C-65/11, EU:C:2013:265; CJEU, Judgement of 25 April 2013, *Commission v. Denmark*, C-95/11, EU:C:2013:268 and CJEU, Judgement of 25 April 2013, *Commission v. Czech Republic*, C-109/11, EU:C:2013:269.

³⁷ Henkow O., ‘Taxable Persons’ in Lang M., Pistone P., Schuch J., Staringer C. and Raponi D. (eds), *ECJ- Recent Developments in Value Added Tax 2014* (Linde Verlag 2013), p. 83.

³⁸ Opinion of Advocate General Jääskinen delivered on 27 November 2012, *Commission v Ireland*, C-85/11, EU:C:2012:753.

³⁹ Judgement 9 April 2013, *Commission v. Ireland*, C-85/11, EU:C:2013:217, paras. 41, 46 and 48.

⁴⁰ Ibid, para. 49.

⁴¹ Ibid paras. 36 to 41.

⁴² Ibid para. 41

⁴³ Ibid para. 46.

9(2) and Articles 10, 12, and 13 provide details in respect of that concept, either by including in it or by permitting Member States to include in it, persons who do not satisfy the general definition. Accordingly, it cannot be inferred from the scheme of Title III of the VAT Directive that a person who does not satisfy the general definition in Article 9(1) is necessarily excluded from being one of the persons referred to in Article 11 thereof⁴⁴.

The Court also stated that a comparison of Articles 9 and 11 does not contradict an interpretation according to which it is those persons, taken together and closely bound to one another by financial, economic and organisational links, who are required cumulatively to satisfy the links-criterion⁴⁵. Henkow mentions that Article 11 must be seen as supplementary to Article 9⁴⁶. A member of the VAT group can be a non-taxable person, as long as all the members of the VAT group together fulfil that criteria⁴⁷.

Thirdly, the Court moved to a teleological interpretation of the provision. On the basis of its legislative history, the latter held that the objectives for the VAT group facility were simplifying administration or combating abuses. Such an example of abuse is the splitting-up of one undertaking among several taxable persons. Each of the undertakings thus might benefit from a special scheme, to ensure that Member States would not be obliged to treat as taxable persons those whose their “*independence*” is purely a legal technicality⁴⁸. The CJEU considered that these objectives did not imply that non-taxable persons were excluded from VAT groups⁴⁹.

Following the same reasoning⁵⁰, the Court ruled in favour of the inclusion of the non-taxable persons in the national VAT grouping regimes in the abovementioned cases⁵¹. These rulings raised the question between the legal scholars whether a Member State is obliged to allow non-taxable persons to join a VAT group or it has the discretion to allow persons with such taxable status to join or form a VAT group⁵². In *Commission v Ireland*, as analysed above, the Court’s stated that, due to the wording, the context and the objectives of Article 11 of the VAT Directive, the rule is not to be interpreted as meaning that non-taxable persons cannot (and not must not) be included in a VAT group⁵³. Likewise, the German translation provides “*können*” (can, may) instead of “*müssen*” (must)⁵⁴. The CJEU gives the right to Member States to include non-taxable

⁴⁴ Ibid para. 44.

⁴⁵ Ibid para. 45.

⁴⁶ Supra n. 37, at p. 83.

⁴⁷ Ibid.

⁴⁸ Judgement 9 April 2013, *Commission v. Ireland*, C-85/11, EU:C:2013:217, para. 47.

⁴⁹ Ibid para. 48. See also supra n. 46.

⁵⁰ Ben Terra

⁵¹ Judgement of 25 April 2013, *Commission v. United Kingdom*, C-86/11, EU:C:2013:267; Judgement of 25 April 2013, *Commission v. the Netherlands*, C-65/11, EU:C:2013:265; Judgement of 25 April 2013, *Commission v. Denmark*, C-95/11, EU:C:2013:268 and Judgement of 25 April 2013, *Commission v. Czech Republic*, C-109/11, EU:C:2013:269

⁵² Supra n. 20 p. 29.

⁵³ Judgement 9 April 2013, *Commission v. Ireland*, C-85/11, EU:C:2013:217, paras. 41, 46 and 50.

⁵⁴ Pfeiffer S., ‘Written Comment to the keynote paper ‘Taxable persons’ in Lang M., Pistone P., Schuch J., Rust A., Staringer C. and Raponi D. (eds.), *ECJ- Recent Developments in Value Added Tax 2014* (Linde Verlag 2013), 90-105.

persons to form or join a VAT group, but it does not clarify whether there is an obligation for Member States to permit non-taxable persons to form or join a VAT group⁵⁵.

A second problematic issue regarding the personal scope of Article 11 was raised in *Skandia America*⁵⁶. The referring court asked, among other things, whether a fixed establishment can be a person for VAT grouping purposes. Skandia was a US corporation and had a fixed establishment in Sweden⁵⁷. Skandia acted as the central procurement company for IT services within the Skandia group and provided these services to companies within the group as well as to branches, including the Swedish branch⁵⁸. The Swedish branch had to process the IT services to a final product and provide it both to the Swedish VAT group members and to companies outside the VAT group⁵⁹. These services were charged with a 5% mark-up to the costs⁶⁰.

The Advocate General analysed at length⁶¹ whether a fixed establishment can be a person separate from its head office for VAT grouping purposes. Eventually, he was of the opinion that a fixed establishment cannot be a person of its own, but the head office and the fixed establishment constitute together a person, even if its head office is located in a different state⁶². However, the Court simply referred to the fact that it is common ground that the Swedish branch is part of the Swedish VAT group and forms with the other members of the group a single taxable person⁶³. Therefore, the question whether or not the branch carries out an independent economic activity by bearing economic risk from its business remained unanswered⁶⁴. By being part of the Swedish VAT group, the branch ceased to be part of the head office, established in a third state and subsequently, the supplies of services from the head office to the branch constituted taxable supplies for VAT purposes as they were carried out between two taxable persons⁶⁵.

The third topic in connection to the personal scope of Article 11 of the VAT Directive revolves around the question whether VAT grouping can be restricted to certain legal forms. From the perspective of the principle of neutrality, the CJEU case-law tends to the conclusion that it should be irrelevant for the application of exemptions which legal form an operator chooses⁶⁶.

⁵⁵ Ibid p. 100.

⁵⁶ Judgement of 17 September 2014, *Skandia America Corp. v Skatteverket*, C-7/13, EU:C:2014:2225.

⁵⁷ Ibid para. 17.

⁵⁸ Ibid.

⁵⁹ Ibid.

⁶⁰ Ibid.

⁶¹ Opinion of Advocate General Wathelet delivered on 8 May 2014, *Skandia America Corp. v Skatteverket*, C-7/13, EU:C:2014:311, paras. 39 to 61.

⁶² Ibid para. 60.

⁶³ Judgement of 17 September 2014, *Skandia America Corp. v Skatteverket*, C-7/13, EU:C:2014:2225 para. 28. (footnote 37)

⁶⁴ Supra n. 20 p. 30.

⁶⁵ Judgement of 17 September 2014, *Skandia America Corp. v Skatteverket*, C-7/13, EU:C:2014:2225 paras. 30 and 31.

⁶⁶ See for example, Judgement of 10 September 2002, *Kügler*, C-141/00, EU:C:2002:473 and Judgement of 10 November 2011, *The Rank Group plc*, Joined Cases 259/10 and 260/10, EU:C:2011:719.

Based on the judgement in *Heerma*⁶⁷, the legal form of persons forming a VAT group is irrelevant. In particular, in *Heerma* the referring national court asked the CJEU whether Mr Heerma could be regarded as a taxable person, when independently from the partnership he formed with his wife, performing economic activities⁶⁸. The Court concluded that since there was no relationship of employer and employee. The partner acted independently of the partnership. Therefore, he could be treated as a single taxable person together with the partnership, but, since the Court did not argue that, there was no need to consider that provision⁶⁹.

In *Larentia+Minerva and Marenave*⁷⁰, the Court, inter alia, dealt with the question whether and when a Member State can exclude certain legal entities and, specifically a limited partnership without legal personality, from being part of a VAT group⁷¹. The CJEU held that national legislation, which reserves the right to form a VAT group solely to entities with legal personality and linked to a controlling company of that group in a relationship of subordination, is incompatible with the VAT Directive⁷². Such a limitation is acceptable in the case that it is necessary and appropriate to prevent abusive practices. Should such a limitation be necessary and appropriate, it is for the referring court to determine⁷³. The Court also ruled that Article 11 not satisfy the conditions necessary to be directly applicable⁷⁴. Subsequently, it is for the Member State to define the actual scope of the links required between the members of a VAT group⁷⁵. One may argue that the Court makes it clear in *Larentia* that the VAT grouping arrangements in Article 11 are conditional in so far as they involve the application of national provisions, determining the scope of the close, financial, economic and organisational links between the persons and have to be specified at national and not at EU level⁷⁶.

Finally, in *Nigl*⁷⁷, three different partnerships asked if they can be considered as a single taxable person. Despite the fact that this case is irrelevant, at first glance, with a VAT grouping scheme, the possible VAT grouping implications in a case such as this where civil partnership cooperate in the light of national provisions could be further discussed

⁶⁷ Judgement of 27 January 2000, *Heerma*, C-23/98, EU:C:2000:46

⁶⁸ Terra B.J.M. and Kajus J., *Introduction to European VAT (Recast), Commentaries on European VAT Directives*, (2018, IBFD Publications), pp. 195-196.

⁶⁹ Ibid.

⁷⁰ Judgement of 16 July 2015, *Larentia and Minerva and Marenave*, Joined Cases C-108/14 and 109/14, EU:C:2015:496.

⁷¹ Ibid para. 34.

⁷² Ibid para. 46.

⁷³ Ibid paras. 41, 43 and 46.

⁷⁴ Ibid para. 47 to 52.

⁷⁵ Ibid para. 50.

⁷⁶ Bomer A.H., 'From Skandia to Larentia: National Jurisdiction to deviate from the VAT Directive', Vol 44 Issue 8 and 9, *Intertax* p. 657-665.

⁷⁷ Judgement of 12 October 2016, *Nigl and Others*, C-340/15, EU:C:2016:764.

in a theoretical level. Nonetheless, in a case like this, the substantive scope of Article 11 of the VAT Directive cannot be applied, so a VAT group cannot be formed⁷⁸.

2.3. The substantive scope of VAT grouping

In order to form a VAT group, financial, economic and organisational links need to be established between the members of the VAT group. The substantive scope of Article 11 of the VAT Directive appears to be the least clear regarding the scope of Article 11 of the VAT Directive. An initial remark, expressed by the Commission⁷⁹, is that the three links have to be examined separately, but need to be met cumulatively during the entire time the VAT group operates. Several judgements have been issued on the topic of VAT grouping by the CJEU, but none of them concerns the “links test” directly.

In *Larentia and Minerva and Marenave*⁸⁰, the CJEU held that “*the fact that the nature of the relationship binding those persons are merely one of ‘closeness’ may, in the absence of any other requirement, not therefore lead to the conclusion that the EU legislature intended to reserve the benefit of the VAT group scheme only to entities in a relationship of subordination with the controlling company of the group of undertakings considered*”⁸¹. The Court, in accordance with Advocate General Mengozzi’s opinion⁸², held that a relationship of control and subordination may prove the element of closeness between the two persons but it is not a condition necessary for the constitution of a VAT group⁸³.

Due to the absence of CJEU’s case law on the substantive scope, the only source of an EU-wide interpretation of 3-links criterion is given by the European Commission. Initially, in the Communication⁸⁴, the Commission held that all the link criteria have to be met cumulatively in order for the substantive scope to be fulfilled. Moreover, the existence of one link does not necessarily lead to the fulfilment of the others. More specifically, firstly, the financial link is defined by reference to a participation in the capital or in voting rights (over 50%), or by reference to a franchise contract. Both direct and indirect (through subsidiaries) participations lead to a financial link⁸⁵. Secondly, the economic link is defined by reference to the existence of at least one of the following three situations of economic cooperation: (a) the principal activity of the group members is of the same nature, or (b) the activities of the group members are complementary or independent, or (c) one member of the group carries out activities

⁷⁸ See Pfeiffer S., ‘VAT Grouping- Consequences of Nigl and Follow-up on Skandia America’, in Lang M., Pistone P., Schuch J., Rust A., Staringer C. and Raponi D. (eds.), *CJEU- Recent Developments in Value Added Tax* 2016, (Linde Verlag 2017), 145, where the facts and the ruling are analysed in detail. S., p. 145.

⁷⁹ European Commission, Communication on the VAT Group option provided for in Article 11 of Council Directive 2006/112/EC on the common system of VAT, COM(2009)325 final, p. 8.

⁸⁰ Judgement of 16 July 2015, *Larentia and Minerva and Marenave*, Joined Cases C-108/14 and 109/14, EU:C:2015:496.

⁸¹ Ibid para. 44.

⁸² Opinion of Advocate General Mengozzi delivered on 26 March 2015, *Larentia and Minerva and Marenave*, Joined Cases C- 108/14 and C- 109/14 ,EU:C:2015:212, para. 99.

⁸³ Supra n. 61 para. 45.

⁸⁴ Supra n. 60 p. 9.

⁸⁵ Ibid.

which are wholly or substantially to the benefit of the other members⁸⁶. Thirdly, the organisational link is defined by reference to the existence of a shared, or partially shared, management structure⁸⁷.

The Commission has also dealt with this issue, specifically in Working Papers 918⁸⁸ and 944⁸⁹. In Working Paper 918, the VAT Committee reiterated that the threefold links-requirement must be met cumulatively and be examined separately. The assessment of the links must be conducted based on the economic substance. The VAT Committee dealt with the issue of providing a minimum on the conditions for determining the existence of a financial link between VAT group members. Furthermore, the Commission services sought to establish a minimum content of the financial link and possible presumptions to assess such a link. Moreover, the Commission endeavoured to crystallise the meaning of the economic and the organisational links. Finally, the VAT Committee referred to *Larentia+Minerva* to illustrate that a relationship of control and subordination between the VAT group members is an indication for the links criterion to be present but it is not the determining factor. Finally, the Commission observed that the CJEU has never dealt with the economic or the organisational link.

In the most recent paper of the VAT Expert Group⁹⁰, the legal practitioners are in favour of the application of a holistic approach based on economic reality and applied on the basis of the three criteria referred to in Article 11. All links need to exist as a whole, cumulatively. However, it is not required that all links be fulfilled to the same degree to both the situations where VAT grouping is optional for economic operators and where it is mandatory for businesses according to the national legislation⁹¹. In order to guarantee legal certainty for taxpayers and tax administrations, a confirmation process is suggested by the VAT Expert Group. This confirmation test functions affirming both the way that a VAT group can be formed and who can be a member of it, as well as the way of applying the 3-links test in a holistic manner. Moreover, the VAT Expert Group highlighted that further guidance is needed on the meaning of the three-links test in order to facilitate uniform implementation and application of Article 11 across the EU, including the abovementioned proposed confirmation test.

⁸⁶ Ibid.

⁸⁷ Ibid.

⁸⁸ VAT Committee, Working Paper No. 918, 'Meaning of "financial, economic and organisational links" among VAT group members', taxud.c.1(2017)982178, Brussels, 16 February 2017.

⁸⁹ VAT Committee, Working Paper No. 944, 'Meaning of "financial, economic and organisational links" among VAT group members- the point of view of VAT Expert Group', taxud.c.1(2018)1694334, Brussels, 20 March 2018.

⁹⁰ VAT Expert Group, VEG No 070 REV1, 'Paper on the topic for discussion "Meaning of "financial, economic and organisational links" among VAT group members', taxud.c.1(2018)1668166, Brussels, 19 March 2018. The Working Paper 944 of the VAT Committee refers to this document and more specifically it is included in it as Annex.

⁹¹ Pfeiffer S., *VAT Grouping from an EU Perspective*, (IBFD Doctoral Series Volume 34), pp. 163-171.

2.4. The territorial scope of VAT grouping

The wording of Article 11 of the VAT Directive provides that the territorial scope of a VAT grouping scheme implemented by a Member State be restricted to persons “established in the territory of that Member State”⁹². Although, there is no existing guidance as to the meaning of the notion “a person established in the territory of that Member State”, the Commission dealt with the interpretation of this notion in its Communication⁹³.

The Commission is of the opinion that the notion includes businesses with their seat of economic activity or fixed establishments of such businesses or of foreign businesses, physically present in the territory of the Member State implementing the VAT grouping scheme. Fixed establishments of businesses that are situated abroad may not join a VAT group. The main justification for such an interpretation is the optional character of VAT grouping schemes. The VAT grouping scheme implemented by a Member State should not have the effect of extending beyond the physical territory of that Member State. In this way, the fiscal sovereignty of another Member State may be violated⁹⁴.

Moreover, if two Member States were to choose to introduce VAT grouping schemes, it is possible that the fixed establishments situated abroad could form part of a VAT group in both Member States. Such a result is incompatible with the basic principles of the common VAT system, as well as uncontrollable for the national administrations. Moreover, the Commission takes the view that such an interpretation that includes fixed establishments of foreign businesses located in the Member State implementing the VAT grouping scheme complies with the fundamental freedoms⁹⁵.

The Commission opined that this interpretation is in line with the findings in *FCE Bank*⁹⁶. *FCE Bank* is the judgement that the CJEU dealt with the concept of out-of-scope intra-branch transactions within the European Union⁹⁷. The Court found that a branch which does not bear the economic risk arising from its business⁹⁸ is not a separate taxable person from its head office. Due to the absence of a legal relationship in which there is a reciprocal performance, supplies of services between a head office and its branch located abroad are out of the scope⁹⁹. The Commission opined that *FCE Bank* makes no reference to makes no reference whatsoever to the situation of a VAT group. Furthermore, it should be noted that, by joining a VAT group, the taxable person becomes part of a new taxable person, the VAT group and, consequently, dissolves

⁹² See a detailed analysis in Pfeiffer S., *VAT Grouping from an EU Perspective*, (IBFD Doctoral Series Volume 34), pp. 63-121.

⁹³ Supra n. 60 p. 6 and 7.

⁹⁴ Terra B.J.M. and Kajus J., Introduction to European VAT (Recast), Commentaries on European VAT Directives, (2018, IBFD Publications) p. 199-200.

⁹⁵ Ibid p. 199.

⁹⁶ Judgement of 23 March 2006, *FCE Bank*, C-210/04, EU:C:2006:196.

⁹⁷ Pfeiffer S., ‘Taxable Persons: VAT Grouping and Fixed Establishments’ in Lang M., Pistone P., Schuch J., Rust A., Staringer C. and Raponi D., *ECJ- Recent developments in Value Added Tax 2014*, (Linde Verlag 2014), 68-84.

⁹⁸ Supra n. 75 para. 35.

⁹⁹ Supra paras. 34 and 37.

itself for VAT purposes from its fixed establishment located abroad. This means that if a taxable person joins a VAT group, any services it subsequently supplies to its fixed establishment abroad would be considered as supplies made between two separate taxable persons. The fact that the fixed establishment situated abroad is excluded from being eligible for a VAT group in that Member State is therefore not at variance with the FCE Bank ruling¹⁰⁰.

In the abovementioned *Skandia America*, reference the Court dealt with the issue of cross-border situations regarding VAT grouping schemes. The referring court asked CJEU whether the supplies from the head office, established in the USA and its fixed establishment in Sweden which is a member of a Swedish VAT group are taxable supplies or not. The CJEU decided in line with the Commission's opinion in the Communication¹⁰¹. After *Skandia America*, it is clear that the FCE Bank criteria cannot be applied between a head office and a branch where the branch is part of a VAT group situated in another Member State.

The VAT Committee issued guidelines regarding the territorial scope of VAT groups, following *Skandia* judgement which affirmed the CJEU's findings¹⁰². The VAT Committee, inter alia, stated that "*the treatment of a VAT group as a single taxable person precludes the members of a VAT group from continuing to operate, within and outside their group, as individual taxable persons for VAT purposes*". This issue of the so-called "external effects" of VAT grouping has concerned many academics, and the Committee's view is that a Member State, even if it has not exercised its option to implement Article 11 of the VAT Directive in its national legislation, is obliged to acknowledge a foreign VAT group. It seems that VAT grouping may have consequences for Member States that have not introduced VAT grouping¹⁰³.

2.5. Anti-avoidance measures

The second paragraph of Article 11 of the VAT Directive allows Member States to adopt any measures needed to prevent tax evasion or avoidance. This paragraph is quite unclear and does not specify or clarify the conditions under which Member States can take measures.

The infringement procedures against Sweden¹⁰⁴ and Finland¹⁰⁵ dealt with the question whether or not Member States retain their right to limit VAT grouping by introducing further criteria in their VAT grouping domestic legislation. More specifically, this restriction constituted on the fact that VAT groups –according to the Commission's allegations- were restricted to the financial and insurance sectors. The Commission took

¹⁰⁰ Doesum van A. and others, *Fundamentals of EU VAT Law* (Kluwer 2016), p. 90.

¹⁰¹ Judgement of 17 September 2014, *Skandia America Corp. v Skatteverket*, C-7/13, EU:C:2014:2225, paras. 29 and 30.

¹⁰² Guidelines resulting from the 105th meeting of 26 October 2015, Document A-taxud c.1(2016)7465801- 886 p. 205.

¹⁰³ See to that effect Lang M. and others, *CJEU- Recent Developments in Value Added Tax 2016*, (Linde Verlag 2017), p. 151-153.

¹⁰⁴ Judgement 25 April 2013, *Commission v. Sweden* C-480/10, EU:C:2013:263.

¹⁰⁵ Judgement of 25 April 2013, *Commission v. Finland*, C-74/11, EU:C:2013:266.

the view that such an implementation of VAT grouping scheme was against the objectives of the VAT Directive and the fundamental freedoms. Against AG's opinion, who proposed that the Court should declare that, by limiting the scope of VAT grouping to the financial and insurance sectors, Sweden had failed to fulfil its obligations under Article 11 of the VAT Directive, the Court decided that in the light of the wording, the context and the objectives pursued such an implementation of the VAT grouping scheme is not against the VAT Directive.

Specifically, the CJEU recognised that it was especially important for the uniform application of the VAT Directive that the notion of 'taxable person' be given an autonomous and uniform interpretation. Article 11 of the VAT Directive forms part of that concept and thus needed a uniform interpretation¹⁰⁶. The Court notes that the conditions outlined in the provision are exhaustive. The provision does not provide that the Member States are entitled to impose other conditions on economic operators in order to form a VAT group, such as carrying out a certain type of activity or being part of a particular sector of activity¹⁰⁷. The Court nevertheless dismissed the Commission's action. It did so on the basis that Sweden claimed it had made use of article 11(2) and enacted measures to prevent evasion and avoidance. Sweden claimed that it had restricted the possibility of forming a VAT group to those undertakings which are placed, directly or indirectly under the supervision of the Finance Inspectorate and which therefore were covered by a public monitoring system. The court found that the Commission had failed to show convincingly that, in the light of the need to combat tax evasion and avoidance, this measure was not well founded¹⁰⁸. This judgement could create fiscal neutrality issues, since companies in a similar situation, either subject to a public monitoring system, or having the right to pay and receive group contributions for the purposes of the income tax act, may have a strong case filing for registration as a group following the application of the principle of neutrality. If a trader finds himself in a comparable situation, he may rely on the principle of neutrality and claim the same treatment¹⁰⁹. In *Commission v Sweden*, Advocate General Jääskinen found that the Swedish regime did not comply with Article 11. In a footnote referred to the matter whether the limitation to a specific sector of the economy, present in the Swedish VAT Act, could constitute illegal State Aid¹¹⁰.

According to Henkow¹¹¹, the Member States' discretion rests rather on the application of the second paragraph of Article 11, which gives them the authority to enact measures needed to prevent evasion or avoidance. Finally, the Court dealt with Article 11(2) of

¹⁰⁶ Supra n. 82 para. 34.

¹⁰⁷ Ibid para. 35.

¹⁰⁸ Ibid para. 39.

¹⁰⁹ Henkow O., 'Taxable Persons' in Lang M., Pistone P., Schuch J., Rust A., Staringer C, and others, ECJ- Recent Developments in Value Added Tax, (Linde Verlag, 2015), p. 85.

¹¹⁰ Ibid.

¹¹¹ Ibid.

the VAT Directive, since it is argued that that restrictions to Article 11 of the VAT directive may only be used to counter tax evasion and avoidance¹¹².

Chapter 3: Fundamental Aspects of the Cost-Sharing exemption

3.1. Introduction

Article 132(f) of the VAT Directive allows an exemption from VAT for cost-sharing arrangements, providing that *"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."*¹¹³

The cost-sharing exemption first appeared in the Proposal for the Sixth Directive¹¹⁴. The exemption was proposed to be limited to services supplied by independent groups of persons to members carrying on medical or paramedical activities, but, finally, Article 13(A)(1)(f) of the Sixth Directive had a broader scope, not restricted to independent professional groups in the medical sector. The wording of article 13(A)(1)(f) was then transposed in the current Article 132(1)(f) of the VAT Directive.

The ratio legis of this provision is to limit the distortive effects of the VAT exemptions without the right of deduction. In fact, its rationale is *"to create an exemption from VAT in order to avoid an entity offering certain services from being required to pay that tax when it has found it necessary to cooperate with other entities by means of a common structure set up to undertake activities essential to the provision of those services"*^{115,116}. Hence, its goal is to prevent VAT from becoming a distortive factor when a group of persons finds it necessary to cooperate. Moreover, it ensures that the objectives of certain other exemptions are met (e.g. reducing the cost of medical care)¹¹⁷. This enables them to remain competitive with big multinational enterprises providing the same type of services, which profit from economies of scale¹¹⁸. From a VAT perspective, the services supplied under the exemption for cost-sharing arrangements are treated the same way as in-house services provided within the same

¹¹² Judgement of 16 July 2015, *Larentia+Minerva and Marenave*, Joined Cases C-108/14 and 109/14, EU:C:2015:496 paras. 63 and 76.

¹¹³ See Appendix Figure 2.

¹¹⁴ Explanatory Memorandum to the proposal for a Sixth Directive of 20 June 1973, COM 73(950).

¹¹⁵ Doesum van A. and others, *Fundamentals of EU VAT Law* (Wolters Kluwer 2016) p. 272.

¹¹⁶ Judgement of 11 June 1989, *Stichting Centraal Begeleidingsorgaan voor de Intercollegiale Toetsing v Staatssecretaris van Financiën*, C-407/07, EU:C:2008:713, para. 37.

¹¹⁷ Doesum van A. and others, *Fundamentals of EU VAT Law* (Wolters Kluwer 2016) p. 273.

¹¹⁸ Opinion of Advocate General Mischo delivered on 3 October 2002, *Assurandør-Societetet acting on behalf of Taksatorringen v Skatteministeriet*, EU:C:2002:562 para. 115.

company¹¹⁹. The members of cost-sharing groups are able to achieve economies of scale ensuring a level playing field with larger competitors who have the capacity to perform the same activities internally¹²⁰.

The manner in which this provision is applied varies from Member State to Member State. In some cases, it had not even been transposed into national law until recently, even though it is a mandatory provision allowing Member States no choice in the matter¹²¹. This in itself shows the need for harmonisation in the application of Community law.

In order to interpret the five conditions that need to be met to apply the cost-sharing exemption, the settled case-law, Advocate Generals' opinions, certain academics' views and the European Commission's opinion¹²², will be used as interpretation aid.

3.2. First condition: Independent group of persons

The first of the five conditions relates to the personal scope of Article 132(1)(f) of the VAT Directive. Although the wording is clear, there is no further guidance about the status of the cost-sharing group, as well as of its members, from a legal perspective or for VAT purposes. The settled case-law, Advocate General Kokott's opinion in *DNB Banka* and the Commission's Working Papers, although no Guidelines are yet published by the Commission, provide concrete conclusions regarding the personal scope of the cost-sharing exemption.

The first case dealing with the cost-sharing exemption was *SUFA*¹²³. A foundation called "SUFA" organized and held lotteries for the foundation called "ALN" on behalf of social and cultural organisations affiliated to ALN. ALN was considered a cost-sharing group and the services rendered by it to its members were exempted from VAT. However, ALN reimbursed the costs incurred by SUFA. SUFA did not account for VAT on the amounts it received from ALN. The Dutch authorities charged VAT on the supplies, and SUFA appealed, arguing that they should be treated as exempt under the cost-sharing exemption. The question thus raised by the national court was whether the services supplied by SUFA to ALN could also be seen as provided by a cost-sharing group and thus exempted¹²⁴. The CJEU concluded that it was not possible to exempt the services provided by SUFA to ALN, on the grounds that neither foundation was a

¹¹⁹ VAT Committee, Working Paper No. 856, 'Scope of the exemption for cost-sharing arrangements: a further analysis', taxud.c.1(2015)2162037, Brussels, 6 May 2015, p. 3.

¹²⁰ Opinion of Advocate General Mischo delivered on 3 October 2002, *Assurandør-Societetet acting on behalf of Taksatorringen v Skatteministeriet*, EU:C:2002:562 paras. 118-119.

¹²¹ Terra B.J.M. and Kajus J., *Introduction to European VAT (Recast) Commentaries on European VAT Directives* IBFD 2018, p. 443.

¹²² The European Commission has discussed the issue in four different meetings, and as a consequence issued four Working Papers, namely Working Papers 450, 654, 856 and 883. The VAT committee has not agreed yet in any guidelines.

¹²³ Judgement of 15 June 1989, *Stichting Uitvoering Financiële Acties v Staatssecretaris van Financiën*, C-348/87, EU:C:1989:246.

¹²⁴ Terra B.J.M. and Kajus J., *Introduction to European VAT (Recast) Commentaries on European VAT Directives* IBFD 2018, p. 443.

member of the other and this is a requirement in order the cost-sharing exemption to be applicable¹²⁵. From this case, it can be submitted that the use of the term “members” in plural in the judgement suggest that at least three bodies must be involved in the cost-sharing arrangements, two members and the cost-sharing group, which provides services to its members¹²⁶. What is of more important and it is implied in *SUFA*, is the fact that, pursuant to the principle of fiscal neutrality¹²⁷, the legal form of the cost-sharing group is irrelevant for the application of the exemption. This is also confirmed in *Taksatorringen*¹²⁸ and *Stichting Centraal Begeleidingsorgaan voor de Intercollegiale Toetsing v. Staatssecretaris van Financiën*¹²⁹, where the persons related to the cases were a foundation and an association respectively.

One of the questions referred to the CJEU in *DNB Banka*¹³⁰ was whether the independent group of persons can be a separate entity or just a group of related undertakings¹³¹. The Court did not answer this question, but Advocate General Kokott provided with some guidance on this issue. In her Opinion, Advocate General Kokott first considered that the cost-sharing exemption is applicable to the supply of services by the “independent group of persons” to its members. This implies that the “independent group of persons” acts as “a taxable person acting as such”¹³². Otherwise, no VAT due would occur¹³³. Then, she dealt with the term “independent”, which, according to her view and based on a literal interpretation of the provision, means that the group is a separate entity from its members, a distinct entity for VAT purposes¹³⁴. She also dealt with the fact whether the group is not necessary to have legal personality to be a taxable person¹³⁵. However, according to the settled case-law that she refers to, a group of several independent companies, based solely on shareholdings among them, does not act as a taxable person and cannot qualify as an independent group of persons that can apply the exemption¹³⁶.

What can be concluded by the abovementioned judgements¹³⁷ is that the legal form of the cost-sharing group is irrelevant for the application of the cost-sharing exemption..

¹²⁵ Judgement of 15 June 1989, *Stichting Uitvoering Financiële Acties v Staatssecretaris van Financiën*, C-348/87, EU:C:1989:246, para. 14.

¹²⁶ Pfeiffer S., ‘Written Comments to the keynote paper taxable persons’ in Lang M., Pistone P., Schuch J., Rust A., Staringer C. and Raponi D., *ECJ- Recent developments in Value Added Tax*, (Linde Verlag 2014),

¹²⁷ Doesum van A. and others, *Fundamentals of EU VAT Law* (Kluwer 2016), p. 273.

¹²⁸ The facts of the case will be analysed in Section 3.5.

¹²⁹ The facts of the case will be analysed in the following page.

¹³⁰ The facts of the case will be analysed in Section 3.2.

¹³¹ Opinion of Advocate General Kokott delivered on 1 March 2017, *DNB Banka AS*, C-326/15, EU:C:2017:145, para. 32.

¹³² Ibid, para. 33.

¹³³ Ibid para. 35.

¹³⁴ Ibid para. 34.

¹³⁵ Ibid para. 38.

¹³⁶ Ibid para. 40 and case-law cited there.

¹³⁷ Judgement of 15 June 1989, *Stichting Uitvoering Financiële Acties v Staatssecretaris van Financiën*, C-348/87, EU:C:1989:246; Judgement of 20 November 2003, *Assurandør-Societetet acting on behalf of Taksatorringen v Skatteministeriet*, C-8/01, EU:C:2003:621 Judgement of 11 December 2008, *Stichting Centraal Begeleidingsorgaan voor de Intercollegiale Toetsing v Staatssecretaris van Financiën*, C-407/07, EU:C:2008:713; and

According to this, the Commission highlighted that “*what is ultimately relevant is the economic unit that the cost-sharing constitutes, rather than its specific legal form*”¹³⁸. Furthermore, from the VAT perspective, the cost-sharing group must be qualified as a taxable person, in order the exemption to be applicable. The latter is implied from the wording of the provision, since the exemption would not apply, if such a supply of services were not taxable, according to Article 2 of the VAT Directive. In regard to the taxable status of the cost-sharing group, the Commission added that a parent company can act as a cost-sharing group and the opposite, a subsidiary can act as a cost-sharing group for its parent company¹³⁹. What is inapplicable is the head office to act as a cost-sharing for its branch, because they are considered as one taxable person¹⁴⁰.

Regarding the legal, as well as the taxable status of the members of the cost-sharing group, Article 132(1)(f) of the VAT Directive does not provide with any specific directions. Adhering to the legal status of the cost-sharing group, its members can be legal or natural persons. For VAT purposes, a literal interpretation of the relevant provision implies the possible inclusion of both taxable and non-taxable persons, since the provision specifically refers to “either an activity exempt from VAT or in relation to which they are not taxable persons”. This approach stems from the position of CJEU regarding the status of persons composing a VAT group, which include both taxable and non-taxable persons. The Commission is of the view that even volunteers may be allowed to join the group, as far as they meet the other conditions¹⁴¹. A Member State can only preclude non-taxable persons from being part of a cost-sharing group, according to Article 131 of the VAT Directive¹⁴², because of tax evasion, tax avoidance or abuse reasons¹⁴³.

Finally, another aspect of the personal scope of the cost-sharing exemption is that the cost-sharing group provides services to its members. Firstly, in *SUFA*, the CJEU held that when an independent group of persons outsources activities to a third party, that third party cannot apply the exemption. In *Stichting Centraal Begeleidingsorgaan voor de Intercollegiale Toetsing*, the CJEU moved forward dealing with the question whether the cost-sharing exemption applies when the cost-sharing association provides its services only to one or several of its members¹⁴⁴. The *Stichting Centraal Begeleidingsorgaan voor de Intercollegiale Toetsing* was an umbrella organization for a number of hospitals and other establishments in the health sector¹⁴⁵, and supplied, for

Opinion of Advocate General Kokott delivered on 1 March 2017, *DNB Banka AS*, C-326/15, EU:C:2017:145

¹³⁸ VAT Committee, Working Paper No.856 p. 5.

¹³⁹ VAT Committee, Working Paper No 856 p. 7.

¹⁴⁰ VAT Committee, Working Paper No 856 p. 7-8.

¹⁴¹ VAT Committee, Working Paper No.883 p. 5-6.

¹⁴² According to Article 131 of the VAT Directive: “*The exemptions provided for in Chapters 2 to 9 shall apply without prejudice to other Community provisions and in accordance with conditions which the Member States shall lay down for the purposes of ensuring the correct and straightforward application of those exemptions and of preventing any possible evasion, avoidance or abuse.*”

¹⁴³ VAT Committee, Working Paper No. 883 p. 6.

¹⁴⁴ Judgement of 11 June 1989, *Stichting Centraal Begeleidingsorgaan voor de Intercollegiale Toetsing v Staatssecretaris van Financiën*, C-407/07, EU:C:2008:713, para. 14.

¹⁴⁵ *Ibid* para. 5.

consideration, services relating to quality standards in the healthcare sector to its members and to defining and promoting a policy of quality in that sector¹⁴⁶. The CJEU concluded that, when a cost-sharing group is formed by many members whose needs differ, it is possible that the services supplied to them by the group may differ or even these services can be supplied only to one or several of those members¹⁴⁷.

3.3. Second condition: Exempt or non-taxable activities of the members

Article 132(1)(f) of the VAT Directive provides that the cost-sharing exemption applies exclusively when the services rendered by the cost-sharing group to its members for their exempt activities or those for which are considered non-taxable persons. Although this condition seems to be unquestionable, there some aspects of it that need to be further explained.

To begin with, the VAT Directive does not set a limit, as regards the extent to which the members are allowed to perform taxable activities. The last-mentioned came to the surface in *Commission v Luxembourg*¹⁴⁸. In Luxembourg, services to members are exempt from VAT under the cost-sharing exemption, providing that their taxable activities do not exceed 30% or in under certain circumstances 45% of their annual turnover¹⁴⁹. The Commission challenged the Luxembourg rule, establishing a threshold for taxed operations and started an infringement procedure against the latter. The Court agreed with Advocate General's opinion and decided that the Commission's action was well founded¹⁵⁰. Since the wording of the provision does not preclude the application of the exemption when the members carried out taxed activities, a threshold for members' taxed activities could be a solution and enhance legal certainty for businesses and tax authorities¹⁵¹.

In addition, in *Aviva*, *DNB Banka* and *Commission v Germany*, the CJEU dealt with an important facet of the cost-sharing exemption and the condition of the members' "exempt or non-taxable downstream activities". In *Aviva*, the Polish Supreme Administrative Court enquired about the possible use of the exemption by a Polish group company of the Aviva Group. Aviva provided insurance services in Europe¹⁵². It was considering setting up a series of shared-service centres in selected Member States of the European Union and pursuing that activity in the form of a European economic interest grouping (EEIG)¹⁵³. The centres would supply services that are directly necessary for the exercise of insurance activities by members of the group (EEIG) such as HR services, financial and accounting services, IT services, administrative services,

¹⁴⁶ Ibid para. 8.

¹⁴⁷ Ibid. para. 8.

¹⁴⁸ Judgement of 4 May 2017, *Commission v Luxembourg*, C-274/15, EU:C:2017:333.

¹⁴⁹ Ibid para. 45.

¹⁵⁰ Ibid paras. 53 to 55.

¹⁵¹ Jovanovic N. and Merckx M.M.W.D., *The Cost Sharing Exemption Under Debate- Part I*, (2016) 27(5) International VAT Monitor 2016 p. 328.

¹⁵² Judgement of 21 September 2017, *Aviva*, C-605/15, EU:C:2017:718, para. 9.

¹⁵³ Ibid paras. 10 and 11.

customer service facilities or new product development services¹⁵⁴. Aviva asked the Polish tax authorities to confirm that the activities of the EEIG would be exempt under the cost sharing exemption¹⁵⁵. This confirmation was withheld and legal proceedings followed. In this case, the referring court requested clarification regarding the requirement of absence of distortion of competition and whether a cross-border situation could lead to different conclusions¹⁵⁶. The CJEU did not examine the national court's questions but, in line with Advocate General Kokott's opinion, decided that the cost-sharing exemption was not applicable in this case in the light of the context¹⁵⁷ and the objectives¹⁵⁸ of Article 132(1)(f) of the VAT Directive. The CJEU concluded that the supply of services which do not contribute directly to the exercise of activities in the public interest referred to in Article 132 of the VAT Directive, but to the exercise of other exempt activities, in particular those referred to in Article 135 of the VAT Directive, cannot fall within the scope of the cost-sharing exemption¹⁵⁹.

In *DNB Banka*, DNB Banka AS received various services from group companies located in other EU countries in the framework of intra-group service agreements¹⁶⁰. The remuneration charged by the group companies amounted to the cost of the services with an uplift of 5%¹⁶¹. The latter uplift was required under transfer pricing rules. DNB Banka claimed the application of the cost-sharing exemption for the intra-group services¹⁶². In order to decide on the case, the referring court sought guidance on the scope of the concept "independent group of persons", as mentioned in article 132(1)(f) of the VAT Directive¹⁶³. It also raised the question of whether the exemption can be combined with the transfer pricing-related uplift of 5%¹⁶⁴. Finally, the Latvian court asked whether the exemption can be used in a cross-border situation¹⁶⁵. Similarly to *Aviva*, the CJEU followed Advocate General Kokott's opinion, and judged that the cost-sharing exemption does not apply when the members of the independent group of persons do not carry on an activity in the public interest referred to in Article 132, but carry on an activity in the area of financial services¹⁶⁶. The CJEU came to that conclusion by examining again the context¹⁶⁷ and the objectives¹⁶⁸ of the cost-sharing exemption.

¹⁵⁴ Ibid para. 10

¹⁵⁵ Ibid para. 12.

¹⁵⁶ Ibid para. 17.

¹⁵⁷ Ibid paras. 25 to 27.

¹⁵⁸ Ibid paras. 28 to 30.

¹⁵⁹ Ibid para. 31.

¹⁶⁰ Judgement of 21 September 2017, *DNB Banka AS*, C-326/15, EU:C:2017:719, paras. 11 to 15.

¹⁶¹ Ibid para. 13.

¹⁶² Ibid para. 21.

¹⁶³ Ibid para. 22.

¹⁶⁴ Ibid.

¹⁶⁵ Ibid.

¹⁶⁶ Ibid para. 45.

¹⁶⁷ Ibid paras. 30 to 32.

¹⁶⁸ Ibid paras. 33 to 35.

In *Commission v Germany*¹⁶⁹, the Commission started infringement procedures against Germany for the application of the cost-sharing exemption in that Member State. The Commission was of the opinion that restricting the cost-sharing exemption only to the health-care sector is incompatible with the VAT Directive¹⁷⁰. The CJEU dismissed Federal Republic of Germany's arguments. The Court reiterated that, on the basis of the context¹⁷¹, the objectives¹⁷² and the drafting history¹⁷³ of Article 132(1)(f) of the VAT Directive, the cost-sharing exemption applies only when the exempt activities of the members of the cost-sharing group are those referred in Article 132 of the VAT Directive. The CJEU also concluded that the cost-sharing exemption cannot be limited to cost-sharing groups whose members carry on an activity only in the health sector¹⁷⁴.

As a consequence of these rulings, the CJEU, following a strict interpretation of the cost-sharing exemption, precludes the application of the latter when the members are engaged in exempt activities in the financial and insurance sector. The opposite is repeatedly supported by the Commission¹⁷⁵. The Commission services are of the opinion that the cost-sharing exemption may also cover activities of commercial nature and not only activities in the public interest.

3.4. Third condition: Directly necessary

The cost-sharing exemption may be applicable to services that are directly connected with the exempt supplies of the members, or with activities in which the members of the group participate as non-taxable persons¹⁷⁶. This requirement is not further explained by the VAT Directive, neither has the CJEU dealt with the interpretation of the term "directly necessary". However, the Commission has discussed the term "directly necessary" and can provide some guidance on the topic.

The Commission has expressed its opinion for a strict interpretation of the expression "directly necessary"¹⁷⁷. The first reason for such a restrictive interpretation is the fact that, according to the CJEU, exemptions without the right to deduct are to be interpreted strictly, since they constitute derogations to the general rule¹⁷⁸. The general rule is that, according to Article 1(2) of the VAT Directive, that EU VAT is a general turnover tax that must be levied on as many supplies of goods and services by taxable persons as possible. The second reason is the principle of fiscal neutrality, in accordance to which the cost-sharing arrangements and the formation of cost-sharing groups provide similar

¹⁶⁹ Judgement of 21 September 2017, *Commission v Federal Republic of Germany*, C-616/15, EU:C:2017:721.

¹⁷⁰ Ibid para. 23.

¹⁷¹ Ibid paras. 44 to 46.

¹⁷² Ibid paras. 47 and 48.

¹⁷³ Ibid paras. 58 and 59.

¹⁷⁴ Ibid para. 60.

¹⁷⁵ VAT Committee, Working Papers No. 450 p. 2, No. 654 p. 6 and No. 856 p. 11.

¹⁷⁶ VAT Committee, Working Paper 856, p. 11.

¹⁷⁷ VAT Committee, Working Paper No. 450 p. 2 and Working Paper No. 654 p. 7.

¹⁷⁸ Judgement of 15 June 1989, *Stichting Uitvoering Financiële Acties v Staatssecretaris van Financiën*, C-348/87, EU:C:1989:246 and Judgement of 19 July 2012, *Finanzamt Frankfurt am Main V-Höchst v Deutsche Bank AG*, C-44/11, EU:C:2012:484. See also Doesum Ad von and Others, *Fundamentals of EU VAT Law*, (Wolters Kluwer 2016), p. 263-265.

VAT treatment for small and medium-sized enterprises compared to larger businesses and allow them to cease competitiveness in a VAT neutral way¹⁷⁹. The latter leads to the third reason for a strict interpretation which is the requirement of absence of competition in order for the exemption to be applicable¹⁸⁰. If the “directly necessary” criterion were to be given a broad interpretation and allow for the inclusion of services that do not constitute an indispensable input for the members’ activities¹⁸¹, this would be more likely to cause distortion of competition issues¹⁸².

Consistent to the Commission’s view, the expression “directly necessary” should be interpreted as referring to services which are specifically related to the downstream activity and which constitute an indispensable input for those activities being carried out¹⁸³. This “direct link” should be looked into on a case-by-case basis, based on the facts of each case¹⁸⁴. Finally, based on the Commission’s approach, services rendered for the benefit of members’ activities of general nature, such as administration, legal and tax advice, management, must not fall within the scope of the exemption, since they are functions, required for all economic operators and not only for cost-sharing groups¹⁸⁵, unless the specific circumstances of the purpose of forming the cost-sharing group provide otherwise.

3.5. Fourth Condition: Exact reimbursement of joint expenses

According to Article 132(1)(f) of the VAT Directive, the cost-sharing group may only claim from its members the exact reimbursement of their share of the joint expenses¹⁸⁶. The brief wording of the provision does not indicate the way that this condition should be examined. It does not also provide the criteria for the cost-sharing group in order to claim its expenses by its members¹⁸⁷.

Firstly, it must be noted that the term “expenses” refers to the group’s costs¹⁸⁸. This is drawn as conclusion, in view of the different language versions of the provision, and especially of the German and French versions¹⁸⁹. Secondly, in principle, this condition provides for a prohibition of profit regarding the services supplied by the group to its members¹⁹⁰. This is inferred by Advocate General Mischo in his Opinion for

¹⁷⁹ Terra B.J.M.. and Kajus J. *Introduction to European VAT (Recast), Commentaries on European VAT Directives 2018*, IBFD, p. 443.

¹⁸⁰ See below Section 3.5.

¹⁸¹ See to that effect: In *Taksatorringen* where the CJEU held that without the services provided by the cost-sharing group, the consequent supply of insurance services by the group’s members would have been very difficult, if not impossible.

¹⁸² Jovanovic N. and Merckx MM.W.D., IVM September/October 2016 p. 328.

¹⁸³ VAT Committee Working Papers No 654 p. 7, No. 856 p. 11 and No. 883 p. 19.

¹⁸⁴ VAT Committee Working Paper No. 883 p. 19.

¹⁸⁵ VAT Committee Working Paper No. 450 p. 2.

¹⁸⁶ VAT Committee Working Paper 450 p. 2.

¹⁸⁷ Swinkels J.J.P., ‘The EU VAT exemption for Cost-Sharing Associations’, (2008) 19(1) International VAT Monitor, Journals IBFD, p. 16.

¹⁸⁸ Ibid.

¹⁸⁹ The German language version provides “...genaue Erstattung des jeweiligen Anteils an den gemeinsamen Kosten”, while the French language version refers to “le remboursement exact de la part leur incombant dans les dépenses engagées en commun”.

¹⁹⁰ VAT Committee, Working Paper No 654 p. 7. See also The Fundamentals of EU VAT Law, p. 274

Taksatorringen, where he notes that it is essential that the group does not exist for purposes of gain, in the sense that it only charges its members for expenses incurred by it in order to meet their requirements, and makes no profit whatsoever out of doing so. This means that the group must be entirely transparent and that, from an economic point of view, it must not have the characteristics of an independent operator seeking to create a customer base to generate profits¹⁹¹. This also emerges from the Commission's view that the VAT is a cost that can be shared and reimbursed by the entity's members¹⁹². A cost-sharing group is a taxable person whose activities are exempt from VAT. The non-deductible VAT incurred by the group is a cost for the group that can be included in its expenses and be refunded by its members¹⁹³.

In the aforementioned *Stichting Centraal Begeleidingsorgaan voor de Intercollegiale Toetsing* judgement, the CJEU concluded that, even when the services are supplied only to one of the members of the cost-sharing group, the services are invoiced to that member at its actual cost, since analytical accounting rules can be used for calculating the exact share of the expenses attributable to each of the services individually¹⁹⁴.

In *DNB Banka*, one of the questions of the referring court to the CJEU was whether the Member State of the establishment of the group should preclude the application of the exemption in a case where an uplift of 5% has been applied, in accordance with the transfer pricing rules of that same Member State¹⁹⁵. The CJEU did not answer this question since the latter held that the cost-sharing exemption is not applicable, when the exempt services provided are those referred in Article 135 of the VAT Directive and not those referred in Article 132 of the VAT Directive. However, Advocate General Kokott provided an answer to this question. She stated that, under Article 132(1)(f) of the VAT Directive, the condition of the exact reimbursement of the share of joint expenses is not met, when a cost uplift is applied, even when such flat-rate cost uplift is required under the legislation on direct taxation¹⁹⁶. Advocate General Kokott's opinion is in line with the Commission's view. The Commission explicitly mentioned that the direct tax consequences which may flow from transfer pricing rules imposed by the VAT Directive, should have no consequences on the VAT treatment of the services provided by the group¹⁹⁷. Van Doesum, van Kesteren, and van Norden take an opposite view. They submit that "transfer pricing adjustments entail a de facto extra retroactive charge to the members, there may no longer be an exact reimbursement of

¹⁹¹ Opinion of Advocate General Mischo delivered on 3 October 2002, *Assurandør-Societetet acting on behalf of Taksatorringen v Skatteministeriet*, EU:C:2002:562, paras. 121 and 122. See also supra 30.

¹⁹² VAT Committee, Working Papers No. 450 p. 2 and No. 856 p. 12.

¹⁹³ Supra n. 96, p. 12.

¹⁹⁴ Judgement of 11 June 1989, *Stichting Centraal Begeleidingsorgaan voor de Intercollegiale Toetsing v Staatssecretaris van Financiën*, C-407/07, EU:C:2008:713, para. 38.

¹⁹⁵ Judgement of 21 September 2017, *DNB Banka AS v Valsts ienemumu dienests*, C-326/15, EU:C:2017:719, para. 22.

¹⁹⁶ Opinion of Advocate General Kokott delivered on 1 March 2017, *DNB Banka AS v Valsts ienemumu dienests*, C-326/15, EU:C:2017:145, para. 52.

¹⁹⁷ VAT Committee, Working Paper No. 654 p. 7

costs”. In their opinion, such costs are to be shared and reimbursed by the group’s members, because this reflects the economic reality¹⁹⁸.

Moreover, the Commission services regard as possible that the cost-sharing group can also provide taxable services to its members and non-members, as long as these services are taxed¹⁹⁹. This results from a literal interpretation of the provision. Since the wording of Article 132(1)(f) does not state otherwise, the cost-sharing group could make profit out of taxed supplies, made to members and third parties, provided that the main activity of the group is to provide exempt services to its members²⁰⁰.

As already indicated, the aforesaid condition presents many difficulties in its application, since no real directions are provided on this matter. This leads to divergences in its application by the Member States. A possible and reasonable solution could be to allow the Member States a margin of discretion when examining its application²⁰¹.

3.6. Fifth condition: Absence of distortion of competition

The cost-sharing exemption may not be applied where it is likely to cause distortion of competition. This expression has led to interpretative problems, and someone may argue that it must be distinguished by the term “distortion of competition” in competition law²⁰². The CJEU dealt with this condition in *Taksatorringen*²⁰³. Taksatorringen was an association established by small and medium-sized insurance companies authorised to underwrite motor-vehicle insurance policies in Denmark²⁰⁴. The purpose of Taksatorringen was to access damage caused to motor vehicles in Denmark on behalf of its members²⁰⁵. The expenses involved in its activity were apportioned among its members in such a way that each member’s payment for services by the association equals to that member’s share of joint expenses²⁰⁶. Its application for a VAT exemption was turned down by the Danish VAT Tribunal, among other things, because an exemption could rise to distortion of competition²⁰⁷. The dispute resulted in questions of the Østre Landsret to the CJEU for a preliminary ruling. The national court needed guidance on the interpretation of the competition clause by its second, third and fourth question²⁰⁸.

¹⁹⁸ Doesum von A. and others, *Fundamentals of EU VAT Law* (Wolters Kluwer 2016), p. 274-275.

¹⁹⁹ VAT Committee, Working Paper No. 883 p. 19.

²⁰⁰ Jovanovic N. and Merckx M.M.W.D., ‘The Cost-sharing exemption under Debate- Part I’, (2016)27(5) International VAT Monitor, Journals IBFD, p. 329.

²⁰¹ Pfeiffer S., *The VAT grouping from an EU perspective*, p. 256.

²⁰² See to that effect Vyncke K., ‘Cost sharing Associations as an Alternative to VAT grouping in Belgium’, (2006) 17(5) International VAT Monitor, IBFD Journals, p. 345.

²⁰³ Judgement of 20 November 2003, *Assurandør-Societetet acting on behalf of Taksatorringen v Skatteministeriet*, C-8/01, EU:C:2003:621.

²⁰⁴ Opinion of Advocate General Mischo delivered on 3 October 2002, *Assurandør-Societetet acting on behalf of Taksatorringen v Skatteministeriet*, C-8/01, EU:C:2002:56, para. 12.

²⁰⁵ Ibid, para. 13.

²⁰⁶ Ibid, para. 14.

²⁰⁷ Judgement of 20 November 2003, *Assurandør-Societetet acting on behalf of Taksatorringen v Skatteministeriet*, C-8/01, EU:C:2003:621. para. 21.

²⁰⁸ Ibid, para. 25.

The Court, following AG Mischo's opinion, made clear that it is the mere fact that the exemption itself and not the fact that the group satisfies the other conditions of the provision in question must be liable to cause distortion of competition²⁰⁹. The Court then clarified that if, irrespective of the application of the exemption, the groups are assured of keeping their members custom, there is no reason to take the view that it is the exemption granted to them that closes the market to independent operators²¹⁰. The Court then concluded that the grant of VAT exemption must be refused if there is a real and genuine risk that the exemption may by itself, immediate or in the future give rise to distortions of competition²¹¹.

In the aforesaid *Commission v Germany*, the CJEU also dealt with the distortion of competition criterion. Germany argued that Member States are allowed to exclude certain sectors or particular activities from the cost-sharing exemption based on the argument that distortion of competition is caused in such cases. Pursuant to AG Wathelet's opinion, CJEU answered positively at the Commission's action²¹². It concluded that the assessment of the conditions relating to the absence of distortion of competition cannot be limited in a general manner by a Member State²¹³ and a case-by-case basis of the absence of competition is required²¹⁴.

In the abovementioned *Aviva*, the referring Court also asked what criteria should be applied in assessing whether there is distortion of competition in accordance with Article 132(1)(f) of the VAT Directive²¹⁵. The CJEU did not answer this question since it took the view that the relevant exemption was not applicable in the case, but Advocate General Kokott provided some guidance on the interpretation of the competition clause. Advocate General Kokott supported a restrictive interpretation of the distortion of competition criterion, having as starting point *Taksatorringen* judgement²¹⁶. She held that the distortion of competition criterion serves to avoid abuse and the cost-sharing exemption must not be applied inappropriately^{217,218}. Advocate General further notes

²⁰⁹ Ibid, para. 58.

²¹⁰ Ibid, para. 59 and Opinion of Advocate General Mischo delivered on 3 October 2002, *Assurandør-Societetet acting on behalf of Taksatorringen v Skatteministeriet*, EU:C:2002:562, para. 131.

²¹¹ Ibid, paras. 63 and 64.

²¹² Judgement of 21 September 2017, *Commission v Federal Republic of Germany*, C-616/15, EU:C:2017:721, para. 71.

²¹³ Ibid, para. 67.

²¹⁴ Ibid, para. 69. See also Opinion of Advocate General Wathelet delivered on 5 April 2017, EU:C:2017:272, *Commission v Federal Republic of Germany*, C-616/15, paras. 119 and 120.

²¹⁵ Judgement of 21 September 2017, *Minister Finansów v Aviva Towarzystwo Ubezpieczeń na Życie S.A. w Warszawie*, C-605/15, EU:C:2017:718, para. 17.

²¹⁶ Opinion of Advocate General delivered on 1 March 2017, *Minister Finansów v Aviva Towarzystwo Ubezpieczeń na Życie S.A. w Warszawie*, C-605/15, EU:C:2017:150, para. 68.

²¹⁷ Opinion of Advocate General Kokott delivered on 1 March 2017, *Minister Finansów v Aviva Towarzystwo Ubezpieczeń na Życie S.A. w Warszawie*, C-605/15, EU:C:2017:150, para. 70.

²¹⁸ In para. 71 of her Opinion, AG Kokott considers "as possible indications of inappropriate application of the exemption when the group supplies the same services for consideration to non-members and is to that extent, by exploiting effects of synergy, operating on the market, or when the main aim of the group's formation is simply to optimise the input VAT burden or when 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."

that Article 132(1)(f) is sufficiently clear to serve the principle of legal certainty and unconditional and therefore, directly applicable²¹⁹.

3.7. The territorial scope of the Cost-Sharing Exemption

The wording of Article 132(1)(f) of the VAT Directive provides that the cost-sharing exemption is not restricted to one Member State. Therefore, on the basis of a literal interpretation of the provision, it is possible to apply the cost-sharing exemption in cross-border situations. The VAT Committee has expressed this opinion several times²²⁰. Furthermore, the latter has discussed possible implications of a cross-border application of the cost-sharing exemption, focusing especially on the requirements provided for the exemption to be applicable²²¹.

Despite the fact that the Court did not answer the referring question regarding the cross-border application of the cost-sharing exemption in *Aviva*, Advocate General Kokott offers her insights on this matter in her opinion²²². Advocate General Kokott started her analysis by a textual interpretation of Article 132(1)(f) of the VAT Directive, stating that the provision does not *prima facie* limit the cost-sharing group and its members geographically in one Member State²²³. Nevertheless, she concluded the opposite; the cost-sharing exemption is namely restricted within one Member State. Based on the provision's drafting history, the scheme of exemptions, the evaluation of Article 11(1) of the VAT Directive and the competition clause contained in Article 132(1)(f) of the VAT Directive, the Advocate General Kokott held that Article 132(1)(f) of the VAT Directive does not cover services supplied by a cross-border group to its members established in other Member States (or third countries). According to the Advocate General not even the fundamental freedoms require the exemption under Article 132(1)(f) of the VAT Directive to be extended to a cross-border group. It is justified by the need to preserve the allocation of the power to impose taxes between Member States. Such extension would, moreover, enable undertakings to exploit the different tax rates and tax regimes in place²²⁴.

Regarding the argument of an incompatibility between a cross-border cost-sharing group scheme and the national VAT grouping facility²²⁵, the Advocate General Kokott argued that it is not possible to apply stricter conditions for the VAT grouping scheme whose territorial scope is restricted to a single Member State than the cost-sharing exemption when it applies in a cross-border situation. That dictates a stricter and not a broader implementation of the cross-border cost-sharing group exemption. =impose

²¹⁹ Opinion of Advocate General delivered on 1 March 2017, *Minister Finansów v Aviva Towarzystwo Ubezpieczeń na Życie S.A. w Warszawie*, C-605/15, EU:C:2017:150, paras. 74 to 76

²²⁰ Working Papers No 450, 654, 856 p. and 883 p. 20.

²²¹ The Cost-Sharing Exemption under Debate- Part II

²²² Opinion of Advocate General Kokott delivered on 1 March 2017, *Aviva*, C- 605/15, EU:C:2017:150

²²³ Opinion of Advocate General Kokott delivered on 1 March 2017, *Aviva*, C- 605/15, EU:C:2017:150, para. 37.

²²⁴ Terra B.J.M. and Kajus J., *Introduction to European VAT (Recast), Commentaries on European VAT Directives*, (2018, IBFD Publications), p. 443

²²⁵ Opinion of Advocate General Kokott delivered on 1 March 2017, *Aviva*, C- 605/15, EU:C:2017:150, paras. 46 to 49.

less strict conditions for a cost-sharing group which applies in a cross-border situation than for a VAT grouping which applies domestically.

Many legal scholars disagree with Advocate General Kokott's opinion in relation to the cross-border application of the cost-sharing exemption²²⁶ and in fact, one may support that the literal interpretation of the provision is sufficient to guide the taxpayers and the tax authorities on the way how to interpret the territorial scope of the cost-sharing exemption²²⁷.

4. Similarities and Differences between the VAT Grouping and the Cost-Sharing Exemption

The VAT grouping and the cost-sharing exemption are two provisions of the VAT Directive that appear to have similarities but also many differences.

Firstly, the EU legislation provided both provisions with the same objective, the enhancement of fiscal neutrality in the EU VAT system²²⁸. VAT should have no influence on business costs

Secondly, someone might argue that both provisions lead to the same outcome, the non-chargeability of VAT, but by following different routes²²⁹. When a VAT group is formed, its members lose their status, and a new single taxable person is created²³⁰. That results in out-of-scope transactions between the members. In this way, VAT groups limit their input VAT in relation to the intra-group transactions of goods and services²³¹. On the other hand, the cost-sharing exemption provides the exemption of services provided to the members of the cost-sharing group by the latter. In this way, certain supplies of goods and services for VAT groups and certain supplies of services for cost-sharing groups not to be subject to VAT. Hence, the cost-sharing organisations reduce their VAT costs of services provided to their members, when the latter have no or limited right to deduct VAT²³².

Thirdly, the settled case-law provides that the personal scope of both provisions is applied in the same way regarding the legal and taxable status of their members. Members of VAT groups as well as of cost-sharing groups can be both taxable and non-

²²⁶ Wolf R.A., 'The end of Cost-Sharing as we know it?', (2017)28(3) International VAT Monitor, Journals IBFD, 203-209; and Jovanovic N. and Merckx M.M.W.D., 'The Cost-Sharing Exemption under Debate- Part II', (2016) 27(5) International VAT Monitor, Journals IBFD, 417-420.

²²⁷ Wolf R.A., 'The end of Cost-Sharing as we know it?', (2017)28(3) International VAT Monitor, Journals IBFD, 203-209.

²²⁸ Pfeiffer S., *VAT grouping from a European Perspective*, (IBFD Doctoral Series Volume 34), p. 257.

²²⁹ Terra B.J.M. and Kajus J., *Introduction to European VAT (Recast), Commentaries on European VAT Directives*, IBFD 2018, p. 443.

²³⁰ Judgement of 22 May 2008, *Ampliscientifica and Amplifin*, C-162/07, EU:C:2008:301.

²³¹ Terra B.J.M. and Kajus J., *Introduction to European VAT (Recast), Commentaries on European VAT Directives*, (2018, IBFD Publications), p. 443.

²³² Terra B.J.M. and Kajus J., *Introduction to European VAT (Recast), Commentaries on European VAT Directives*, (2018, IBFD Publications), p. 443.

taxable persons, with the legal form being irrelevant for the application of both provisions. Furthermore, as Pfeiffer mentions “*both rules aim to be neutral in terms of competition*”. Article 11(2) of the VAT Directive stipulates that the Member States is allowed to take measures in order to prevent tax avoidance or evasion, while Article 132(1)(f) of the VAT Directive provides that the exemption is applicable solely in the absence of distortion of competition²³³.

The first and more striking difference is that VAT grouping is an optional provision, while the cost-sharing exemption is a mandatory provision of the VAT Directive. This is reflected in the case-law, where in *Larentia+Minerva and Marenave*, the Court held that the substantive scope of the VAT grouping leaves a margin of discretion in the national legislation to define the latter, whereas Advocate General Kokott in her opinion in *DNB Banka/Aviva* advocates for the direct applicability of the cost-sharing exemption. The second main difference is that the VAT groups may provide both good and services to their members, while cost-sharing groups can provide only services to its members that are directly necessary for their exempt or non-taxable activities.

Regarding the personal scope of the provisions, there are also striking differences. Firstly, VAT group can be formed of two members. A cost-sharing group can consist only from the independent group and two more persons, so three persons need to agree to form an independent group of persons for the cost-sharing exemption to be applicable²³⁴. Secondly, VAT group is a legal fiction and it is considered as a single taxable person. The members of the VAT group dissolve themselves from any possible, existing legal form and instead becomes part of a new separate taxable person for VAT purposes²³⁵. This is not the case in the cost-sharing exemption. Article 132(1)(f) of the VAT Directive requires, for the exemption to apply that services are supplied by a cost-sharing group only to its members. This membership requisite seems to entail that the cost-sharing group “belongs” to its members²³⁶, and must be distinguished from being a “member” of the VAT group under Article 11 of the VAT Directive, where the members lose their personality and merge into the new single taxable person. Moreover, there is no sector limitation for the formation of a VAT group, unless such a restriction is justified in the purpose of the second paragraph of Article 11. After *DNB Banka, Aviva* and *Commission v Germany*, the cost-sharing exemption is not applicable for services in the financial and insurance sectors.

Another difference is the territorial scope of each provision. VAT grouping schemes are restricted within the territory of a Member state. This is the result of the optional character of Article 11 of the VAT Directive. Article 132(1)(f) of the VAT Directive is

²³³ Pfeiffer S., *VAT grouping from an EU Perspective*, (IBFD Doctoral Series 34), p. 258.

²³⁴ Judgement of 15 June 1989, *Stichting Uitvoering Financiële Acties v Staatssecretaris van Financiën*, C-348/87, EU:C:1989:246, para. 14.

²³⁵ See above: Judgement of 22 May 2008, *Ampliscientifica and Amplifin*, C-162/07, EU:C:2008:301 (footnote 17) and Judgement of 17 September 2014, *Skandia America Corp. v Skatteverket*, C-7/13, EU:C:2014:2225.

²³⁶ See above: Judgement of 20 November 2003, *Assurandør-Societetet acting on behalf of Taksatorringen v Skatteministeriet*, C-8/01, EU:C:2003:621.

applicable both domestically and in cross-border situations, as the wording of the provision does not provide for a territorial limitation²³⁷.

Last but not least, cost-sharing exemption aims at levelling the playing field between big and small enterprises in order to achieve economies of scale²³⁸. In contrast, VAT groups are implemented by large enterprises.

5. The Interaction between VAT Grouping and the Cost-Sharing Exemption

5.1. The VAT group as member of the independent group of persons

The Commission's approach is that the wording of Article 132(1)(f) does not exclude a priori a VAT group from being a member of a cost-sharing association²³⁹. There is no obvious reason to exclude single taxable persons who are themselves composite entities from the benefit of the exemption. In such a case, the prerequisites of the abovementioned provision must be met by the VAT group as a whole, since the latter is the only existing taxable person²⁴⁰.

It may be argued that the VAT group may not be required to fulfil the requirements of Article 132(1)(f) of the VAT Directive. That is a false approach since from the formation of the VAT group there is only one single taxable person for VAT purposes, the VAT group. Furthermore, it must be noted that when a cost-sharing group renders services to the VAT group for its out-of-scope intra-group supplies of services. Only if the provided service is directly necessary for carrying out the exempt service, the exemption will be applicable.

5.2. The independent group of persons part of the VAT group

As abovementioned, one of the main effects for a person entering a VAT group is the "*effect of dissolution*". The person entering the VAT group loses any existing simultaneously legal personality and a new separate taxable person is considered for VAT purposes²⁴¹. The initial approach of the Commission services, expressed in the Working Paper No 856 of the VAT Committee, was that the cost-sharing group as a member of the VAT group loses practically its VAT identification number (until now it was a separate from its members taxable person) and is no longer able to operate it. The entity supplying the services is the VAT group as a whole and not the cost-sharing

²³⁷ Opinion of Advocate General Kokott delivered on 1 March 2017, *Aviva*, C-605/15, EU:C:2017:150 and Opinion of Advocate General Kokott delivered on 1 March 2017, *DNB Banka AS*, C-326/15, EU:C:2017:145

²³⁸ Ibid. See also Opinion of Advocate General Mischo delivered on 3 October 2002, *Assurandør-Societetet acting on behalf of Taksatorringen v Skatteministeriet*, C-8/01, EU:C:2002:562, para. 120.

²³⁹ Supra n. 198.

²⁴⁰ See Appendix Figure 3.

²⁴¹ European Commission, Communication from the Commission to the Council and the European Parliament on the VAT group option provided for in Article 11 of Council Directive 2006/112/EC on the common system of value added tax, Brussels 2 July 2009, COM(2009)325 final.

group so the cost-sharing exemption is no longer applicable. In working Paper No 883, the Commission evolved its approach. Notably, the individual members of an independent group of persons for cost-sharing exemption will not automatically become members of the VAT group on account of the cost-sharing group's action. Joining the VAT group is dependent for the members of the cost-sharing group, upon the 3-links test. The Commission holds specifically that *“nothing seems to prevent the VAT group as a whole from acting as a cost-sharing group and taking over the role played by the original cost-sharing group which can no longer operate individually for VAT purposes. Subject to the rest of the requirements being met (which is dependent upon the characteristics of the activities of the individual members), it appears that the exemption could be applied under the circumstances described”*²⁴². One may argue that such an approach is far-reaching and it is practically inapplicable. By forming a VAT group, the VAT group members merge into one taxable person. In such a case, the personal scope of the cost-sharing exemption is not fulfilled. Furthermore, as the intra-group supplies of both goods and services are deemed to be out of the scope, the application of the exemption is without any meaning²⁴³.

6. Conclusion

First of all, VAT grouping and the cost-sharing exemption are two provisions in the VAT Directive which present interpretation difficulties and discrepancies in their application from Member State to Member State²⁴⁴. The different elements of the scope of Article 11 of the VAT Directive are further cleared by the CJEU to a certain degree, with the assistance of the opinions of the Advocate Generals in the relevant case-law²⁴⁵ and the European Commission²⁴⁶. Taxable persons and non-taxable persons can form or join a VAT group, irrespectively of their legal form, strictly within the territory of one Member State. The substantive scope of VAT grouping facilitation exhibits still unclear aspects compared to the personal and territorial scope, since the CJEU has never dealt with this aspect directly. Article 132(1)(f) of the VAT Directive was the subject of interpretation for the CJEU in only seven cases²⁴⁷. Regarding the personal scope, the independent entity, the cost-sharing group is always a taxable person and its members, can be either taxable or non-taxable persons, with the legal form of the group as well as the members being irrelevant. Regarding the territorial scope, the literal interpretation of Article 132(1)(f) does not restrict the application of the exemption exclusively to the territory of a single Member State. The cross-border application of

²⁴² See Appendix Figure 4.

²⁴³ Pfeiffer S., *EU VAT Grouping from an EU Perspective*, (IBFD Doctoral Series Volume 34), p. 260.

²⁴⁴ This is the fact provided that VAT grouping is transposed by a Member State to its domestic legislation, prior consultation of the VAT Committee.

²⁴⁵ The case-law referred is analysed in Chapter 2 of the present thesis.

²⁴⁶ Despite the facts that the European Commission interpretation of the provisions of the VAT Directive is not legally binding.

²⁴⁷ This case-law is presented in Chapter 3 of the present thesis.

the exemption within the EU or where a third state is involved, presents major difficulties. The directly necessary criterion as well as the condition of the exact reimbursement of the joint expenses of the cost-sharing group are the requirements that present the least discrepancies. Finally, the most difficult element of the requirements of the cost-sharing exemption is the absence of distortion.

In respect to the comparison of the two provisions, they demonstrate similarities and difficulties. Aiming to fiscal neutrality, they lead to the same actual income, the fact that certain transactions are either not taxable or VAT exempt, namely not subject to VAT. However, they display many fundamental differences. Cost-sharing groups are not subject to any territorial limitation, while VAT groups are not, in principle, subject to any sector limitation. The material and the formal scope of the provisions are different. Furthermore, some aspects of the personal scope of the said articles are utterly different.

Regarding the interaction of the two concepts, the Commission and part of the literature are of the opinion that there should be no limitation for the application of the exemption in combination with the VAT grouping provision as long as the conditions of the provisions are met. In principle, the case of a VAT group being a member of a cost-sharing group does not provide with any practical difficulties. The opposite, which is recently opined by the Commission seems to far from applicable.

As final remarks, both provisions must be harmonized at EU level or amended to enhance the internal market. It seems that the VAT grouping scheme is now the alternative of the cost-sharing exemption in light of the recent abovementioned judgements with the territorial restriction of the VAT grouping remaining a hindrance for the economic operators. An alternative solution could be the inclusion of a new provision for the application of the cost-sharing exemption for the activities referred to in Article 135 of the VAT Directive, as proposed in 2007²⁴⁸. This is for the future researchers and foremost the EU legislature and the European Commission to deal with anew.

²⁴⁸ In 2007, the European Commission presented a proposal for reform of the EU VAT Directive as regards the tax regime applicable to financial services but it was never adopted.

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Appendix

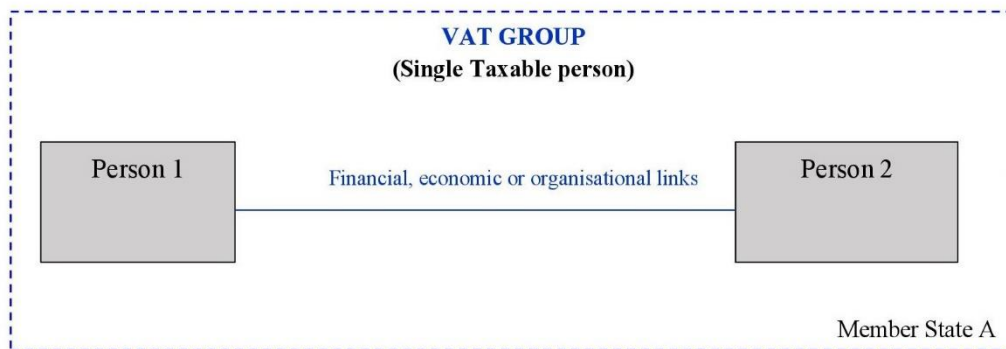


Figure 1: A VAT Group

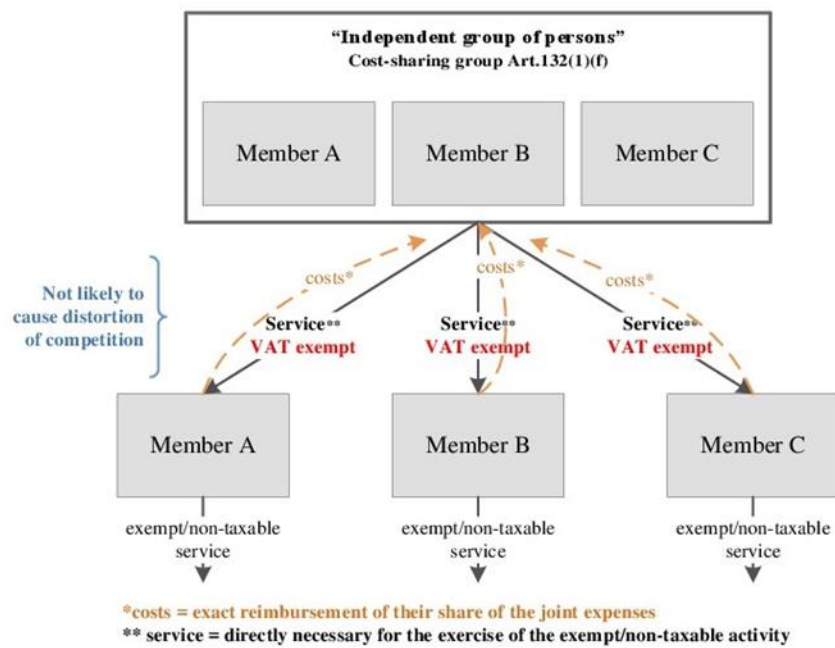


Figure 2: A cost-sharing group

(As depicted in Working Paper 883, VAT Committee)

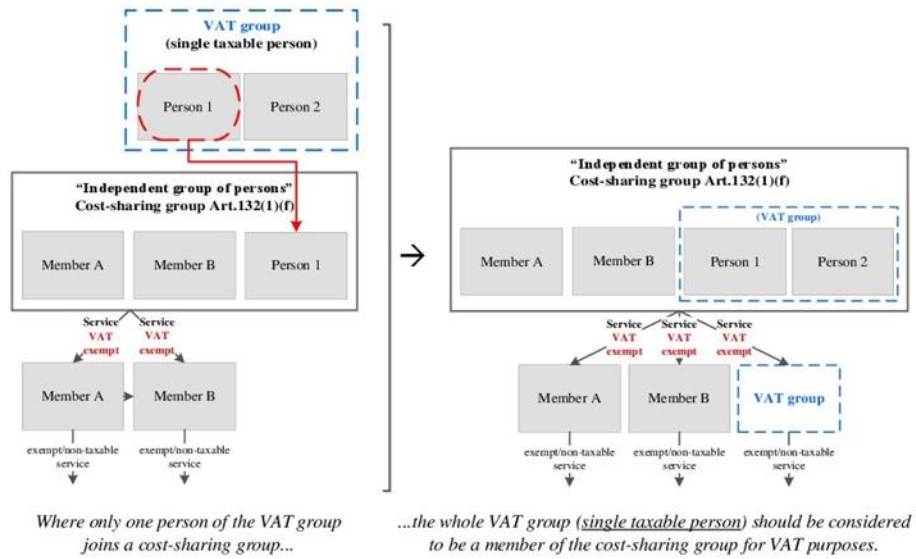


Figure 3: A VAT Group as part of a Cost-Sharing Group

(As depicted in Working Paper 883, VAT Committee)

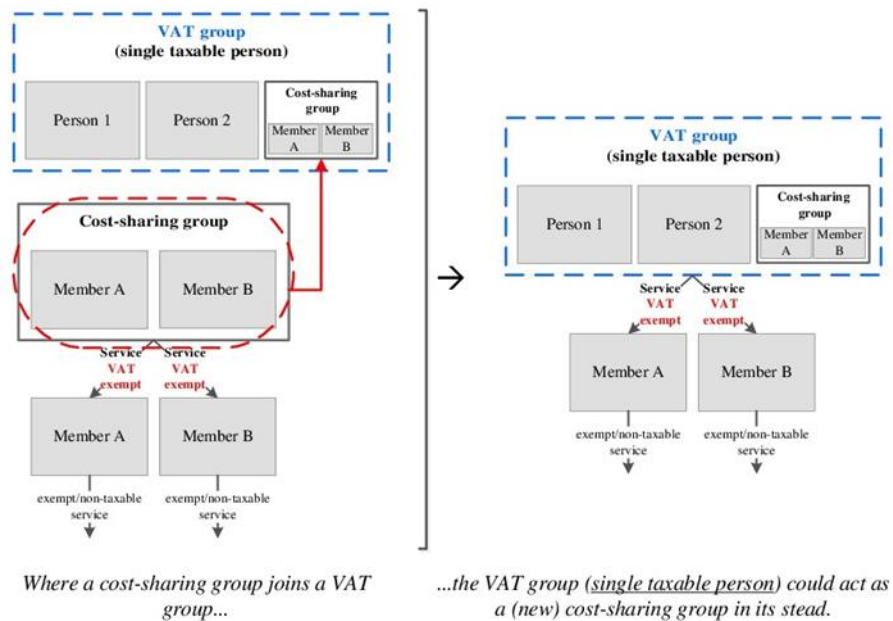


Figure 4: A Cost-Sharing Group as part of VAT Group

(As depicted in Working Paper 883, VAT Committee)