Studi Tributari Europei. Vol.10 (2020)
ISSN 2036-3583

VAT grouping – EU law and Austrian implementation

Sebastian Pfeiffer*

Published: April 26, 2021

Abstract

Under the EU VAT Directive, Member States have to option to introduce VAT grouping. This article discusses the EU VAT grouping notion as well as the Austrian implementation of VAT grouping. After an historic overview of VAT grouping, the reasons of the VAT grouping regime are analyzed. Subsequently, the optionality of VAT grouping, the substantive scope and the territorial restriction will be examined.

Keywords: VAT grouping; fundamental freedoms; Organschaft; link criteria; optionality of VAT grouping; territorial restriction.

1. Introduction and historic overview

Austria's history with VAT grouping is closely linked to the German system of *Organschaft*. Indeed, the wording of the German and Austrian implementation of VAT grouping is nearly identical.

The Austrian regime of VAT grouping (also called *Organschaft*) has been part of the Austrian VAT legislation since 1945.[1] However, since Austria became a Member State of the European Union, the VAT grouping legislation is to be interpreted as the implementation of Art 11 VAT Directive.

Nevertheless, VAT grouping is far from new with regard to European VAT legislation. Historically, VAT grouping can already be found in the Second VAT Directive.[2] Art 4 of the Second Directive defined taxable persons as "any person independently engaging in transactions pertaining to the activities of producers, traders or persons providing services, whether or not for gain." Further clarification could be found in Annex A para 2 of the Second Directive, where the term "independent" was further defined as allowing *"[…] 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 organizational relationships*."

Legislative changes were made with the Sixth Directive.[3] Art 4 para 4 of the Sixth Directive depicts the requirements of VAT grouping as they are known today.[4] While the Second Directive – more

* Institut für Österreichisches und Internationales Steuerrecht (Austria); ✉ se.pfeiffer@bfg.gv.at

1. See further Rechtsüberleitungsgesetz of 1 May 1945, StGBl. Nr 6/1945; also at Prechtl, *Die umsatzsteuerliche Organschaft*, in Achatz/Tumpel (Hrsg.), *Umsatzsteuer im Konzern* (2003) 27 (28 et seq.); Kühbacher, *Die umsatzsteuerliche Organschaft in Deutschland und Österreich*, SWI 2012, 411 (412).

2. See 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 value added tax.

3. See Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization oft he laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment.

4. Furthermore, an interesting change may be seen there as Annex A para 2 of the Second Directive dealt with „taxable persons" forming a VAT group, while the Sixth Directive spoke only of „persons."

or less – merely recognized that some Member States had some kind of VAT grouping regime in place,[5] the Sixth Directive altered the wording and – more importantly – the aim and intention of the EU VAT grouping notion. The Commission in its explanatory memorandum to the Sixth Directive notes that "*in the interest of simplifying administration or of combating abuses (e.g. the splitting up of one undertaking among several taxable persons so that each may benefit from a special scheme) Member States will not be obliged to treat as taxable persons those whose 'independence' is purely a legal technicality*."[6]

With the VAT Directive, only slight changes were made and a second paragraph added in order for Member States to prevent tax evasion or avoidance through the use of VAT grouping.

In the following, this contribution shall discuss the Austrian implementation of VAT grouping while also discussing the underlying EU law issues. Therefore, in section 2, the reasons for introducing VAT grouping will be discussed. In section 3, the question of optionality of VAT grouping will be determined. In section 4, the substantive scope of VAT grouping will be dealt with. Lastly, section 5 will discuss the territorial limitations of VAT grouping.

2. Reasons for VAT grouping

In order to determine the rationale of VAT grouping, it is worthwhile to look back in history to a VAT system without input VAT deduction. In such a VAT system, every supply of goods was subject to tax within the chain of companies without input VAT deduction. In other words, the larger the production chain of a product was, the more irrecoverable VAT was levied on that product. At the end of the day, that fatal flaw lead to an incentive for companies to merge or insource in order for their products not be burdened with VAT more than once.

Here is where VAT grouping comes in. Looking at the historic reasoning of German courts, the aim of VAT grouping was to face the economic reality: It should be irrelevant for VAT purposes if a part of a company is outsourced as a separate taxpayer (e.g. a production or distribution company) or acts as the department of a bigger corporation.[7] Hence, a company that is integrated in another company similar to a department, should be treated as one taxable person.[8]

Compared to the current VAT system, this historic reasoning of VAT grouping has lost its merits: by allowing input VAT deduction between taxpayers, a supply is – in general – not burdened with irrecoverable VAT. Indeed, however, this historic reasoning of VAT grouping still remains true where exemptions are applied. As a taxpayer subject to an exemption will not be able to deduct input VAT, the supply will still be burdened with VAT which cannot be deducted. Therefore, this reason – in a

5. Arguably the Netherlands and Germany; see A. Parolini, *European VAT and groups of companies*, in G. Maisto (ed.) *International and EC Tax Aspects of Groups of Companies* (2008).

6. See European Commission, Proposal for a sixth Council Directive on the harmonization of Member States concerning turnover taxes – Common system of value added tax: Uniform basis of assessment (1973) Supplement to Bulletin oft he European Economic Community 1, 8 = COM(73) 950).

7. See H. G. Ruppe, M. Achatz, *Umsatzsteuergesetz*, 5th edition, Vienna, 2017, § 2 m. no. 114, with reference to VwGH 9. 4. 1970, 135/68 (*„Organ und OT müssten eine wirtschaftliche Einheit bilden, bei der das Organ dem OT zugeordnet ist und die Untergesellschaft den Betrieb der Obergesellschaft nach Art einer Betriebsabteilung fördere";* translation by the author: "parent and subsidiary need to form an economic unity where the subsidiary acts as the parent's department"); see also T. Kühbacher, *Die umsatzsteuerliche Organschaft in Österreich und Deutschland*, in SWI, 2012, pp. 416 et seq. and Schimetschek, *Die Entwicklung der Organlehre*, in FJ, 1975, p. 81..

8. See B. Prechtl, *Die umsatzsteuerliche Organschaft*, in M. Achatz, M. Tumpel (eds) *Umsatzsteuer im Konzern*, 2003, p. 28; RFH 23. 11. 1926, I B 101/26: *„[B]eide Gesellschaften [müssen] sich zueinander wie die mehreren Abteilungen eines Großunternehmens verhalten" translation by the author: „both companies must act towards each other like several departments of a large company." RFH* 11. 11. 1927, I A 75/27: *„[Die Tochtergesellschaft] muss finanziell, wirtschaftlich und organisatorisch in das andere geschäftliche Unternehmen – nach Art. einer bloßen Geschäftsabteilung – eingegliedert sein"* translation by the author: „The subsidiary must be financially, economically and organizationally integrated into the other corporation – in the manner of a mere business department".

limited capacity – is still valid today[9]. Other than that, other authors have suggested reasons for VAT grouping, i.e. that only one VAT return needs to be filed or that there is administrative simplification for the tax administration (as only one taxpayer needs to be audited) and the taxpayers (as no VAT needs to be invoiced).[10]

3. Optionality of VAT grouping

Art 11 VAT Directive stipulates that each Member State "*may*" introduce VAT grouping. Therefore, it is clear from the wording of Art 11 VAT Directive that implementing VAT grouping to domestic law is an option for the Member States themselves. In other words, at first, the Member State itself has the option to introduce VAT grouping or not.

The second aspect of the optionality of VAT grouping revolves around the question whether, once implemented in domestic law, VAT grouping may be optional for domestic taxpayers as such. In other words, do domestic persons or taxpayers have the option to opt for VAT grouping? This question is answered differently throughout academia and Member States. Indeed, most of the Member States that implemented VAT grouping also allow for an optional application in their domestic law.[11] Some Member States, however, take the position that once implemented in domestic law, VAT grouping has to be applied obligatorily.[12]

Legally – in the author's opinion – the question is quite clear. Art 11 VAT Directive is an option targeted towards Member States. No indication is given whether or not Member States retain the right to decide if they want to establish a mandatory or an optional domestic VAT grouping system. Assuming that such a "double option" was possible, it would run counter to the system of options used in the VAT Directive. Indeed, other rules in the VAT Directive can be found where Member States are obliged to offer options in their national law.[13] However, such clear rules that Member States must provide for an option is missing with regard to Art 11 VAT Directive. If a double option were possible, the VAT Directive would provide for a specific rule stipulating the domestic optional character. However, without such an explicit provision, the VAT grouping option – from a purely legal viewpoint – cannot be interpreted to be optionally applied by the taxpayers.

However, there are policy arguments to be brought forward for the optional application of VAT grouping by taxpayers. Indeed, if one of the key rationales of VAT grouping is to be found in administrative simplification,[14] such simplification is maximized – at least for the taxpayers – if they retain the right to choose VAT grouping or not. Moreover, this promotes the taxpayers' flexibility[15] and legal certainty if taxpayers actively choose to apply VAT grouping.

Other authors, however, argue, that making domestic VAT grouping optional may be based on do-

9. See already D. Hummel, Missbrauch der umsatzsteuerrechtlichen Organschaft bei Kooperationen im Gesundheitswesen? MwStR 2013, 294 et seq.

10. See further S. Pfeiffer, *VAT Grouping from a European Perspective*, 2015 pp. 163 et seq. with further references. However, one might argue that the main reason of VAT grouping is the fact that intra-group transactions are out-of-scope of VAT. While it is true that the VAT group only has to submit one VAT return, the supplies of all group members have to be recorded. The simplification of filing only one VAT return – especially when done electronically – is miniscule. The administrative simplification for tax administrations is actually also not that great as the audit needs to comprise the supplies of all group members even though only one VAT taxpayer is audited.

11. Amongst others and not limited to Belgium, Italy and Hungary.

12. E.g., Austria, Germany and the Netherlands.

13. See for example the rules for the special VAT treatment of farmers (Art 296 para 3 of the VAT Directive) or Art 137 VAT Directive fort he option for taxation of certain exempt supplies.

14. Judgment of 22 May 2008, Ampliscientifica and Amplifin, C-162/07, EU:C:2008:301, para. 30.

15. See F.M. Moreno & MF. Gómez, *VAT Grouping in Spain: An Interesting Opportunity*, 37 Intertax 3, p. 177.

mestic procedural law which is outside of the purview of the harmonization by the VAT Directive.[16] Therefore, an optional domestic VAT grouping regime should be possible. While compelling, this argument has the flaw that by taking that view, every other obligatory rule of the VAT Directive could be made optional by the Member State.[17]

4. Substantive Scope

4.1. EU law

The substantive scope of VAT grouping comprises the financial, economic and organizational links necessary between the VAT group members. The main question here is, whether these links have an EU law meaning, i.e. whether there is a uniform EU law approach as to what a financial, economic and organizational link is.

The European Commission indeed presented its opinion on the link criteria twice. Firstly, in the Communication regarding VAT grouping in 2009.[18] Secondly, in a working paper to be discussed in the VAT Committee.[19] However, in light of the CJEU case law of *Larentia+Minerva*, it seems that the link criteria are not to be interpreted uniformly. Quite on the other hand, the definition of the link criteria seems to lie in the purview of the Member States: *"[…] the formation of a VAT group is subject to the existence of close financial, economic and organisational links between the persons concerned [which] need[…] to be specified at national level."*[^19] Therefore, it stands to reason to assume that the substantive scope has a purely domestic meaning.[20]

At the outset, this makes a lot of sense: VAT grouping is restricted to one Member State (in detail see below). Furthermore, it is an option for the Member State. Therefore, if a rule is optional and does not influence any other Member State's revenue or taxpayers, the details on how it should be applied should lie with the Member State that decides to implement the option.

While this argument seems to have merit at the outset, it becomes clear in light of the case *Skandia America* that the implementation of VAT grouping in one Member State may have repercussions on other Member States taxpayers.

4.2. Austrian implementation

4.2.1. General remarks

The Austrian VAT Act does not provide any guidance of the link criteria. However, the VAT guidelines issued by the Austrian Ministry of Finance lay down a number of rules on how to interpret the link criteria.[21] Furthermore, Austrian case law can be found which deals with the link criteria.

16. See Joachim Englisch, *Unionsrecht und Organschaft*, in UR vol. 21, 2016, p. 836 who argues that only two Member States – Austrian and Germany – do not offer an optional application of the domestic VAT grouping scheme.

17. A compelling example is the application of Art 196 VAT Directive which lays down the regular reverse-charge mechanism of cross-border B2B services. It is quite clear that this rule is to be applied mandatorily by Member States. However, following the argument of procedural law, Member States could circumvent the obligatory application of the cross-border reverse-charge mechanism by providing an option in their domestic procedural law.

18. See 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, COM(2009) 325 final.

19. See European Commission, Working Paper 918, Meaning of „financial, economic and organisational links" among VAT group members, taxud.c.1(2017)982178.

20. However, it is not completely clear if that is the case. The CJEU ruled that Art 11 VAT Directive cannot be relied upon directly by taxpayers as the link criteria are to be defined by the Member States. However, whether nor not there is a uniform basic approach to all three link criteria is still open and will have to be answered by the Court.

21. The Austrian VAT guidelines can be found in German at https://findok.bmf.gv.at

The Austrian link criteria are based on the fact that the Austrian VAT grouping regime follows a top-down approach. In other words, a VAT group is present were subsidiaries fulfil the links to a parent company. Under Austrian law, all three links have to be fulfilled. However, not all links have to be there in full intensity. In other words, if one link is especially strong, the other links can be weaker.

4.2.2. Financial link

The financial link is deemed to be present if the capital of a company is controlled. However, primarily it is not the capital but the voting rights conferred by that capital that leads to the existence of the financial link. Therefore, a financial link is present when 75% of the capital of another company is held. However, a financial link can also be present with a capital holding between 50% and 75% if the economic and organizational link is strong.[22]

4.2.3. Economic link

An economic link between a subsidiary and its parent company is present, where the subsidiary's business forms an organic part of the entire business of the parent company. In principle there needs to be a reasonable business context between the parent and its subsidiary. Their activities need to complement each other and need to have a coherent character. This is the case if their businesses are interconnected, supplementary to each other or coordinated.[23]

The Austrian case law on the existence of economic links is casuistic on the basis of the general definition of an economic link.[24] For example, an economic link is deemed to exist where the VAT group member's entire turnover resulted from the sale of crude oil, to which certain other high-grade oils produced by the parent company were added. Therefore, only by adding both products was the VAT group member able to produce sellable products.[25] Moreover, a group member essentially selling almost exclusively the product of the parent company (5% third-party profits) leads to the existence of an economic link.[26] In another judgment, the Austrian Supreme Administrative Court ruled that an economic link was deemed to exist where a group member, engaged in food retailing, sold meat products produced by a different VAT group member.[27] An economic link also present where a VAT group member supplied the EFTA market, while the head of the VAT group took care of the EEC market.[28] Moreover, the rent of immovable property by the parent company to its subsidiary in order for the subsidiary to use it as distributing warehouse fulfils the criterion of an economic link.[29] An economic link was furthermore ruled to exist where a prospective customer could not realize that the VAT group member was actually an own company as that VAT group member appeared as part of the whole corporation.[30] An economic link was also seen to exist where a parent company contractually obliged its subsidiary to sell energy without mark-up to customers which normally needed to have been supplied by the parent company itself.[31] More recently, with reference to ECJ case *Larentia+Minerva*, the Austrian Supreme Administrative Court ruled recently that solely by

22. See Austrian VAT guidelines, para. 236.
23. See Austrian VAT guidelines, para. 237.
24. See also in great detail S. Pfeiffer, *VAT Grouping from a European Perspective*, Masterdam, 2015 pp. 135–139.
25. See Austrian Supreme Administrative Court, 7 May 1979, 2319/78, ECLI:AT:VWGH:1979:1978002319.X01.
26. See Austrian Supreme Administrative Court, 16 June 1966, 1319/65, ECLI:AT:VWGH:1966:1965001319.X01, ECLI:AT:VWGH:1961:1960001844.X01.
27. See Austrian Supreme Administrative Court, 5 June 1961, 1844/60.
28. See Austrian Supreme Administrative Court, 30 June 1964, 1639/62.
29. See Austrian Supreme Administrative Court, 20 September 2001, 98/15/0007, ECLI:AT:VWGH:2001:1998150007.X00..
30. See Austrian Federal Fiscal Court, 13 November 2003, FSRV/0090-L/02.
31. See Austrian Supreme Administrative Court, 13 December 2007, 2006/14/0043, ECLI:AT:VWGH:2007:2006140043.X00.

renting out office space to the head of the VAT group, a subsidiary is economically integrated to the head of the VAT group.[32]

In summary, most of the case law on the economic link dealt with supplies of goods. However, more and more questions arise whether an economic link is present where only certain services are provided, especially in a holding structure. For example, is an economic link present where the parent company supplies certain administrative services (marketing, IT) to its subsidiaries? Is this already enough for an economic link to be present? As the economic link is the most elusive of all three link criteria, it remains to be seen how the jurisprudence of the Supreme Administrative Court will develop.

4.2.4. Organizational link

An organizational link is deemed to be present where the parent company has the potential to enforce its will regarding business decisions of the subsidiary. It is secured by sending members of the management board of the parent to the management board of the subsidiary or measures with a similar organizational effect, such as group directives and policies legally binding the management of the integrated company to the parent's decisions. It does not suffice, however, if the parent has the right to appoint the members of the management board of the integrated company or to terminate their appointment.[33]

5. Territorial restriction

5.1. General remarks

Art 11 VAT Directive restricts the formation of a VAT group to "*any persons established in the territory of that Member State*." In its essence, the restriction of VAT groups to persons established in one Member State may lead to questions on the compatibility with the fundamental freedoms. This issue has already been discussed by academics in a number of ways.[34] The second issue of the territorial restriction of VAT grouping refers to the so called cross-border external effects of domestic VAT groups.

5.2. Compatibility with the fundamental freedoms

5.2.1. General remarks

The VAT Directive is an EU secondary law instrument. It is well known that secondary law instruments have to be in line with primary law. This has been demonstrated by the CJEU a couple of times.[35] At the outset – however – the discussion of whether the territorial restriction of Art 11 VAT Directive is in line with the fundamental freedoms is quite an academic one. Indeed, in practice,

32. See Austrian Supreme Administrative Court, 23 November 2016, Ro 2014/15/0031, ECLI:AT:VWGH:2016:RO2014150031.J00..

33. See Austrian VAT guidelines, para. 239.

34. C. Bjerregaard Eskildsen, *VAT Grouping versus Freedom of Establishment*, in EC Tax Review 2011, 114; T. Ehrke-Rabel, *VAT Grouping: the Relevance of the Territorial Restriction in Article 11 VAT Directive*, in WJOVL, vol. 1, 61–79; J. Boor, *Die Gruppenbesteuerung im harmonisierten Mehrwertsteuerrecht*, 2014, 70; T. Hartmann, *Die Vereinbarkeit der umsatzsteuerrechtlichen Organschaft mit dem Europäischen Unionsrecht*, 2013, 97; A. van Doesum, H. van Kesteren, G-J. van Norden, *The Internal Market and VAT: Intra-Group Transactions of Branches, Subsidiaries and VAT Groups*, in EC Tax Review 2007, 34–43.

35. See Judgment of 26 October 2010, Schmelz, C-97/09, EU:C:2010:632, para. 50; Judgment of 25 June 1997, Kieffer and Thill, C-114/96, EU:C:1997:316, para. 27; Judgment of 9 August 1994, Meyhui NV v Schott Zwiesel Glaswerke AG, C-51/93, EU:C:1994:312, para. 11; Judgment of 17 May 1984, Denkavit, 15/83, EU:C:1984:183, para. 15.

the CJEU was and continues to be quite reluctant to declare tax law specific secondary law to be not in line with the fundamental freedoms.[36]

In order to determine whether or not the territorial restriction of Art 11 VAT Directive is in line with primary law, the CJEU's steadily ruled evaluation criteria will be used. Therefore, firstly, the fundamental freedoms' scope of protection needs to be affected. Secondly, there needs to be an unequal treatment between purely domestic and cross-border situations. Thirdly, this unequal treatment needs to be examined in the light of possible justifications. Lastly, possible justifications need to comply with the principle of proportionality.

5.2.2. Affected fundamental freedoms

In principle, three fundamental freedoms could be restricted by the territorial restriction of Art 11 VAT Directive. Firstly, due to the fact that Art 11 VAT Directive restricts the use of VAT grouping to persons established within a Member State, the freedom of establishment pursuant to Arts. 49 and 54 TFEU could be infringed. Secondly and as a consequence of treating intra-group supplies to be out-of-scope, the free movement of goods and the freedom to provide services could be restricted. This follows the logic that within a VAT group, supplies between the VAT group members are treated to be out-of-scope for VAT purposes. However, due to restriction of VAT grouping to one Member State a VAT group cannot be formed across the border, the regular VAT rules will apply, i.e., regular intra-Community supplies and acquisitions for the supply of goods and the application of the normal rules regarding services, especially the place of supply rules and the reverse-charge mechanism.

5.2.3. Restriction of fundamental freedoms

Whether or not the fundamental freedoms are restricted depends on whether different rules are applied to comparable situations or if similar rules are applied to different situations.[37] In other words, a pair of comparison must be found.

The pair of comparison must consist of a domestic VAT group (parent and subsidiary) and a parent company established in one Member State and a subsidiary established in another Member State that fulfil the requirements of VAT grouping but cannot form a VAT group due to the territorial restriction. Within that pair of comparison, the VAT treatment of the supply of goods and services bust be analysed, in order to determine whether there is an unequal treatment.

Where within a domestic VAT group supplies of goods and services are provided, they are out-of-scope for VAT purposes. In a cross-border scenario, the general VAT rules apply. Insofar as in the cross-border scenario, both entities are able to fully deduct input VAT, no different VAT treatment applies at the end of the day: In the case of a supply of goods, the cross-border supply will be zero-rated by the seller, while the acquisition in the other Member State will be subject to VAT as intra-Community acquisition with input VAT deduction. Therefore, except for additional administrative burdens, no different VAT treatment compared to a VAT group applies. The same result is reached for supplies of services: In a VAT group, such services are out-of-scope; across the border, they are – in principle – taxed at destination by applying the reverse-charge mechanism with input VAT deduction.

This result changes where the recipient of the supplies is not (fully) able to deduct input VAT. Again, where a VAT group is formed, the supply of goods and services is out-of-scope. No non-recoverable input VAT is incurred. Where the VAT group cannot be formed across the border, however, the application of the regular VAT rules leads to non-recoverable input VAT, as the recipient of the

36. See further N. Zorn, *Überlegungen zu gemeinschaftsrechtlichen Grundrechten*, in M. Achatz et al. (eds) *Steuerrecht – Verfassungsrecht - Europarecht:Festschrift für Hans Georg Ruppe*, Vienna, 2007, p. 755.

37. See Judgment of 29 April 1999, Royal Bank of Scotland, C-311/97, EU:C:1999:216, para. 26; Judgment of 21 September 1999, Saint-Gobain, C-307/97, EU:C:1999:438, paras. 47 et seq.; Judgment of 14 February 1995, Schumacker, C-279/93, EU:C:1995:31, para. 30.

supply is not fully able to deduct the input VAT incurred (either in form of the intra-Community acquisition or the reverse-charged VAT of a service). Therefore, in these situations, there is an unequal treatment between a purely domestic situation and a cross-border situation.

5.2.4. Justification

Whether a restriction of the fundamental freedoms really leads to an infringement of said freedoms depends on whether the restriction can be justified.

Indeed, while almost all academics come to the conclusion that the territorial restriction restricts the fundamental freedoms, there are different results whether or not this restriction is justified.[38] While the author in earlier works was of the opinion that the restriction to the fundamental freedoms could not be justified,[39] the recent CJEU case law on the non-application of cross-border cost-sharing arrangements indicates differently. Indeed, the restriction of the fundamental freedoms can be justified by the need to preserve the allocation of the power to impose taxes between Member States.[40]

As indicated above, Art 11 VAT Directive is an option for the Member State. Therefore, introducing VAT grouping is a Member State's genuine VAT policy decision.[41] Conversely, however, not introducing VAT grouping is also a valid VAT policy decision. Both decisions are equal. If VAT grouping were to be applied across the border, the Member States' decisions on implementing VAT grouping would clash. On the one hand, if one Member State did not implement VAT grouping, it had to accept the consequences of another Member State exercising the option by disregarding the regular VAT rules. Imagine the following example:

> Member State 1 implemented VAT grouping. Parent company "P" is established in Member State 1.
>
> Member State 2 did not implement VAT grouping. Subsidiary "S" is established in Member State 2.
>
> Under the domestic law of Member State 1, a VAT group could be formed between P and S. Services rendered from P to S would be out-of-scope of VAT by applying Member State 1's domestic law. However, under Member State 2's domestic law, there is no VAT group. Therefore, the regular VAT rules should apply: services rendered across the border from P to S should be taxed in Member State 2.

There is no legal basis for binding a Member State to the policy decision of another Member State.[42] Furthermore, such a binding effect could also have an impact on the VAT revenue of the other state.

Similar results may also be reached where both Member States introduced VAT grouping. As long as the substantive scope is in the purview of the Member States themselves, there is the possibility that one Member State accepts the formation of a VAT group while the other Member State does not. Why should the interpretation of the VAT grouping rule of one Member State be more valid than the interpretation of another Member State?

Therefore, as long as VAT grouping is optional and not harmonized in as far as there is a uniform approach among all Member States, a restriction to the fundamental freedoms is justified. The

38. See further ibid fn. 34.

39. See especially S. Pfeiffer, VAT Grouping from a European Perspective (2015) Chapter 4 and S. Pfeiffer, Current questions of EU VAT grouping, World Journal of VAT/GST Law 2015, 1 et seq.

40. See Opinion of AG Kokott, 1 March 2017 on Case C-605/15, *Aviva*, para. 58 with further references.

41. See Case C-85/11 Commission v Ireland [2012] ECLI:EU:C:2012:753, Opinion of Advocate General Jääskinen, para 46.

42. See S. Pfeiffer, *EU VAT Grouping - Past, Present Future*, in Egholm Elgaard et al (eds.) *VAT Grouping & Cost-Sharing*, Copenhagen, 2020, pp. 32 et seq. with further references.

decision of one Member State to introduce VAT grouping cannot and should not lead to effects of other Member States or impede their policy decisions.

5.3. Cross-border effects of domestic VAT groups

Even though cross-border VAT groups are impossible *de jure*, domestic VAT groups have effects in cross-border situations. This follows the logic that once a VAT group is formed, it is considered to be a single taxable person. The following examples paint a picture of these cross-border effects of VAT groups:

Example: Domestic supplies by foreign VAT groups[43]

> A UK VAT group consists of two taxable persons (parent and subsidiary) who are fully able to deduct input taxes. They do not have fixed establishments in Austria. The parent company sells goods to its subsidiary. The goods are located in Salzburg (Austria) and transported to Vienna (Austria).
>
> From the perspective of the UK VAT group, that transaction is out-of-scope as it constitutes an intra-group supply of goods.

In this example, the question needs to be posed whether the other Member State (in this case Austria) is obliged to take the consequences of UK VAT grouping into account. If there was no foreign VAT group, the domestic sale of goods in Austria would constitute a taxable supply pursuant to Art 31 VAT Directive.

Example: Chain transaction[44]

> An Austrian parent company and its subsidiary form a VAT group in Austria. A French taxpayer orders goods from the Austrian subsidiary. The subsidiary passes the order to its parent company. The parent company directly transports the goods to the French customer.
>
> From the point of view of the Austrian VAT legislation, there is no chain transaction but merely one intra-Community sale of goods that can be zero-rated. However, from the point of view of France, there should first be an intra-Community acquisition by the Austrian subsidiary and a subsequent domestic supply of goods in France.

These two examples make it clear that even though a VAT group cannot be formed across the borders of a Member State, the formation of a VAT group still has cross-border effects. Therefore, if a VAT group cannot be formed across the border of Member States due to the fact that the allocation of VAT is jeopardized, should the effects of a VAT group also be restricted to one Member State? Indeed, it seems that the VAT Committee came to the conclusion that the effects of a domestic VAT group have to be considered by other Member States, even if that other Member State did not implement VAT grouping.[45] It seems that this has been accepted by the CJEU as well. In the *Skandia America* case, the CJEU ruled that a third state head-office's branch that is part of a VAT group in a Member State dislodges from the third state head-office. In other words, it becomes a part of the VAT group. As a consequence, services supplied from the head-office to the branch will

43. See already S. Pfeiffer, *Current questions of EU VAT grouping*, in World Journal of VAT/GST Law 2015, 1 (9 et seq).

44. See already S. Pfeiffer, *Current questions of EU VAT grouping*, in World Journal of VAT/GST Law 2015, 1 (10).

45. See in that regard the VAT Committee Guidelines on *Skandia America*, taxud.c.1(2015)747072: „The VAT Committee by a large majority confirms that by joining a VAT group pursuant to Article 11 of the VAT Directive, an entity (head office or branch) becomes part of a new taxable person for VAT purposes – namely the VAT group – irrespective of the legal person to which it belongs. The large majority of the VAT Committee also confirms that the treatment of a VAT group as a single taxable person precludes the members of the VAT group from continuing to operate, within and outside their group, as individual taxable persons for VAT purposes."

not be out-of-scope of VAT[46] but will be taxed.[47] Hence, the CJEU in a nutshell ruled, that the VAT group formed in a Member State has an external effect. Indeed, the CJEU did not elaborate on the question if the other state is bound to take the consequences into consideration as well. However, this eventually leads to a fissure between the VAT treatment of a single service: While one state – righty so – takes the opinion that a service is out-of-scope,[48] the other state taxes the service.

The *Skandia America* case only dealt with supplies of services performed to a VAT group. But should the *Skandia* case also apply to the inverse situation, i.e., the supply of a fixed establishment which is part of a VAT group to its head office located in another Member State? While the VAT Committee Guidelines prefer a symmetric approach, the author is of the opinion that a symmetrical application of the Skandia America consequences may lead to unwanted results, both regarding input and output VAT.[49] As VAT grouping is optional for Member States, not all Member States have exercised the option to introduce VAT grouping. If the *Skandia* consequences were applied in the inverse situation, i.e., in outbound cases, non-taxation might occur: The Member State of destination that in principle is able to tax on the one hand might not acknowledge its taxing right or is simple not aware of it.[50] If the destination state did not introduce VAT grouping, a situation where a branch that is part of a foreign VAT group supplies to its head-office would still be covered by the *FCE Bank* consequences.[51] Similarly, that Member State could merely argue that as the VAT grouping option was not exercised, the consequences of *Skandia* do not apply.[52]

Even where the Member State of destination introduced VAT grouping, it may argue that a VAT group formed under a foreign Member State's domestic law is not a single taxable person under its own domestic law.[53] Therefore, if the *Skandia* consequences are applied symmetrically, the VAT

46. See Judgment of 23 March 2006, FCE Bank, C-210/04, EU:C:2006:196.

47. See Judgment of 17 September 2014, Skandia America, C-7/13, EU:C:2014:2225.

48. Which could imply a bar on input VAT deduction as well.

49. With more details also at S. Pfeiffer, EU VAT grouping – past, present and future, Copenhagen (2020) in print.

50. See S. Pfeiffer,*VAT Grouping – Consequences of Nigl and Follow-up on Skandia America*, in M. Lang et al (eds) *CJEU – Recent Developments in Value Added Tax 2016*, Vienna, 2017, pp. 146 et seq.; S. Pfeiffer, *Taxable Persons: VAT Grouping and Fixed Establishments*, in M. Lang et al (eds) *CJEU – Recent Developments in Value Added Tax 2014*, Vienna, 2015 pp. 72 et seq. with further references; S. Pfeiffer, *Rs Skandia America und ihre möglichen Auswirkungen auf die österreichische Organschaft*, in ÖStZ, 2015, pp. 313 et seq (at p. 314).

51. See G-J. van Norden, State of Play in Respect of the Skandia America Corporation Case, in EC Tax Review, vol. 4, 2016, p. 216. The author argues that the Commission will not start infringement procedures against Member States that do not apply the *Skandia America* judgment; see also British arguments to the *Skandia America* case at A. Lang-Horgan, *Die britische Interpretation des Territorialitätsprinzips – Skandia und seine Folgen für deutsche Banken und Versicherungen*, in MwStR, vol. 8, 2015, pp. 288 et seq.; similarly at H. Nieskens, *Widerstreitende Grundprinzipien in der Umsatzsteuer: der Grundsatz der Unternehmenseinheit und der Grundsatz der Organschaft – zugleich ein Beitrag zur EuGH-Entscheidung Skandia*, in BB, vol. 22, 2015, pp. 1303 et seq. (at p. 1307); with reference of the loss of taxing rights see F. Becker, *EuGH-Urteil vom 17. 9. 2014, Skandia America Corp. (USA): Begrenzung der Organschaft auf inländische Unternehmensteile und Grundsatz der Unternehmenseinheit*, in UStB, vol. 12, 2014, pp. 346 et seq. (at p. 352); similarly also G-J. van Norden, *Skandia America. VAT group. Taxable supplies. Court of Justice*, in H&I 2014, pp. 22 et seq. (at p. 28), who argues for a differentiation between Member States that have exercised the option or not; similarly J. Boor, *Die Gruppenbesteuerung im harmonisierten Mehrwertsteuerrecht*, 2014, p. 54.

52. See again G-J. van Norden, *State of Play in Respect of the Skandia America Corporation Case*, in EC Tax Review, vol. 4, 2016, p. 216; similarly Sundberg, *Insight Skandia America*, in Tax Planning International European Tax Service, vol. 12, 2014, pp. 4 et seq. (at p. 6) with direct reference to France and Spain. Similarly, the Skandia America judgment shall not apply, where a Member State did not choose Sweden's mode of implementation. See also G-J. van Norden, *Skandia America. VAT group. Taxable supplies. Court of Justice*, in H&I 2014, pp. 22 et seq. (at p. 28); G-J. van Norden, *State of Play in Respect of the Skandia America Corporation Case*, in EC Tax Review, vol. 4, 2016, pp. 213 et seq.; R. Stratton, *Skandia America Corporation USA, Filial Sverige v Skatteverket: VAT grouping and intra entity supplies*, in BTR, vol. 1, 2015, pp. 19 et seq. (at p. 24); with reference to Germany see W. Reiß, in W. Reiß, J. Kräusel, M. Langer (eds) UStG, 128th ed, 2016 § 2 para. 127.5 (translation by author): *"It seems that the tax administration does not consider the judgment of the CJEU to be relevant for German law"*. Meanwhile, however, see a draft of the German tax administration to include a very strict interpretation of the *Skandia America* judgment in their VAT implementation guidelines commented by the Deutscher Steuerberaterverband: https://www.dstv.de/interessenvertretung/steuern/stellungnahmen-steuern/2018-s11-entwurf-bmf-schreiben-umsetzung-eugh-rs-skandia-america.

53. This follows the logic of a number of authors that a Member State should not be bound by options exercised by other

group providing services could influence their deductible input VAT as the services lead to taxed output supplies. This gains relevance especially where the VAT group is not fully able to deduct input VAT. Conversely, the Member State of destination would not tax the service. Hence, there would be a zero-rated supply of services within the EU. It stands to reason that such non-taxed supplies were the reason for the Court to decide as it decided in *Skandia America*.

6. Conclusion

The historic rational of VAT grouping should not be valid anymore in today's VAT system. Unfortunately, as the EU VAT system is not perfectly neutral, VAT grouping is used as a means to offset the negative effects of irrecoverable input VAT. In addition, as the Court has issued its strict judgments on the cost-sharing arrangements, VAT grouping has gained further popularity.[54]

Nevertheless, a number of issues of VAT grouping are still unclear. That starts with the very basic questions of whether the substantive scope has an EU law meaning or if the Court case law needs to be interpreted that there is a purely domestic meaning to the link criteria. It is furthermore followed by the question if – domestically – VAT grouping can be an option for taxpayers. These questions – in an overall European view – should be answered uniformly. Should not the same rules apply for Austrian and Italian VAT groups? Or asked differently: should such taxpayers be treated differently because they are established in different Member States?

It remains to be seen how the CJEU will develop the VAT grouping notion further. As it stands now, we know that the VAT group cannot be formed across the borders of a Member State. In light of recent CJEU case law, this probably constitutes a justified restriction of the fundamental freedoms. Nevertheless, the large majority of the Member States follows the interpretation that the formation of a domestic VAT group has cross-border effects.

Further clarifications will follow by the Court as currently two cases regarding VAT grouping are pending at the CJEU.[55]

Judgment of 16 July 2015, Larentia+Minerva and Marenave, C-108/14 and C-109/14, EU:C:2015:496, para. 50.

Sebastian Pfeiffer: Institut für Österreichisches und Internationales Steuerrecht (Austria)
✉ se.pfeiffer@bfg.gv.at
Dr. Sebastian Pfeiffer, LL.M. (WU) is a judge at the Austrian Federal Fiscal Court and an external lecturer at the Vienna University of Economics and Business.

Member States. See W. Reiß, *Begrenzung der Organschaftswirkung auf das Inland*, in J. Englisch, H. Nieskens (eds) *Umsatzsteuer-Kongress-Bericht 2010*, 2011, p. 209; W. Reiß, *Umsatzsteuerliche Organschaft und Mehrwertsteuergruppe*, in UR 2016, at p. 762; S. Pfeiffer, *VAT Grouping – Consequences of Nigl and Follow-up on Skandia America*, in M. Lang et al (eds) *CJEU – Recent Developments in Value Added Tax 2016*, Vienna, 2017, pp. 146 et seq.

54. See S. Pfeiffer, *EU VAT Grouping - Past, Present Future*, in Egholm Elgaard et al (eds.) *VAT Grouping & Cost-Sharing*, Copenhagen, 2020, pp. 36 et seq. with further references..

55. See pending Cases C-141/20, *Norddeutsche Gesellschaft für Diakonie* and C-269/20, *T* referred by the German Supreme Fiscal Court.