KPMG Meijburg & Co Tax & Legal

Court of Justice of the European Union rules on financial integration in a German VAT group

On December 1, 2022 the Court of Justice of the European Union (CJEU) rendered judgment in two German cases concerning a VAT group, the *Norddeutsche Gesellschaft für Diakonie mbH* (C-141/20) and *Finanzamt T* (C-269/20) cases. In this memorandum we take a closer look at the impact these judgments could potentially have on Dutch practice. The judgments rendered by the CJEU in these cases raise the question whether the Dutch Supreme Court's interpretation of financial integration is compatible with EU law.

1. Background

The EU VAT Directive allows Member States to regard legally independent persons established within their territory as a single taxable person (VAT group) provided those persons are closely bound to one another by financial, economic and organizational links. In doing so, the Member States may take any additional measures necessary to prevent abuse and combat tax fraud and tax avoidance.

In Germany, legally independent companies are treated as a VAT group (*Organschaft*) if it is clear from the entire set of actual circumstances that they are financially, economically and organizationally integrated with one another. With regard to financial integration, German VAT legislation requires the controlling company of the *Organschaft* (the *Organträger*) to not only hold the majority interest in the capital of the other members of the *Organschaft*, but also to hold the majority of the accompanying voting rights.

According to German VAT legislation, the *Organträger* is regarded as the taxable person and is as such obliged to comply with the VAT requirements of all the members of the *Organschaft*, including filing the VAT returns on behalf of the *Organschaft*. The separate members of the *Organschaft* are regarded as non-independent entities for VAT purposes, but nevertheless remain jointly and severally liable for the VAT debts of the *Organschaft* as such.

2. Norddeutsche Gesellschaft für Diakonie mbH (C-141/20)

Norddeutsche Gesellschaft für Diakonie mbH is a German company limited by shares. Fifty-one percent of the shares in the company are held by A. The remaining 49% are held by C e.V., a German association. The manager of Norddeutsche Gesellschaft für Diakonie mbH is also the manager of A and the executive chairman of C e.V. Norddeutsche Gesellschaft für Diakonie mbH took the position that it, together with A, forms an *Organschaft*.

The German tax authorities denied that there was an *Organschaft* between Norddeutsche Gesellschaft für Diakonie mbH and A, because they believe that A does not hold the majority of the voting rights in that company.

The referring court questioned whether the EU VAT Directive allows Germany to regard the *Organträger* as a taxable person rather than the *Organschaft* as such. Secondly, it questioned whether, for the purposes of forming a VAT group, Germany can require the *Organträger* to not only hold the majority interest in the capital of a company, but also to hold the accompanying voting rights. Lastly, the referring court questioned whether

Germany is allowed to regard the other members of the *Organschaft* as non-independent entities.

With regard to the first question, the CJEU ruled that the EU VAT Directive does not preclude treating the *Organträger* as the taxable person within the *Organschaft*. The CJEU took into consideration that it is the *Organträger* that files the VAT returns on behalf of the *Organschaft*, which means there is only one taxable person that fulfills the VAT obligations of the *Organschaft*. According to the CJEU, this situation is factually no different from the situation where the *Organschaft* as such would be regarded as the taxable person and would file the VAT returns. Furthermore, the CJEU concluded that the German tax authorities can hold all the members of the *Organschaft* to account if the VAT obligations of the *Organschaft* are not complied with.

With regard to the second question, the CJEU ruled that the requirement of financial integration does not imply that there should be a relationship of subordination between companies. According to the CJEU, this means that the requirement that the *Organträger* not only holds the majority interest in the capital of a company, but also the accompanying voting rights, is not a necessary and appropriate measure to prevent abuse and to combat tax fraud and tax avoidance.

Lastly, the CJEU ruled that the mere fact that the *Organträger* fulfills the VAT obligations on behalf of the *Organschaft* does not alter the fact that the members of the *Organschaft* bear the financial risks associated with their economic activity. According to the CJEU, they therefore cannot be regarded as non-independent entities simply because they are members of an *Organschaft* and those entities must be regarded as carrying out uncurtailed independent economic activities.

3. Finanzamt T (C-269/20)

The Finanzamt T case involved an *Organträger* that performs both economic and non-economic activities (public sector activities) and together with a subsidiary forms an *Organschaft*. The subsidiary performs cleaning services for the *Organträger*, some of which relate to the public sector activities of the *Organträger*.

In addition to the question whether Germany is allowed to designate the *Organträger* in this situation as the taxable person that should fulfill the VAT obligations of the *Organschaft*, the key question in this case was whether the services that the subsidiary performed for the public sector activities of the *Organträger* are subject to VAT. The CJEU answered that question in the negative.

4. Importance for the Dutch practice

Since 1989 the Dutch Supreme Court has ruled that being closely integrated in financial terms requires not only holding a majority interest in the capital of a company, but also holding the accompanying voting rights. The judgments rendered by the CJEU in the aforementioned cases raise the question whether the Dutch Supreme Court's interpretation of financial integration is compatible with EU law.

In Dutch practice, organizational integration is usually seen as a derivative of financial integration, because the ultimate control over the appointment of directors generally

lies with the majority shareholder of a company with share capital. However, if the majority shareholder does not also hold the majority of the voting rights, this may have the effect of breaking the organizational integration between companies, and thus the possibility of forming a VAT group. In both the above cases, the existence of organizational integration was evidently a given for the CJEU. This may also be connected to the German condition that there is a clearly, identifiable controlling body (*Organträger*) within the VAT group. In the Netherlands we do not have a controlling body within the VAT group and each member is equal. The abbreviation "c. s." also always appears in the name of the VAT group, which stands for the Latin *cum suis,* meaning "with members".

Nevertheless, there are situations where it is conceivable that organizational integration is not a corollary of financial integration. For those situations, the judgment by the CJEU could mean that it is indeed possible to form a VAT group where it was not previously possible to do so due to the fact that the majority shareholder did not hold the majority of the voting rights.

It is also not entirely clear what the CJEU means in its ruling in the Norddeutsche Gesellschaft für Diakonie mbH case that members of the *Organschaft* perform uncurtailed independent economic activities. However, partly in light of the ruling in the Finanzamt T case, we do not think it likely that the CJEU means that members of a VAT group can mutually perform activities subject to VAT.

If you would like to know more about how the above CJEU judgments could impact your company, feel free to contact your Meijburg advisor.

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