

Case C-7/13 (Skandia America Corp.) of the Court of Justice of the EU

In what is considered to be the most important European VAT case of the last 10 years, the Court of Justice of the EU (CoJEU) has ruled that supplies between a head-office and its overseas branch can be subject to VAT, if the branch is a member of a VAT group.

In the case at hand, a bank head-quartered in the USA (Skandia America Corp.) had established a branch in Sweden. The branch was a member of a Swedish VAT group, along with other local Skandia entities. The group had centralized purchases of IT-services to the American head-office. The American head-office allocated the costs for the IT-services to its Swedish branch, which in turn charged the IT-services onward to the other members of the VAT group. Through this structure no reverse charged VAT was reported by the branch on the basis that transactions within the same legal entity are to be disregarded from a VAT perspective¹. Further, transactions between members of a VAT group are viewed as transactions within one taxable person, which thus also fall outside of the scope of VAT². Consequently, where 25% VAT would otherwise have been due on the purchase of IT-services, of which only a minor portion would have been deductible, the services were purchased without any VAT charges being reported. The structure was challenged by the Swedish Tax Author-

ities, and eventually led to a referral to the CoJEU.

In its judgment of September 17, 2014 the CoJEU had its say on the structure. One of the CoJEU's first observations was that a branch is not independent of its head-quarters, and can as such not qualify as a taxable person under Article 9 of the VAT Directive (2006/112/EC). With this, the CoJEU confirmed that transactions between a head-office and its foreign branch should as a rule be considered as transactions within the same legal entity, and thus not be subject to VAT. The CoJEU went on to state that

¹ In accordance with case C-210/04 (FCE Bank Plc)

² This applies in the case of true VAT groups. It should be noted that some countries have implemented VAT group rules which only allow joint VAT return filings but nonetheless require VAT to be charged on supplies between group members.

when an entity becomes a member of a VAT group, it becomes part of a new taxable person, and can no longer be identified from a VAT perspective as an individual taxable person within or outside of the group. Thus, the CoJEU appears to have adopted the reasoning of the Commission that, by joining a VAT group, a branch “dissolves itself for VAT purposes from its fixed establishment located abroad”³.

Thus, the CoJEU concludes that a supply from a head-office to its foreign branch, which is a member of a VAT group, is to be viewed from a VAT perspective as a transaction between the foreign head-office and the VAT group, i.e. a transaction between two separate taxable persons. As such, the transaction falls within the scope of VAT, and VAT is thus to be reported under the reverse charge mechanism by the VAT group, provided that the services supplied are subject to VAT.

Interestingly enough, the CoJEU did not touch upon the point whether the outcome of the case would be the same if there were a VAT group only on the supplier’s side of the transaction, i.e. if the head-office, but not the branch, had been a member of a VAT group. In the given case this would have required an ex officio statement of the Court, seeing as an American head-office could not even hypothetically have been a member of a VAT group. However, given that there are likely to be numerous cases of European companies head-quartered in one Member State, with branches in various countries, it would seem natural that the Court must have given this possible scenario some thought as well. While it could be deduced that the intention of the CoJEU was that its reasoning should apply in all scenarios where a VAT group is involved on one end of the transaction, the lack of a clear statement in this regard inevitably, leaves the Member States with room for interpretation.

To businesses operating within a sector with a limited right to deduct VAT, the consequences of this case can be significant.

Currently, the Member States have differing views on how transactions between a head-office and branch should be treated when one of the parties is a member of a VAT group. Some Member States have applied the view of the Commission for some time already, whereas others have been of the opinion that such transactions fall outside the scope of VAT irrespective of whether or not a VAT group is involved. While the judgment can be expected to prompt tax authorities in numerous Member States to implement the CoJEU’s view going forward, the procedure and timeline for implementation can vary greatly. It is even possible that some Member States will implement the judgment retroactively, while others could put off implementation indefinitely. There is also great uncertainty at the moment around the consequences in Member States where VAT grouping rules currently only exist for VAT return/reconciliation purposes, such as Italy. While it could be argued that the judgment should not apply in those countries, as the existing VAT grouping would not allow structures that result in non-taxation, there is nonetheless a risk that the tax authorities could see this as an opportunity to collect additional tax revenue.

On the face of it the CoJEU judgment should lead to harmonization of the VAT treatment of transactions between head-quarters and foreign branches. However, it is currently too early to say whether or not that will in fact be the outcome, and as is unfortunately often the case, the Court’s reasoning leaves almost as many questions unanswered as it helped to clarify. Our strong recommendation at this stage is for businesses operating internationally in sectors with a limited right to deduct VAT, with branches and VAT groups, to look into their structures in order to identify jurisdictions where changes to the current VAT treatment could arise as a result of the judgment.

³ COM (2009) 325, section 3.3.2.2

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