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What Has the Trinity Doctrine Got to Do with VAT: Some Reflections on the CJEU Judgment in C-77/19 Kaplan International Colleges UK (Part I)

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On 18 November 2020, the CJEU delivered its judgment in case C-77/19 *Kaplan International Colleges UK**[1]*** (I will further refer to it as *Kaplan*). The questions which had been referred by the UK national court in the case had raised hopes that the CJEU would provide important clarifications as to the geographical scope of application of the so-called "cost-sharing exemption", as well as correlation between the exemption and the VAT grouping provisions.[2] The CJEU has completely dashed those hopes when it comes to the determination of the geographical scope of application of Article 132(1)(f) of the VAT Directive[3] (for my commentary, see the second part of the article), but it drew interesting conclusions on the consequences of simultaneous membership of persons in, on the one hand, a cost-sharing group and, on the other hand, a VAT group. In this article, I will take a closer look at the reasoning of the CJEU.

Setting the Background

Article 132(1)(f) of the VAT Directive provides an exemption for independent groups of persons (IGPs). It allows members of such groups, who provide exempt or out-of-scope supplies, to receive services without VAT, where those services are supplied by the group at a cost. Compared to other exemptions from VAT laid down in the VAT Directive, the cost-sharing exemption stands out, first of all, because of a long list of conditions for its application, and secondly because of its underlying rationale. The cost-sharing exemption is meant to mitigate the negative consequences of other exemptions, which stem from the non-deductibility of input VAT for providers of exempt services. It is supposed to increase the neutrality of VAT for businesses and offset competitive disadvantage faced by less aggregated undertakings. From the perspective of this rationale, the cost-sharing exemption can resemble VAT grouping, as provided in Article 11 of the VAT Directive. Pursuant to that provision, Member States may regard as a single taxable person persons established in the territory of that Member State who, while legally independent, are closely bound to one another by financial, economic and organizational links. The consequences of the application of the provisions on VAT grouping and cost-sharing lead to no VAT being applied on either transactions between the members (VAT grouping, since these are supplies within one taxable person) or transactions between the cost-sharing group and the members (exemption for certain supplies by the IGPs). Besides this similarity, VAT grouping and cost-sharing differ in every other respect: conditions for application and tax technique through which the "non-taxation" is achieved.

To apply the cost-sharing exemption, five conditions must be fulfilled, each of them causing interpretative difficulties as to what exactly they imply:

- There is an independent group supplying services to its members.
- The members are carrying on an activity which is either exempt from VAT or in connection to which the members are non-taxable persons.
- The services provided by the group are directly necessary for the exercise of the activity the members carry on.
- The group merely claims from the members exact reimbursement of its share of the joint expenses.
- The exemption is not likely to cause distortion of competition.

Various of these conditions were subject to analysis by the CJEU, which provided some clarification in its judgments (nine cases in total).[4] In *Kaplan*, four questions were referred, seeking further clarification of the membership condition and whether the exemption can apply to cross-border IGPs.

***Kaplan* Case**

In this case, an independent group established in Hong Kong supplied services to its members – various colleges established in the UK. Apart from being members of the cost-sharing group, the colleges were members of a VAT group within the meaning of Article 11 of the VAT Directive. However, the representative member of the VAT group (a holding company owning shares in all the colleges) was not a member of the cost-sharing group. The national court wanted to know whether, in such circumstances, the cost-sharing exemption can apply to the services supplied by the cost-sharing group to the members. To that end, the issue of how the formation of the VAT group and the fact that the group is established outside the Union impacts fulfilment or lack thereof of the conditions in Article 132(1) were referred to the CJEU.

The CJEU has chosen to first answer the question on the relationship of cost-sharing and VAT grouping membership. Finding that, in the circumstances of the case, the formation of the VAT group made it impossible to apply the cost-sharing exemption, the CJEU considered the answer to the question on the geographical scope of Article 132(1)(f) not needed.

The findings of the CJEU on the relationships with VAT grouping provide new insights as to the membership requirement. From the Court's reasoning, it follows that when the other conditions laid down in Article 132(1)(f) are fulfilled, the exemption is applicable to services supplied to a VAT group whose members are also members of a cost-sharing group. The exemption, however, is applicable provided that all the members of the VAT group are also members of a cost-sharing group and carry out activities exempt from VAT that belong to exemptions in the public interest or activities outside the scope of the VAT Directive. That was not the case in *Kaplan*, and thus the exemption could not apply.

However, in arriving at the conclusions, the CJEU used reasonings that apparently lack consequence and shows that the CJEU is torn between, on the one hand, considering the VAT group as one person and, on the other hand, giving that group attributes of a person pluralistic enough to constitute "members" of a cost-sharing group.

The Relationship between the Membership in a VAT Group and in a Cost-sharing Group

As a starting point, I would like to recall that cost-sharing arrangements, as encompassed by the VAT Directive, do not constitute any specific type of legal entity or structure that would require the members to be connected to each other in any particular way. A cost-sharing group, however, has to be separate from the members' taxable person able to provide services, which can thus become a subject matter of an exemption.[5] Article 132(1)(f) of the VAT Directive is focused on an exemption for transactions that take place between a group and its members.

The cost-sharing group differs from a VAT group, which is a specific type of taxable person existing for VAT purposes only and the creation of which results in "disappearance" of the members as individual taxable persons.[6] This does not mean that the members disappear other than for VAT purposes. They still exist as legal entities which can independently acquire rights and obligations. For example, VAT grouping members can, in their own capacity, acquire shares in a company and form a cost-sharing group. Could such a group then be the cost-sharing group within the meaning of Article 132(1)(f), so that its supplies to the members should be exempt? Should it not be the entire VAT group that necessarily as a whole becomes a member of a cost-sharing group? At the end of the day, each of the provisions of the VAT Directive, and also Article 132(1)(f), consist of independent Union concepts, that is, concepts having a specific meaning in the context of the harmonized system of European VAT. In other words, when we discuss cost-sharing groups for the purposes of VAT, we enter the famous "fiscal theme park in which factual and legal realities are suspended or inverted"[7]. This means that, once we are in the theme park, several members of a VAT group become one taxable person and only that one person exists for VAT purposes. For the same reasons for which only that one person – the VAT group – can be a recipient of goods and services[8], only that one person can be considered a member of a cost-sharing group within the meaning of VAT. For VAT purposes, individual members should not exist anymore.[9] It is important to note that Article 132(1)(f) requires that there are at least two persons as members of the group for the exemption to apply, and if we considered the entire group to be one member, that condition would not be fulfilled. However, this is not the way in which the CJEU seems to interpret Article 132(1)(f), at least now when contemplating the membership requirement.

The CJEU followed the reasoning of AG Kokott and ruled that the individual members of the VAT group can, in fact, be members of a cost-sharing group in the meaning of VAT, as the wording of Article 132(1)(f) does not preclude this possibility. Indeed, the provision refers to an IGP and not to taxable persons. Would that not be enough to conclude that the exemption does not apply based on the very basic argument that the condition of the services being supplied to the members is not fulfilled? If the individual colleges are the members, and the supply is to a VAT group[10], then there is a lack of identity of the members and the recipient of the supply.

And yet, this is not at all the way in which the CJEU sees it. The CJEU argues that, from the fact that it is the VAT group who is the recipient of the services, it follows that all the members of that VAT group receive those services. Does this perhaps mean that the VAT group should be regarded "simply as a screen" between the cost-sharing group and the members, in a way that AG Mischo had in mind in his opinion in *SUFA*?[11]

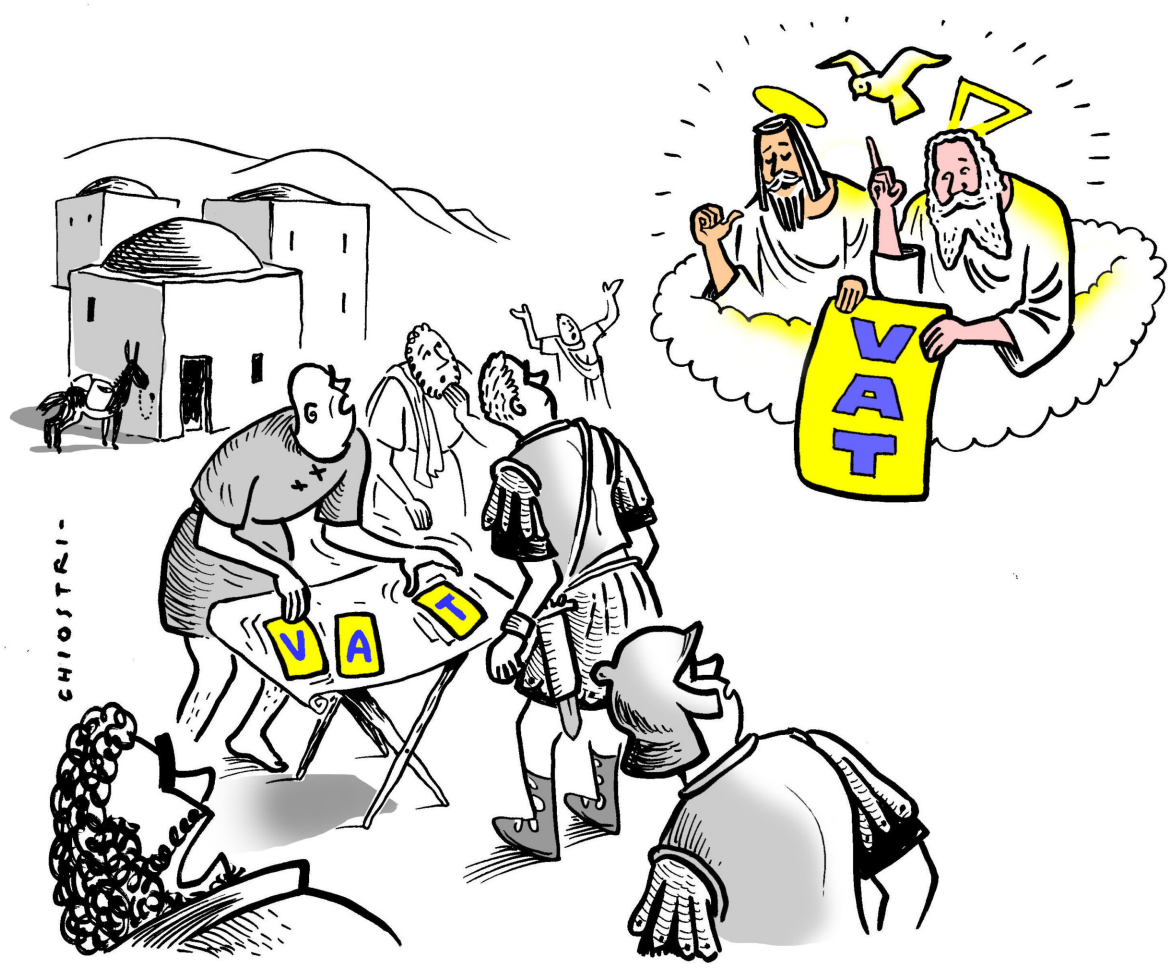
The CJEU's reasoning implies that the members are also recipients of one supply, which cannot be split into several supplies to individual members. All the members of the VAT group benefit from that one indivisible supply. If all the members of the VAT group were, therefore, members of the

cost-sharing group (and assuming that all other conditions, including that of activity in the public interest by all the members of the group, would be fulfilled), the cost-sharing exemption would be applicable. The members would acquire the services through the VAT group, and, therefore, even though the formal acquirer would be separate from the members' taxable person, the exemption would apply. It is only because one of the members of the VAT group was not at the same time a member of the cost-sharing group, which made the exemption inapplicable in *Kaplan*. Application of the exemption would mean that also a non-member benefits from it, which would be against the purpose of Article 132(1)(f).[12] The consequences of this shifting between unity and plurality mean that, on the one hand, the membership in VAT group does not cause the spreading of the membership in cost-sharing to all the members, and, on the other hand, it causes the spreading of a supply of services to all the members.

Conclusions

Kaplan case is one of several cases on the interpretation of Article 132(1)(f) decided by the CJEU in recent years. It arguably provides for another step forward in a clarification of the scope of application of the cost-sharing exemption and its correlation with the VAT grouping provision. The judgment opens up a possibility to benefit from the exemption to members of VAT groups, where all these members are also members of a cost-sharing group.

There is a certain paradox in the reasoning of the CJEU, which sees a VAT group as one person but of a pluralistic nature, and hence at the same time several persons. It reminds me of the Christian doctrine of Trinity. Perhaps to those who have strong faith in the CJEU, the reasoning in *Kaplan* makes perfect sense. You simply need to accept that in the VAT theme park, one is not always one but, sometimes, can be two or three.



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[1] C-77/19, *Kaplan International Colleges UK*, EU:C:2020:934.

[2] Both issues have been subject to analysis by VAT Committee, *see* especially Working Paper no 856 and Working Paper no 883.

[3] Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax.

[4] Cases 348/87, *Stichting Uitvoering Financiële Acties od Staatssecretaris van Financiën* (SUFA) EU:C:1989:246; C-8/01 *Taksatorringen*, EU:C:2003:621; C-407/07, *Stichting Centraal Begeleidingsorgaan voor de Intercollegiale Toetsing*, EU:C:2008:713; C-274/15, *Commission v Luxembourg*, EU:C:2017:333; C-326/15, *DNB Banka*, EU:C:2017:719; C-605/15 *Aviva*, EU:C:2017:718; C-616/15 *Commission v Germany*, EU:C:2017:721; C-400/18 *Infohos*, EU:C:2019:992; and *Kaplan*.

[5] C-274/15, *Commission v Luxembourg*, EU:C:2017:333.

[6] C-162/07, *Ampliscientifica and Amplifin*, EU:C:2008:301.

[7] Lord Justice Sedley's decision in the UK case *Royal & Sun Alliance v C&E Commissioners* (Court of Appeal) 2001.

[8] C-7/13, *Skandia America (USA)*, EU:C:2014:2225.

[9] *See* also the VAT Committee's position expressed in Working Paper no 856 and Working Paper no 883.

[10] This is a necessary consequence of the CJEU's findings in C-7/13 – *Skandia America (USA)*.

[11] Opinion of AG Mischo in C-348/87, *SUFA*, EU:C:1989:16, para. 16.

[12] In *Infohos*, the CJEU confirmed that the fact that other than member persons also receive services from the cost-sharing group does not render the exemption inapplicable to the supplies to the members. In case of VAT group, there is however only one supply, which cannot be split to be partly taxed and partly exempt.

[13] Thomas Jefferson, Letter to Francis Adrian Van der Kemp on 30 July 1810 denouncing the Christian doctrine of the Trinity.

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