

## SETTING THE BOUNDARIES: THE SCOPE OF VAT EXEMPTIONS

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### 1 Introduction

It is fair to say that the European VAT system is more harmonised than not, although we are still in a transitional period which the Sixth VAT Directive<sup>2</sup> contemplated would end years ago. Whether there will ever be a truly common system of VAT remains to be seen. Even if harmonisation meant that VAT operated in exactly the same way throughout the Member States, it would not put an end to all territorial disputes. Frontiers will continue to be disputed, although these borders will be legal rather than geographical and arise from the implementation and interpretation of the VAT Directives. The European Court of Justice ("the Court") has played, and will continue to play, a crucial role in defining and policing these frontiers. An area which has already provided plenty of opportunity for legal argument is the meaning and scope of Article 13 of the Sixth VAT Directive ("Art 13"), which sets out the various exemptions from VAT. This article identifies some guiding principles which the Court has laid down for itself and the national courts, and then considers how those have been applied in relation to the exemptions under Art 13.

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<sup>2</sup> Sixth Council Directive of 17 May 1977 (77/388/EC)

## 2 Guiding Principles

### 2.1 Strict Construction

On many occasions the Court has stressed that Art 13 must be construed strictly.<sup>3</sup> This is because the exemptions constitute “*independent concepts of Community law whose purpose is to avoid divergences in the application of the VAT system from one Member State to another.*”<sup>4</sup> The general principle underlying the common VAT system is that turnover tax is levied on all services supplied for consideration by a taxable person. As exemptions constitute exceptions to that general principle, the terms used to specify those exemptions should be interpreted strictly.<sup>5</sup>

### 2.2 Margin of Appreciation

Nevertheless, as Advocate-General Cosmas stated in his Opinion in *Gregg*,<sup>6</sup> the restrictive construction of an exemption is not an end in itself, nor can it undermine the logic of the system that the rule requiring interpretation is endeavouring to establish. Because the language of the Sixth Directive is not wholly clear and consistent there is an “inherent incapacity of the terminology - where synonymous terms are sought in many different languages - to express a constantly changing reality and to stamp legal concepts with a clear inter-state and durable character”.<sup>7</sup> The task of interpreting the provisions cannot be accomplished “by drawing arguments from the wording of the provisions at issue and comparing them with each other. Instead of adhering to the superficial content of the Sixth Directive, it is preferable to seek its true meaning by treating it as an aggregate rational system of rules”.<sup>8</sup> There is therefore a margin of appreciation which allows a rule to be

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<sup>3</sup> *EC Commission v Germany* (Case 107/84) [1985] ECR 2655 at 2668, *Stichting Uitvoering Financiële Acties v Staatssecretaris van Financiën* [1989] ECR 1737 at 1752–1753, *Builthuis-Griffioen v Inspecteur der Omzetbelasting* (Case C-453/93) [1995] ECR I-2341; [1995] STC 954

<sup>4</sup> Para 15 of *Card Protection Plan v Commissioners of Customs and Excise* (Case C-349/96) [1999] ECR I-973 [1999] STC 270 at 291 para 11

<sup>5</sup> *Stichting Uitvoering Financiële Acties v Staatssecretaris van Financiën* (*supra*) at 1753.

<sup>6</sup> *Gregg v Commissioners of Customs and Excise* (Case C-216/97) [1999] ECR I-4947; [1999] STC 934; [1999] All ER (EC) 775, Court points 11 and 23

<sup>7</sup> *Ibid* point 9.

<sup>8</sup> *Ibid* point 11.

construed in a way which remedies shortcomings in its wording. This margin is limited because the result must not produce an interpretation which attributes a meaning to a legal term that is completely different from the meaning it bears when used in daily life or in another legal context. As the A-G stated, "the particular legal definition of a term may not go completely beyond its hitherto commonly accepted subject-matter".<sup>9</sup>

### 2.3 Diverging Texts

One of the inevitable issues with which the Court has to grapple is the difference in the texts in the various languages of the Member States. It is now settled case law<sup>10</sup> that the wording used in one language version of a Community provision cannot serve as the sole basis for the interpretation of that provision. Nor can one language version be made to override the others, because such an approach would be incompatible with the need for the uniform application of Community law. In the event of divergence between the language versions, "*the provision in question must be interpreted by reference to the purpose and general scheme of the rules of which it forms a part*".<sup>11</sup>

### 2.4 Conditions Under Art 13A.2(a)

The exemptions in Art 13A.1(b), (g), (h), (i), (l), (m) and (n) are subject to certain overriding conditions which are set out in Art 13A.2(a).<sup>12</sup> These conditions have their own independent meaning in Community law,<sup>13</sup> in the same way as the exemptions, but they do not in any way affect the definition of the subject matter of the exemptions envisaged by that provision.<sup>14</sup>

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<sup>9</sup> *Ibid* para 12.

<sup>10</sup> *Milk Marketing Board of England and Wales v Cricket St Thomas Estate* (Case C-372/88) [1990] ECR I-1345, paragraph 19; *Institute of the Motor Industry v Commissioners of Customs and Excise* (Case C-149/97) [1998] STC 1219, EC, *EC Commission v United Kingdom* (Case 100/84) [1985] ECR 1169 at 1182, para 17, *EC Commission v Denmark* (Case C-100/90) [1991] ECR I-5089 at 5105, para 8, and *Rockfon A/S v Specialarbejderforbundet i Danmark* [1995] ECR I-4291 at 4317, para 28.

<sup>11</sup> *Milk Marketing Board of England and Wales v Cricket St Thomas Estate* (supra).

<sup>12</sup> See Appendix

<sup>13</sup> *Bulthuis Griffioen*, (supra) para 18.

<sup>14</sup> *EC Commission v Spain* (Case C-124/96) [1998] STC 1237; [1998] ECR I-2501, Court, para 11.

## 2.5 The Person Making the Supply

Exemption under some of the provisions of Art 13A.1, (e.g. points (b) and (g)) depends on the person who is making the supply rather than the nature of the services supplied. In one case,<sup>15</sup> the Court held that supplies made by an individual running a day nursery were not exempt because Art 13 A.1 (g)<sup>16</sup> refers expressly to the concept of 'body' or 'organisation', and, "the exemption may be claimed only by legal persons [rather than] natural persons including traders".<sup>17</sup> In the later case of *Gregg*,<sup>18</sup> however, the Court took a less restrictive view. The Advocate-General commented:

"I consider that tailoring different tax treatment to the personality of the operator of the activity and consequently the alteration of conditions of competition on the sole basis of the legal guise of that activity is to be avoided; it does not fit in with the logic of the tax system as it stands nor is it in keeping with the actual intention of the draftsman of the Sixth Directive."<sup>19</sup>

He then distinguished *Bulthuis-Griffioen* (in which he had also given his Opinion) on the narrow ground that there was evidence that there was "*an essential merging of the nursery with the teacher who ran it*"<sup>20</sup> so that the operator was, ultimately, a natural person rather than an entity which fulfilled the characteristics of a "body" or "organisation". The Court was more robust and held that, notwithstanding *Bulthuis-Griffioen*, the terms "*establishments*" in Art 13A.1(b) and "*organisations*" in Art 13A.1(g) were "*in principle sufficiently broad to include natural persons as well...It may be inferred that, in employing those terms, the Community legislature did not intend to confine the exemptions referred to in that provision to the activities carried on by legal persons, but meant to extend the scope of those exemptions to activities carried on by individuals. It is true that the terms 'establishment' and*

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<sup>15</sup> *Bulthuis-Griffioen v Inspecteur der Omzetbelasting Bulthuis-Griffioen v Inspecteur der Omzetbelasting* (Case C-453/93) [1995] ECR I-23 41; [1995] STC 954.

<sup>16</sup> See Appendix.

<sup>17</sup> *Bulthuis-Griffioen* (supra) para 20.

<sup>18</sup> *Gregg and another v Commissioners of Customs and Excise* (Case C-216/97) [1999] STC 933.

<sup>19</sup> *Ibid* point 28.

<sup>20</sup> *Ibid* point 30.



'organisation' suggest the existence of an individualised entity performing a particular function. Those conditions are, however, satisfied not only by legal persons but also by one or more natural persons running a business."<sup>21</sup> The Court commented that its view was consistent with the principle of fiscal neutrality, which would be frustrated if the benefit of the exemption in Art 13A.1 (b) and (g) was dependent on the legal form in which the taxable person carried on his activity. It may, therefore, be safely assumed that the approach taken in *Gregg* is now of limited application.

## 2.6 Transitional Measures

During the "transitional period",<sup>22</sup> Art 28.3(a) of the Sixth Directive permits Member States to continue to exempt certain of the transactions in Art 13. These transactions are set out in Annex E to the Sixth Directive<sup>23</sup> (as amended by Art 1(1) of the Eighteenth Directive with effect from 1st January 1990).<sup>24</sup> In addition, Art 28(3)(b) permits Member States to continue to tax certain transactions which are contained in Art 13, under the conditions existing in the Member State concerned. These are set out in Annex F to the Sixth Directive,<sup>25</sup> (as amended by the Eighteenth Directive).<sup>26</sup> These transitional provisions must also be construed strictly.<sup>27</sup>

## 2.7 No New Exemptions

The Court has ruled on several occasions that there can be no new exemptions because the wording of Art 28.3(b) precludes the introduction of new exemptions or any extension of the scope of existing exemptions.<sup>28</sup>

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<sup>21</sup> *Ibid* paras 17 and 18.

<sup>22</sup> See Appendix.

<sup>23</sup> See Appendix.

<sup>24</sup> See Appendix.

<sup>25</sup> See Appendix.

<sup>26</sup> See Appendix.

<sup>27</sup> Point 21 of the A-G's Opinion in *EC Commission v Germany* (Case C-74/91).

<sup>28</sup> *EC v Commission v Germany* (Case C-74/91) para 15, *Kerrutt v Monchen Gladbach-Mitte* (Case C-73/85) [1986] ECR 2219 at 2238 para 17, *EC Commission v Spain* (Case C-35/90) [1991] ECR I-5073 at 5085-6 paras 6-9.

## 2.8 Abolition of Existing Exemptions

On the other hand, there is no prohibition on the abolition or reduction of the transitional exemptions retained under Art 28.3(b) because the abolition of such transitional measures is the objective of Art 28.4 of the Sixth Directive.<sup>29</sup>

## 2.9 Travaux Préparatoires

As with any other provision of EC law, it is possible to rely on the preparatory material which led to the adoption of a provision to discern the intention of the legislature in framing it. An example of this approach was in the case of *Institute of the Motor Industry*.<sup>30</sup>

# 3 The Extent of Exemption for Activities in the Public Interest Under Art 13a

## 3.1 Postal Services

Art 13A.1(a) exempts “*the supply by the public postal services of services other than passenger transport and telecommunications services, and the supply of goods incidental thereto.*” In order to fall within this exemption the services must be provided by the organisation claiming exemption. In *EC Commission v Germany*<sup>31</sup> the Court held that, in an early example of outsourcing, a business which delivered mail from one post office to another, without coming into contact with the public, could not claim exemption. This was because, although some language versions could be interpreted as referring to all postal services, it was clear from the syntax of Art 13A.1(a) that the services had to be provided by the public postal service itself.

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<sup>29</sup> *Ideal Tourism v Belgian State* (Case C - 36/99) para 32.

<sup>30</sup> *Institute of the Motor Industry v Commissioners of Customs and Excise* (Case C-149/97) [1998] ECR I-7053; [1998] STC 1219.

<sup>31</sup> *EC Commission v Germany* (Case 107/84) [1985] ECR 2655.

### 3.2 Hospital and Medical Care

The exemptions for hospital and medical care are set out in Art 13A.1(b)<sup>32</sup> and (c).<sup>33</sup> The Court commented in one case<sup>34</sup> that the services in Art 13A.1(b) “*encompass a whole range of medical care normally provided on a non-profit-making basis in establishments pursuing social purposes such as the protection of human health.*”<sup>35</sup> Although Art 13A.1(b) of the Sixth Directive does not include any definition of the concept of activities closely related to hospital and medical care, that concept does not require an especially narrow interpretation. This is because “*the exemption of activities closely related to hospital and medical care is designed to ensure that the benefits flowing from such care are not hindered by the increased costs of providing it that would follow if it, or closely related activities, were subject to VAT.*”<sup>36</sup> The Court has also noted that it “*is clear from the position of [Art 13A.1(c)]... directly following the indent concerning hospital care, and from its context, that the services involved are provided outside hospitals and similar establishments and within the framework of a confidential relationship between the patient and the person providing the care, a relationship which is normally established in the consulting room of that person.*”<sup>37</sup> These provisions have given rise to a variety of cases, most of which tell us what is not, rather than what is, exempt. They fall into several categories.

#### 3.2.1 Supplies by Veterinary Surgeons

Supplies by veterinary surgeons do not fall within the exemption. This is because all the language versions of Art 13A.1(c) except the English and Italian expressly limit the exemption to the provision of care to “persons”.<sup>38</sup> Moreover, as the Advocate-General pointed out, “*the context in which the exemption at issue is placed... appears to confirm... that it was intended to cover a set of activities of a particular*

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<sup>32</sup> See Appendix.

<sup>33</sup> See Appendix.

<sup>34</sup> *EC Commission v United Kingdom* (C-353/85) [1998] STC 251.

<sup>35</sup> *Ibid*, para 32.

<sup>36</sup> *EC Commission v France* (Case 76/99), paras 22 and 23.

<sup>37</sup> *EC Commission v United Kingdom* (supra) para 33.

<sup>38</sup> *EC Commission v Italy* (C-122/87) ECR 1998 2685 at para 9.

*social and human dimension, connected with human health*".<sup>39</sup> In addition, the inclusion of veterinary services in Art 23.3 (b) and Annex F (until it was amended by the Eighteenth Directive) indicates that it was not intended to include those services in the common list of exemptions in Art 13.

### 3.2.2 Expert Medical Evidence

The term "provision of medical care" in Art 13A.1(c) of the Sixth Directive only applies to medical services which provide care to persons by diagnosing and treating a disease or any other health disorder. The services of a doctor who was ordered by a court to provide expert evidence establishing the genetic affinity of individuals were, therefore, not exempt.<sup>40</sup>

### 3.2.3 Transmission of Medical Samples

The transmission of a medical sample, by the laboratory which took it, to another specialised laboratory for the purpose of analysis, falls within Art 13A.1(b). This is because those services are closely related to the analysis, so that they must be treated in the same way as the analysis for fiscal purposes and, accordingly, must not be subject to VAT.<sup>41</sup>

### 3.2.4 The Supply of Goods by the Medical and Paramedical Professions

In *EC Commission v United Kingdom*<sup>42</sup>, the Court held that the supplies of medicines and other goods, such as corrective spectacles prescribed by a doctor or by other authorised persons, are not within Art 13A.1(c), apart from minor provisions of goods which are strictly necessary at the time when the care is provided and physically and economically dissociable from the supply. The Court pointed out that, although Art 13 grants exemption in certain cases where the supply of goods is connected with the provision of services, it expressly lists the cases in which the supply of goods is exempt. This is because such exemptions derogate from the general principle laid down by Art 2(1) of the Sixth Directive that all supplies of goods or services should be subject to value added tax. Because, unlike other provisions such as Art 13A.1(e), Art 13A.1(c) does not expressly mention supplies

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<sup>39</sup> *Ibid* points 21 and 22 of the A-G's Opinion.

<sup>40</sup> *D v W* (C-384/98).

<sup>41</sup> *EC Commission v France* (Case 76/99).

<sup>42</sup> (Case C-353/85) [1988] STC 250.

of goods, it is not intended to include the supply of goods.<sup>43</sup>

### 3.4. Welfare Services

As discussed in paragraph 2.5 above, the Court seems to have gone back on its restrictive interpretation of Art 13A.1(g) and to have come to the conclusion that the exemption for “*the supply of services and of goods closely linked to welfare and social security work, including those supplied by old people’s homes, by bodies governed by public law or by other organisations recognised as charitable by the Member State concerned,*” can apply to one or more natural persons running a business, such as a partnership.<sup>44</sup>

### 3.5 Trade Unions

The meaning of the term “trade union”, in Art 13A.1(l)<sup>45</sup> was considered in *Institute of the Motor Industry*<sup>46</sup>. The Court concluded that the expression ‘trade-union’ in that provision means specifically an organisation whose main object is to defend the collective interests of its members, whether they are workers, employers, independent professionals or traders carrying on a particular economic activity, and to represent them vis-à-vis the appropriate third parties, including the public authorities.”<sup>47</sup> This will include a “*non-profit-making organisation whose main object is to defend and represent the collective interests of its members... in so far as it provides its members with a representative voice and strength in negotiations with third parties*”.<sup>48</sup>

### 3.6 Services Closely Linked to Sport

The exemption under Art 13A.1(m)<sup>49</sup> for supplies closely linked to sport or physical

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<sup>43</sup> *Ibid* para 35.

<sup>44</sup> *Gregg and another v Commissioners of Customs and Excise* (Case C-216/97 ) *supra* (EC).

<sup>45</sup> See Appendix.

<sup>46</sup> (Case C-149/97) [1998] ECR I-7053; [1998] STC 1219.

<sup>47</sup> *Ibid* para 20.

<sup>48</sup> *Ibid* para 21.

<sup>49</sup> See Appendix.

education cannot be limited to private establishments whose membership fees do not exceed a certain amount<sup>50</sup>. As has already been discussed in paragraph 2.4 above, the conditions under Art 13.2(a) that the supplier should not systematically aim to make a profit did not permit the imposition of such a limitation. On the other hand, however, the exemption cannot apply to profit making organisations.<sup>51</sup>

#### 4 The Extent of the Exemptions Under Article 13B

##### 4.1 Insurance and Reinsurance Transactions

Art 13B(a) exempts “*insurance and reinsurance transactions, including related services performed by insurance brokers and insurance agents*”.

##### 4.1.1 Meaning of Insurance Transactions

The Court has taken the view that there is no reason for the interpretation of the term “insurance” to differ according to whether it appears in the Directives on insurance<sup>52</sup> or in the Sixth Directive although neither Directive defines the expression<sup>53</sup>. The essentials of an insurance transaction are that “*the insurer undertakes, in return for a prior payment of a premium, to provide the insured, in the event of the materialisation of the risk covered, with the service agreed when the contract was concluded*”<sup>54</sup>. It is not essential that the service the insurer has undertaken to provide in the event of loss consists in the payment of a sum of money, as that service may also take the form of the provision of assistance in cash or in kind of the types listed in the Insurance Directive.<sup>55</sup> The expression “insurance transactions” “*covers in any event cases where the transaction is carried out by the*

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<sup>50</sup> *Commission v Spain* (Case C-124/96).

<sup>51</sup> *Stockholm Lindöpark Actiebolag v Swedish State* (Case C-150/99) para 19.

<sup>52</sup> EC Council Directive 73/239 of 24 July 1973 on the co-ordination of laws, regulations and administrative provisions relating to the taking-up and pursuit of the business of direct insurance other than life insurance (OJ L228 16.8.73 p 3), as amended by EC Council Directive 84/641 of 10 December 1984 (OJ L339 27.12.84 p 21).

<sup>53</sup> *Card Protection Plan Ltd v Commissioners of Customs and Excise Commissioners* (Case C-349/96)[1999] STC 270; [1999] 2 AC 601.

<sup>54</sup> *Ibid* para 17.

<sup>55</sup> *Ibid* para 18.

*actual insurer who has undertaken to cover the risk insured against*".<sup>56</sup>

#### 4.1.2. The Insurance Provider

The term "insurance transactions" also includes the provision of insurance cover by a taxable person who is not himself an insurer but, in the context of a block policy, procures such cover for his customers by making use of the supplies of an insurer who assumes the risk insured.<sup>57</sup> The Sixth Directive exempts insurance transactions but gives Member States, in Art 33, the possibility of maintaining or introducing a tax on insurance contracts. Consequently, "*if 'insurance transactions' refers solely to transactions performed by insurers themselves, the final consumer might have to pay not only that tax but also VAT, in the case of block policies. Such a result would be contrary to the purpose of the exemption provided for by Art 13B(a)*".<sup>58</sup> Nevertheless, there must be a contractual relationship between the beneficiary of the insurance service and the person whose risks are covered by the insurance, i.e. the insured. Thus, a co-operative arrangement under which one insurance company ran the business of another insurance company in return for remuneration at market rates, but without assuming the related liabilities, when the latter company concluded insurance contracts in its own name, was held not to constitute an insurance transaction within the meaning of Art 13B(a) of the Sixth Directive.<sup>59</sup>

#### 4.2 Leasing or Letting of Immovable Property

##### 4.2.1 The Meaning of Leasing or Letting

In common with most of the exemptions in Art 13, there is no definition of "letting and leasing of immovable property" in Art 13B(b). As the Court has commented, "*the wording of [the] article...does not shed any light on the scope of the terms leasing or letting of immovable property*".<sup>60</sup> In *Stockholm-Lindöpark* the Advocate-General observed that in order to qualify for exemption under Article 13B(b) of the

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<sup>56</sup> *Ibid* para19.

<sup>57</sup> *Ibid* para 22 .

<sup>58</sup> *Ibid* 23.

<sup>59</sup> Case C-240/99 *Försäkringsaktiebolaget Skandia (publ)*.

<sup>60</sup> *Commission v United Kingdom* (Case C-359/97) [2000] ECR I-6355 [2000] STC 777, paragraph 65, and *Commission v Ireland* (Case C-358/97) [2000] ECR I-6301, paragraph 53.

Sixth Directive, a contract must possess “*the essential characteristics of a lease or let, which include the grant of a right to occupy a defined piece or area of immovable property as one's own and to exclude or admit others, and an agreement between the parties taking account of the duration of that occupation, in particular as a criterion for determining the price; such characteristics must, moreover, predominate in the contract*”.<sup>61</sup> The Court took the same view in *EC Commission v United Kingdom* and held that “*the term cannot be considered to cover contracts where...the parties have not agreed on any duration for the right of enjoyment, which is an essential element of a contract to let*”.<sup>62</sup>

#### 4.2.2 Surrenders of Leases

If a lease is exempt within Art 13B(b) the surrender of that lease will also be exempt. This is because a change in the contractual relationship arising from a transaction which is an exempt supply, such as termination of the lease for consideration, must also be regarded as falling within the scope of that exemption.<sup>63</sup> As the Advocate-General commented in the recent case of *Mirror Group plc*, “*the crucial factor for the Court appears to have been that the purpose of the contract was to pass the right to enjoy the property back to the landlord; that is to say, it served the same purpose as the original contract, even though the right was transferred in the opposite direction*”.<sup>64</sup>

#### 4.2.3 Inducements

The liability of the supply made when a landlord pays a prospective tenant an inducement to enter into a lease, or to take an assignment of a lease, is still being considered by the Court.<sup>65</sup> In his Opinion in *Mirror Group plc* the Advocate-General accepted the reasoning in *Stockholm-Lindöpark* (set out in paragraph 4.2 above) that the characteristics of a lease or let must predominate in the contract for it to come

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<sup>61</sup> Supra point 31 of the Opinion.

<sup>62</sup> Supra para 68.

<sup>63</sup> *Lubbock Fine & Co v Commissioners of Customs and Excise* (Case C-63/92) [1993] ECR I-6665.

<sup>64</sup> *Mirror Group plc v Commissioners of Customs and Excise* (Case C-409/99) point 32 of the Opinion.

<sup>65</sup> *Mirror Group plc v Commissioners of Customs and Excise* (supra) and *Cantor Fitzgerald International v Commissioners of Customs and Excise* (Case C-108/99).



within the exemption.<sup>66</sup> It was then necessary to identify “*the element which the legal traditions of various European countries term the cause of the contract and understand as the economic purpose, calculated to realise the parties’ respective interests, lying at the heart of the contract*”.<sup>67</sup> In the case of a lease, this was the transfer by one party to another of an exclusive right to enjoy immovable property for an agreed period. Following those principles, he came to the conclusion that the transactions were exempt because the purpose of the whole transaction was to transfer the right of enjoying the immovable property from the landlord to the tenant. In *Cantor Fitzgerald International*,<sup>68</sup> the Advocate-General adopted the same reasoning in relation to an inducement to accept the assignment of a lease. He advised the Court that the assignment of a lease by a tenant to a third person, in return for the payment by the tenant to that person is also exempt under Art 13B(b) because the overall transaction was to “*vary the original lease, in terms of the identity of the parties thereto*”.<sup>69</sup>

#### 4.2.4 Road Tolls

In a series of judgments,<sup>70</sup> the Court has considered the liability of road tolls. In *EC Commission v United Kingdom*<sup>71</sup> the UK sought to argue that road tolls were exempt under Art 13B(b). The Court refused to accept that argument because Art 13 was to be interpreted strictly, and the agreement between the provider and the user did not include a limit on the duration of the user’s right of enjoyment, which was an essential element of a letting contract.

#### 4.2.5 Exclusions from Exemption

Article 13B(b) contains certain exclusions from the exemption for the leasing or

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<sup>66</sup> *Mirror Group plc v Commissioners of Customs and Excise* (supra) point 25 of the Opinion.

<sup>67</sup> *Ibid* point 28.

<sup>68</sup> *Supra*.

<sup>69</sup> *Ibid* point 47 of the Opinion.

<sup>70</sup> *EC Commission v UK* (Case C-359/97), in *EC Commission v France* (Case C-276/97) and *EC Commission v Ireland* (Case C-358/97), but in *EC Commission v Netherlands* (Case C-408/97) and *EC Commission v Greece* (Case C-260/98) the Court dismissed the Commission’s actions, on the ground that in those Member States the tolls were operated exclusively by bodies governed by public law.

<sup>71</sup> *Supra*.

letting of immovable property.<sup>72</sup> The Court has examined the scope of these exclusions in a number of cases.

#### 4.2.5.1 Short Term Accommodation

The Court has held that Member States have a margin of discretion in setting the criteria for distinguishing “*dwelling accommodation*” from “*accommodation in the hotel sector or in sectors with a similar function*”. Duration of the letting is “*an appropriate criterion of distinction*”.<sup>73</sup> The exception from exemption under German law for all accommodation let for less than six months was therefore permissible. As a result, it was not contrary to Art 13B(b) to tax the provision of accommodation for refugees under agreements which were for less than six months, even though the accommodation was residential and the refugees could, and did, stay for longer than six months.

#### 4.2.5.2 Tents, Caravans and Mobile Homes

The exclusion in Art 13B(b) 1 was considered by the Court in the case of *EC Commission v France*.<sup>74</sup> The Court held that France had infringed Art 2 of the Sixth Directive by exempting certain caravans, tents, mobile homes and light framed leisure dwellings which were fixed installations, even though they had been specially adapted for residence and were used exclusively as living quarters.

#### 4.2.5.3 Garages

Art 13B(b) 2 expressly excludes from the exemption “*the letting of premises and sites for parking vehicles*,” a phrase which was considered in the case of *Henriksen*.<sup>75</sup> Because the different wording in the various language versions of Art 13B(b) 2 did not make it clear whether the exclusion was restricted to sites for parking vehicles, or could include closed garages, “*recourse must therefore be had to the context in which it occurs and the structure of the Sixth Directive*”.<sup>76</sup> As the provision is an exception to an exemption, it must not be construed restrictively, and

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<sup>72</sup> See Appendix.

<sup>73</sup> *Blasi v Finanzamt München* (Case C-346/95) [1998] ECR I-481; [1998] STC 336, para 23.

<sup>74</sup> (Case C-60/96) [1999] STC 480.

<sup>75</sup> *Skatteministeriet v Henriksen* (Case C-173/88) [1990] STC 768; [1989] ECR 2763.

<sup>76</sup> *Ibid* para 11.

so must be taken to include both open parking spaces and closed garages. Nevertheless, the Court concluded that the letting of garages, which had been built in conjunction with a development of thirty-seven houses, did not fall within the exclusion. This was because the phrase “*leasing or letting of immovable property*”, in Art.13B (b) of the Sixth Directive encompassed, in addition to the letting of the property which is the subject of an exempt letting, the letting of all property which is accessory to that property.<sup>77</sup> The Court came to this conclusion even though the garages were not in the same ownership as the houses, because the fact that the parking place and the houses were part of a single complex meant that the two lettings constituted “*a single economic transaction*”.<sup>78</sup> The Court observed that the same reasoning would apply if the letting of the houses and the garages was by the same person. It is interesting to speculate whether, in the light of the cases such as *Blasi*<sup>79</sup> and *EC Commission v France*;<sup>80</sup> the same conclusion would have been reached today.

#### 4.3 The Granting of Credit

Article 13B (d) 1 exempts “*the granting and the negotiation of credit and the management of credit by the person granting it*”. In *Muys’ en De Winter’s Bouw-en Aannemingsbedrijf BV v Staatssecretaris van Financien*<sup>81</sup> the Court held that the term “granting of credit” is sufficiently broad to encompass credit granted by a supplier of goods in the form of deferral of payment, provided that the contractual arrangements and terms are such that the credit transaction is clearly dissociable from the main supply of goods. The Court commented, “*the wording of the provision in no way suggests that there is any limitation on the scope of Art 13B(d) 1 only to loans and credits guaranteed by banking and financial institutions*”.<sup>82</sup> That interpretation is borne out by the aim of the common system of VAT, which aims to secure equal treatment for taxable persons. “*That principle would be disregarded if a purchaser were to be taxed on credit granted by his supplier, whereas a purchaser seeking credit from a bank or another lender received an exempted*

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<sup>77</sup> *Ibid* para 14.

<sup>78</sup> *Ibid* paras 15 and 16.

<sup>79</sup> *Supra*.

<sup>80</sup> *Supra* .

<sup>81</sup> (Case C-281/94) [1993] ECR I-5405; [1997] STC 664.

<sup>82</sup> *Ibid* para 13.

*credit.*"<sup>83</sup> Nevertheless, there can only be exemption when there is a deferral of payment which has become due. If "interest" is charged before delivery, when the purchase price would normally become payable, it must be included in the consideration under Art 11A(1)(a)<sup>84</sup> as it is consideration for the goods, not for a supply of credit.

#### 4.4 Outsourced Transactions Under Art 13B(d) 3 and 5<sup>85</sup>

In *Sparekassernes Datacenter (SDC) v Skatterministeriet*,<sup>86</sup> the Court considered the scope of Art 13B(d) 3 and 5 in the context of services which had been outsourced by a bank to a data-handling centre, and set out the following important principles.

##### 4.4.1 The Person Providing the Services

The transactions exempted are defined according to the nature of the services provided rather than the person providing them. The provisions do not, in contrast to Art 13B(d) 1 and 2, refer to the person providing the services and for that reason the legal identity of that person is irrelevant.<sup>87</sup>

##### 4.4.2 The Manner in which the Services are Provided.

In the same way, Art 13B(d) 3 and 5 make no reference to the manner in which the services are performed, and so whether they be delivered electronically, automatically or manually does not affect the application of the exemption.<sup>88</sup>

##### 4.4.3 The Relationship with the Customer

The services need not be supplied by an institution which has a legal relationship with the customer and a transaction can still be exempt if it is a service performed by a third party which appears to the customer to be a service provided by the bank.

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<sup>83</sup> *Ibid* para14.

<sup>84</sup> See Appendix.

<sup>85</sup> See Appendix.

<sup>86</sup> (Case C-2/95) [1997] ECR I-3017; [1997] STC 932.

<sup>87</sup> *Ibid* paras 31 to 35.

<sup>88</sup> *Ibid* para 37.

The Court observed that “a transfer is a transaction consisting of the execution of an order for the transfer of a sum of money from one bank account to another. It is characterised in particular by the fact that it involves a change in the legal and financial situation existing between the person giving the order and the recipient and between those parties and their respective banks and, in some cases, between the banks. Moreover, the transaction which produces this change is solely the transfer of funds between accounts, irrespective of its cause”. As a transfer is only a means of transmitting funds, “the functional aspects are decisive for the purpose of determining whether a transaction constitutes a transfer for the purposes of the Sixth Directive.”<sup>89</sup> The wording of Art 13B(d) 3 is sufficiently wide to include services provided by operators other than banks to persons other than their customers. When a data-handling centre or a third party effects a transfer for a customer of the bank, without any involvement of the bank, perhaps under a standing order or at the customer’s request, the customer’s right to have those transactions effected derives from his contractual links with the bank. This is so even if the services provided by the data-handling centre or the third party are invoiced as services provided to the bank.<sup>90</sup>

#### 4.4.4 The Nature of the Services

In order to fall within the exemption, the services must be distinct in character and must be specific to and essential for the exempt transaction. In order for there to be an exempt transaction concerning transfers, the services provided must therefore have the effect of transferring funds and entail changes in the legal and financial situation. An exempt service must be distinguished from a mere physical or technical supply, such as making a data-handling system available to a bank. As the Advocate-General commented in his Opinion, “the institutions effecting the transfers offer their customers a specific financial service consisting in facilitating a movement of capital, a service which is exempted by the Sixth Directive. The fact that, for performing that service they are obliged to use certain technical or material means or the services of third persons (undertakings providing telecommunications, transport of money, postal services, computer services, legal advice and other services) must not lead to the confusion between the exempt transaction as such and the technical auxiliary services which make possible, to which that exemption does not extend... It is therefore inappropriate to apply the exemption to ...instrumental

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<sup>89</sup> *Ibid* para 53.

<sup>90</sup> *Ibid* para 55 .

*functions [such as data-handling which does not effect the credit transfer].*"<sup>91</sup>

#### 4.4.5 The Provision of Information

The provision of financial information does not fall within Art 13B(d) 3 and 5.<sup>92</sup>

#### 4.4.6 Invoicing

In *SDC* the services were performed by a third party which invoiced them to SDC which in turn invoiced them to the banks. The Court held that, provided the service is specified, it fulfils the criteria for invoicing and the invoice relates only to that service, the mere fact that, for organisational reasons, the invoicing is done through a third party does not prevent the transaction from being exempt. It was "*the legal relationship between the person providing a service and the person receiving it and the principle of mutual performance*" which were the important factors. Therefore, the supply can still be exempt if the data-handling centre, which effects the transactions, and the third party which invoices them, in reality "*constitute a unit created to serve the common interests of the persons for whom the services of the data-handling centre are intended*".<sup>93</sup>

#### 4.5 Transactions in Securities

Although the guidance in *SDC* is useful, it could be said to raise as many questions as it answers. There may be further clarification when the Court considers another reference concerning outsourced services, in this case those provided to an insurance company in relation to Personal Equity Plans.<sup>94</sup> The Court has been asked whether Art 13B(d) 5 exempts the provision of information to potential investors, and receiving and processing applications from investors for the issue of a security (but not including preparing and despatching the document of title to the security), where that service is provided to a person who has legal rights or obligations under the security by a person who does not have any such legal right or obligation.

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<sup>91</sup> *Ibid* points 72 and 73.

<sup>92</sup> *Ibid* para 76.

<sup>93</sup> *Ibid* paras 79 and 80.

<sup>94</sup> *Commissioners of Customs and Excise v CSC Financial Services Ltd (formerly Continuum)* Case C-235/00.

#### 4.6 The Supply of Land other than Building Land

Article 13B(h) exempts “*the supply of land which has not been built on other than building land as described in Article 4. 3(b)*”.<sup>95</sup> The Court has held that Art 4.3(b) refers to land, irrespective of whether or not it has been improved, which has been defined by the Member States as land intended for building. Such a definition must, however, comply with the objective of Art 13B(h) which is “*to exempt from tax only supplies of land which has not been built on and is not intended to support a building*”.<sup>96</sup>

### 5 Conclusion

It can be seen from the approach the Court has taken to the various exemptions that it has endeavoured to keep to its own guiding principles, while at the same time trying to ensure that the law remains dynamic. The tension between the necessity to retain the integrity of the tax and the requirement to reflect economic and commercial realities is brought sharply into focus by the Court’s approach to the question of outsourcing. The story is only just beginning to unfold, and it is likely that *SDC* and *CSC* will be followed by other cases involving similar issues. Even if those are resolved there will, no doubt, be other equally challenging boundary disputes on which the Court will have to adjudicate in the future. The taxation of e-commerce is an obvious example, although it is unlikely that cyberspace will prove to be the final frontier.

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<sup>95</sup> Art 4.3(b) refers to “*The supply of building land. ‘Building land’ shall mean any unimproved or improved land defined as such by the Member States*”

<sup>96</sup> *Gemeente Emmen v Belastingdienst Grote Ondernemingen* (Case C-468/93) [1996] ECR I-1195; [1996] STC 495 paras 25 and 26.

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## Appendix

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# APPENDIX

## Extracts from the Sixth Council Directive of 17 May 1997 (77/388/EC)

### Article 11A (1) provides:

*“The taxable amount shall be: (a) in respect of supplies of goods and services other than those referred to in (b), (c) and (d) below, everything which constitutes the consideration which has been or is to be obtained by the supplier from the purchaser, the customer or a third party for such supplies including subsidies directly linked to the price of such supplies.”*

### Article 13

Exemptions within the territory of the country

*A. Exceptions, for certain activities in the public interest*

1

Without prejudice to other Community provisions, Member States shall exempt the following under conditions which they shall lay down for the purpose of ensuring the correct and straightforward application of such exemptions and of preventing any possible evasion, avoidance or abuse:

- (a) the supply by the public postal services of services other than passenger transport and telecommunications services, and the supply of goods incidental thereto;
- (b) hospital and medical care and closely related activities undertaken by bodies governed by public law or, under social conditions



comparable to those applicable to bodies governed by public law, by hospitals, centres for medical treatment or diagnosis and other duly recognised establishments of a similar nature;

- (c) the provision of medical care in the exercise of the medical and paramedical professions as defined by the Member State concerned;
- (d) supplies of human organs, blood and milk;
- (e) services supplied by dental technicians in their professional capacity and dental prostheses supplied by dentists and dental technicians;
- (f) services supplied by independent groups of persons whose activities are exempt from or are not subject to value added tax, for the purpose of rendering their members the services directly necessary for the exercise of their activity, where these groups merely claim from their members exact reimbursement of their share of the joint expenses, provided that such exemption is not likely to produce distortion of competition;
- (g) the supply of services and of goods closely linked to welfare and social security work, including those supplied by old people's homes, by bodies governed by public law or by other organisations recognised as charitable by the Member State concerned;
- (h) the supply of services and of goods closely linked to the protection of children and young persons by bodies governed by public law or by other organisations recognised as charitable by the Member State concerned;
- (i) children's or young people's education, school or university education, vocational training or retraining, including the supply of services and of goods closely related thereto, provided by bodies governed by public law having such as their aim or by other organisations defined by the Member State concerned as having similar objects;
- (j) tuition given privately by teachers and covering school or university education;
- (k) certain supplies of staff by religious or philosophical institutions for the purpose of sub-paragraphs (b), (g), (h) and (i) of this Article

and with a view to spiritual welfare;

- (l) supply of services and goods closely linked thereto for the benefit of their members in return for a subscription fixed in accordance with their rules by non-profit-making organisations with aims of a political, trade-union, religious, patriotic, philosophical, philanthropic or civic nature, provided that this exemption is not likely to cause distortion of competition;
- (m) certain services closely linked to sport or physical education supplied by non-profit-making organisations to persons taking part in sport or physical education;
- (n) certain cultural services and goods closely linked thereto supplied by bodies governed by public law or by other cultural bodies recognised by the Member State concerned;
- (o) the supply of services and goods by organisations whose activities are exempt under the provisions of sub-paragraphs (b), (g), (h), (i), (l), (m) and (n) above in connection with fund-raising events organised exclusively for their own benefit provided that exemption is not likely to cause distortion of competition. Member States may introduce any necessary restrictions in particular as regards the number of events or the amount of receipts which give entitlement to exemption;
- (p) the supply of transport services for sick or injured persons in vehicles specially designed for the purpose by duly authorised bodies;
- (q) activities of public radio and television bodies other than those of a commercial nature.

2

- (a) Member States may make the granting to bodies other than those governed by public law of each exemption provided for in 1(b), (g), (h), (i), (l), (m) and (n) of this Article subject in each individual case to one or more of the following conditions:
  - they shall not systematically aim to make a profit, but any profits nevertheless arising shall not be distributed, but shall

be assigned to the continuance or improvement of the services supplied,

- they shall be managed and administered on an essentially voluntary basis by persons who have no direct or indirect interest, either themselves or through intermediaries, in the results of the activities concerned,
- they shall charge prices approved by the public authorities or which do not exceed such approved prices or, in respect of those services not subject to approval, prices lower than those charged for similar services by commercial enterprises subject to value added tax,
- exemption of the services concerned shall not be likely to create distortions of competition such as to place at a disadvantage commercial enterprises liable to value added tax.

(b) The supply of services or goods shall not be granted exemption as provided for in 1 (b), (g), (h), (i), (l), (m) and (n) above if:

- it is not essential to the transactions exempted,
- its basic purpose is to obtain additional income for the organisation by carrying out transactions which are in direct competition with those of commercial enterprises liable for value added tax.

#### *B. Other exemptions*

Without prejudice to other Community provisions, Member States shall exempt the following under conditions which they shall lay down for the purpose of ensuring the correct and straightforward application of the exemptions and of preventing any possible evasion, avoidance or abuse;

- (a) insurance and reinsurance transactions, including related services performed by insurance brokers and insurance agents;
- (b) the leasing or letting of immovable property excluding:

1 the provision of accommodation, as defined in the laws of the

Member States, in the hotel sector or in sectors with a similar function, including the provision of accommodation in holiday camps or on sites developed for use as camping sites;

- 2 the letting of premises and sites for parking vehicles;
- 3 lettings of permanently installed equipment and machinery;
- 4 hire of safes.

Member States may apply further exclusions to the scope of this exemption;

- (c) supplies of goods used wholly for an activity exempted under this Article or under Article 28(3)(b) when these goods have not given rise to the right to deduction, or of goods on the acquisition or production of which, by virtue of Article 17(6), value added tax did not become deductible;
- (d) the following transactions:
  - 1 the granting and the negotiation of credit and the management of credit by the person granting it;
  - 2 the negotiation of or any dealings in credit guarantees or any other security for money and the management of credit guarantees by the person who is granting the credit;
  - 3 transaction, including negotiation, concerning deposit and current accounts, payments, transfers debts, cheques and other negotiable instruments, but excluding debt collection and factoring;
  - 4 transactions, including negotiation, concerning currency, bank notes and coins used as legal tender, with the exception of collectors' items; "collectors' items" shall be taken to mean gold, silver or other metal coins or bank notes which are not normally used as legal tender or coins of numismatic interest;
  - 5 transactions, including negotiation, excluding management and safe-keeping, in shares, interests in companies or associations, debentures and other securities, excluding:
    - documents establishing title to goods:

- the rights or securities referred to in Article 5(3);
- 6 management of special investment funds as defined by Member States;
- (e) the supply at face value of postage stamps valid for use for postal services within the territory of the country, fiscal stamps, and other similar stamps;
- (f) betting, lotteries and other forms of gambling, subject to conditions and limitations laid down by each Member State;
- (g) the supply of buildings or parts thereof, and of the land on which they stand, other than as described in Article 4 (3)(a);
- (h) the supply of land which has not been built on other than building land as described in Article 4(3)(b).

**Article 28(4) provides that**

*“The transitional period shall last initially for five years as from 1 January 1978. At the latest six months before the end of this period, and subsequently as necessary, the Council shall review the situation with regard to the derogations set out in paragraph 3 on the basis of a report from the Commission and shall unanimously determine on a proposal from the Commission, whether any or all of these derogations shall be abolished.”*

**Annex E to the Sixth Directive**

**TRANSACTIONS REFERRED TO IN ARTICLE 28(3)(a)**

1...

2 Transactions referred to in Article 13A(1)(e).

3-6...

7 Transactions referred to in Article 13A(1)(g).

8-10...

- 11 Supplies covered by Article 13B(g) in so far as they are made by taxable persons who were entitled to deduction of input tax on the building concerned.

12-14...

- 15 The services of travel agents referred to in Article 26, and those of travel agents acting in the name and on account of the traveller, for journeys outside the Community.

The transactions referred to in points 1, 3-6, 8-10, and 12-14 were abolished by the Eighteenth Council Directive 89/465/EEC of 18 July 1989 with effect from 1st January 1990; see OJ L226, 3.8.1989, p 21.

#### **Annex F to the Sixth Directive**

##### **ANNEX F—TRANSACTIONS REFERRED TO IN ARTICLE 28(3)(b)**

- 1 Admission to sporting events.
- 2 Services supplied by authors, artists, performers, lawyers and other members of the liberal professions, other than the medical and paramedical professions, in so far as they are not services specified in Annex B to the second Council Directive of 11 April 1967.
- 3-4...
- 5 Telecommunications services supplied by public postal services and supplies of goods incidental thereto.
- 6 Services supplied by undertakers and cremation services, together with goods related thereto.
- 7 Transactions carried out by blind persons or workshops for the blind provided these exemptions do not give rise to significant distortion of competition.
- 8 The supply of goods and services to official bodies responsible for the construction, setting out and maintenance of cemeteries, graves and monuments commemorating war dead.
- 9...
- 10 Transactions of hospitals not covered by Article 13A(1)(b).

11...

12 The supply of water by public authorities.

13-15...

16 Supplies of those buildings and land described in Article 4(3).

17 Passenger transport

The transport of goods such as luggage or motor vehicles accompanying passengers and the supply of services related to the transport of passengers, shall only be exempted in so far as the transport of the passengers themselves is exempt.

18-22...23

The supply, modification, repair, maintenance, chartering and hiring of aircraft, including equipment incorporated or used therein, used by State institutions.

24...

25 The supply, modification, repair, maintenance, chartering and hiring of warships.

26...

27 The services of travel agents referred to in Article 26, and those of travel agents acting in the name and on account of the traveller, for journeys within the Community.

The transactions referred to in points 3, 14 and 18-22 were abolished with effect from 1st January 1990 by Art 1(2) of the Eighteenth Council Directive 89/465/EEC of 18th July 1989; see OJ L226, 3.8.1989, p 21. The transactions referred to in points 4, 13, 15 and 24 abolished with effect from 1st January 1991 by *ibid*, Art 2. The transaction referred to in point 9 abolished with effect from 1st January 1992 by *ibid*. The transactions referred to in point 11 abolished with effect from 1st January 1993 by *ibid*. The transactions referred to in point 26 abolished with effect from 17th October 1998 by EEC Council Directive 98/80, Art 2; with effect from 17th October 1998.