OPINION OF ADVOCATE GENERAL JACOBS

delivered on 20 September 2001 [1]

1. This case concerns the way in which the basis of assessment for value added tax ('VAT') is to be determined where, as part of a promotional scheme, the original supplier of an item compensates a subsequent retailer for a price reduction granted by that retailer to his customer in exchange for a coupon or voucher issued by the original supplier, but where one or more other traders are present in the chain between supplier and retailer and where the prices paid by and to those other intervening traders are unaffected by the reimbursement.

2. The Commission considers that, by failing to provide for the taxable amount to be adjusted in respect of the first supplier in those circumstances, the German authorities have not complied with their obligations under the Sixth VAT Directive, [2] particularly in view of the Court's judgment in *Elida Gibbs*. [3]

Legal background

The VAT system in general

3. The principle on which VAT operates is set out as follows in Article 2 of the First VAT Directive: [4]

'The principle of the common system of value added tax involves the application to goods and services of a general tax on consumption exactly proportional to the price of the goods and services, whatever the number of transactions which take place in the production and distribution process before the stage at which tax is charged.

On each transaction, value added tax, calculated on the price of the goods or

1 — Original language: English.

2 — Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of assessment, OJ 1977 L 145, p. 1 (hereinafter 'the Sixth Directive').

3 — Case C-317/94 *Elida Gibbs* [1996] ECR I-5339.

4 — First Council Directive 67/227/EEC of 11 April 1967 on the harmonisation of legislation of Member States concerning turnover taxes, OJ, English Special Edition 1967, p. 14 ('the First Directive').

services at the rate applicable to such goods and services, shall be chargeable after deduction of the amount of value added tax borne directly by the various cost components.' [5]

4. The deduction system is designed to avoid a cumulative effect where VAT has also been levied on goods and/or services used in order to produce those supplied — that is to say, to avoid VAT being levied anew on VAT already charged. By its operation, a chain of transactions builds up, in which the net amount payable in respect of each link is a specified proportion of the value added at that stage. When the chain comes to an end, the total amount levied will have been the relevant proportion of the final price.

5. That approach also ensures the 'neutrality' of VAT as regards taxable persons — suppliers in the chain of transactions. They must account for tax in that they must charge VAT to the recipients of their supplies but by the operation of the system of deductions they do not in principle [6] bear the burden of any tax themselves; only the final consumer at the end of the chain of supply in fact bears that burden.

The relevant provisions of the Sixth Directive

6. Under Article 11(A)(1)(a) of the Sixth Directive, subject to certain detailed exceptions which do not affect the issue in the present case, the taxable amount for transactions within the territory of a country is to be

'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'.

7. Article 11(A)(3)(b) specifies that the taxable amount is not to include 'price discounts and rebates allowed to the cus-

5 — In discussions of the relationship between two transactions of which one is a cost component of the other, the former is commonly referred to as an 'input' and the latter as an 'output', the VAT on each being referred to respectively as 'input tax' and 'output tax'.

6 — With the apparently paradoxical exception of exempt transactions, which may in certain circumstances require a supplier to bear some non-deductible VAT burden. However, exempt transactions are not in issue in the present case.

tomer and accounted for at the time of the supply'.

8. Under the first subparagraph of Article 11(C)(1):

'... where the price is reduced after the supply takes place, the taxable amount shall be reduced accordingly under conditions which shall be determined by the Member States'.

9. Article 17(2) provides:

'In so far as the goods and services are used for the purposes of his taxable transactions, the taxable person shall be entitled to deduct from the tax which he is liable to pay:

(a) value added tax due or paid in respect of goods or services supplied or to be supplied to him by another taxable person;

...'

10. In accordance with Article 20(1):

'The initial deduction shall be adjusted according to the procedures laid down by the Member States, in particular:

...

(b) where after the return is made some change occurs in the factors used to determine the amount to be deducted, in particular where... price reductions are obtained;...'

11. Finally, under Article 21:

'The following shall be liable to pay value added tax:

1. under the internal system:

...

(c) any person who mentions the value added tax on an invoice or other document serving as an invoice;

...'

The German legislation in issue

12. Paragraph 17(1) of the Umsatzsteuergesetz (German VAT Law, 'the UStG') provides:

'Where the basis of assessment of a taxable transaction... has changed,

(1) the trader who made the supply shall adjust the amount of tax payable and

(2) the trader who received the supply shall adjust the amount of input tax deductible in that regard;

...'

The Court's judgment in Elida Gibbs

13. In this case[7] a manufacturer operated promotional schemes of two basic kinds. Under the 'money-off' schemes, a retailer would accept price reduction vouchers from customers in part-payment for an item and would be reimbursed the amount of the reduction by the manufacturer, regardless of whether he had bought the goods directly from the manufacturer or through a wholesaler. Under the 'cash-back' scheme, the manufacturer printed vouchers with a particular face value on the packaging of its products and would redeem those vouchers for cash directly to any end-purchaser who submitted them.[8] The VAT and Duties Tribunal, London, asked the Court whether the manufacturer's taxable amount was the price at which it had originally supplied the goods or that price less the reimbursement.

14. In answering that question, the Court stressed the basic principles of the VAT

7 — Cited above in note 3.

8 — The term 'cash-back' is also used (at least in the United Kingdom) for a different kind of commercial practice. When a customer pays by credit or debit card, retailers may offer to charge to the card an amount greater than that required to pay for the goods sold, and to hand the customer cash equivalent to the difference between the two sums. This pragmatic arrangement has no VAT repercussions whatever and is entirely distinct from the price refund schemes in issue in Elida Gibbs (and in the present case), regardless of the fact that the term 'cash-back' may be used for both.

system, in particular its neutrality as regards taxable persons and the fact that the tax burden is borne by the final consumer, with the result that the taxable amount serving as a basis for the VAT to be collected cannot exceed the consideration actually paid by that consumer. [9]

15. Bearing those principles in mind, and interpreting the concept of 'consideration' in Article 11(A)(1)(a) of the Sixth Directive in accordance with its previous case-law [10] to the effect that such consideration is the value actually received in each specific case, the Court held that, in the circumstances of either of the types of scheme in issue:

'It would not... be in conformity with the directive for the taxable amount used to calculate the VAT chargeable to the manufacturer, as a taxable person, to exceed the sum finally received by him. Were that the case, the principle of neutrality of VAT vis-à-vis taxable persons, of whom the manufacturer is one, would not be complied with.

Consequently, the taxable amount attributable to the manufacturer as a taxable person must be the amount corresponding to the price at which he sold the goods to the wholesalers or retailers, less the value of [the] coupons.

That interpretation is borne out by Article 11(C)(1) of the Sixth Directive which, in order to ensure the neutrality of the taxable person's position, provides that, in the case of cancellation, refusal or total or partial non-payment, or where the price is reduced after the supply takes place, the taxable amount is to be reduced accordingly under conditions to be determined by the Member States.' [11]

16. The Court considered that the absence of a direct contractual link between the manufacturer and the final consumer did not affect that finding, [12] and rejected objections put forward by the United Kingdom, German and Greek Governments to the effect that the required adjustments to the taxable amounts of intermediate traders would render the system unworkable, pointing out that there was in fact no need for those amounts to be adjusted. [13]

9 — See paragraphs 18 to 25 of the judgment.

10 — Case 89/81 *Hong Kong Trade* [1982] ECR 1277), paragraph 13 of the judgment, Case 230/87 *Naturally Yours Cosmetics* [1988] ECR 6365, paragraph 16, and Case 126/98 *Boots* [1990] ECR I-1235, paragraph 19.

11 — Paragraphs 28 to 30.

12 — Paragraph 31.

13 — Paragraphs 32 and 33.

Procedure in the present case

17. In 1992, the Commission asked all the Member States whether under their legislation a manufacturer who reimbursed a retailer for a reduction granted to a final consumer in exchange for a voucher was entitled to reduce his taxable amount accordingly. The German Government replied to the effect that under Paragraph 17(1) of the UStG such a reduction was possible only where the amount of the transaction between the manufacturer and his immediate customer was affected; where the reimbursement was made to another person further removed in the chain of supply the manufacturer's taxable amount could not be reduced.

18. The Commission considered that situation to be incompatible with the Sixth Directive and set in motion the procedure provided for in Article 169 of the EC Treaty (now Article 226 EC) but, after an exchange of correspondence, agreed to suspend that procedure pending delivery of the judgment in *Elida Gibbs*. When, following that judgment, the German Government still did not amend its legislation but maintained its previous position, [14] the Commission issued a reasoned opinion on 23 March 1998 and brought the present action on 26 November 1998, seeking a declaration that, by failing to adopt provisions enabling the basis of assessment to be adjusted when 'money-off' vouchers are redeemed, the Federal Republic of Germany has failed to fulfil its obligations under Article 11 of the Sixth Directive.

19. The French and United Kingdom Governments both announced their intention to intervene in support of Germany in this case, but the French Government subsequently withdrew. [15] The United Kingdom has submitted observations in intervention. At the hearing, oral argument was presented by the German and United Kingdom Governments and by the Commission.

Analysis

The scope of the dispute

20. First, it is common ground that the German provisions in issue do indeed have the effect which the Commission ascribes to them. The question to be decided is whether that effect is compatible with the Sixth Directive.

14 — Affirmed in a circular dated 15 April 1998 from the Federal Finance Ministry to the tax authorities of the *Länder*.

15 — By letter of 4 October 1999. The Commission states that the French authorities adopted administrative instructions on 8 November 1999 bringing their practice into line with the judgment in *Elida Gibbs*.

21. Second, the Commission seeks a declaration only in respect of Germany's treatment of 'money-off' vouchers although, as the German Government has pointed out, it devotes an appreciable part of its submissions to the treatment of 'cash-back' vouchers.

22. It is clear that the Court's ruling must be confined to the treatment of 'money-off' vouchers.

23. However, the situation of which the Commission complains is Germany's failure to provide for adjustment of the original supplier's taxable amount when he redeems a voucher by making a cash payment to a retailer who accepted the voucher in part-payment of goods sold to a final consumer, *when the original supplier did not supply those goods directly to the retailer*. There is no material difference — as regards the adjustment of the original supplier's taxable amount — between that situation and one in which the cash payment is made directly to the consumer. What is at issue is the possibility of making an adjustment to a supplier's taxable amount as a result of a payment (a price reduction or rebate) which 'leapfrogs' one or more links in the normal VAT chain.

24. At the hearing, the German Government argued that the 'money-off' and 'cash-back' situations were very different. However, that appeared to be on the basis of the examples set out in the table which it presented to the Court, in which the original supplier had sold directly to the retailer. [16] In that situation, the German rules allow for an adjustment to be made to the amount of that original transaction where a 'money-off' voucher is used, but not where a 'cash-back' voucher leads to a payment direct from the first supplier to the final consumer. There is thus a difference there, but that difference disappears when another link — say a wholesaler — is added to the chain between the original supplier and the retailer. In that case, which is the situation of which the Commission complains, the German rules prevent adjustment of the supplier's taxable amount equally where 'money-off' and 'cash-back' vouchers are concerned.

25. Thus, despite the circumscribed nature of the order formally sought, it is in my view acceptable, for the purposes of analysis, to consider the situation of 'cash-back' vouchers alongside that of 'money-off' vouchers.

26. Third, the German and United Kingdom Governments invite the Court to

16 — That situation is currently under consideration by the Court in Case C-398/99 *Yorkshire Cooperatives*, in which Advocate General Stix-Hackl delivered her Opinion today.

reconsider its judgment in *Elida Gibbs*, either overturning it or in some way limiting its effects. [17] The Commission points out that the arguments advanced by the German Government are essentially those which it put forward in that case, and which were explicitly rejected by the Court. Both Governments consider that judgment to be, at least in part, incompatible with the principles of the VAT system. The United Kingdom Government specifically points out that the judgment was given by a Chamber of five judges reduced to three and that it went against the views of the Advocate General.

27. Indeed, unless *Elida Gibbs* is reversed, the case against Germany seems straightforward and difficult to defend. The terms of the judgment are clear and it is common ground that the German rules are not consistent with them.

28. This case may be addressed, therefore, as a reopening, before a Full Court, of the issues in *Elida Gibbs*.

17 — Although it appears that the United Kingdom has in fact brought its legislation into line with the judgment and that Germany is now the only Member State not yet to have complied with it.

The basic chain

29. It will be necessary to look at some detailed examples of how the system works. For that purpose, it may be helpful to set down at this point a simplified model of a standard VAT chain. It should be stressed that such a model, like the similar models used by the parties in their submissions, is of an abstract nature and does not reproduce all the complex realities of VAT in actual trade. Despite its level of abstraction, however, it does provide an accurate picture of the application of the tax.

30. I shall base my simplified chain on that used by the German Government in its rejoinder, in which there are four parties (and three transactions). The four parties comprise three taxable persons (who might be a manufacturer, a wholesaler and a retailer) and a final consumer. I shall refer to them respectively as A, B, C and D.

31. We may assume that the transactions in question are successive sales of the same item, with an increase in price at each stage, although the essentials would in principle remain the same for other types of chain. In fact, the nature of 'leapfrogging' voucher schemes is such that they

almost inevitably apply only to goods and only when the goods concerned are not noticeably transformed by the transactions in the chain — A's aim is to promote the sale of his own goods, not of goods incorporating his supplies.

32. To make matters as simple as possible, I shall take a fictitious rate of VAT of 10% and I shall assume the increase in price at each stage to be 100 (the currency being immaterial), exclusive of tax.

33. Thus, the basic chain is as follows: (i) A sells to B at a net price of 100, plus 10% VAT, making a total of 110, and accounts to the tax authorities for output tax of 10; [18] (ii) B sells to C at a net price of 200, plus 10% VAT, making a total of 220; B must therefore account to the tax authorities for output tax of 20, from which he deducts his input tax of 10; (iii) C sells to D at a retail (VAT-inclusive) price of 330, made up of a net price of 300, plus 10% VAT; C must in turn pay 10 to the tax authorities, representing the VAT of 30 which now burdens the item, less the 20 which has already been accounted for at the earlier stages.

34. In that chain the traders A, B and C have in fact not borne the burden of any VAT themselves, but have merely added tax in proportion to the amount by which they increased the net price and passed that on, together with the amount of VAT already burdening their inputs, to the next person in the chain. At each stage, the full amount of their output tax is collected from that next person and the difference between that and their input tax is paid to the tax authorities. D, however, at the end of the chain, not being a taxable person who is going to use the goods for his own taxable outputs, pays the total net price of 300, plus VAT at 10%, making a total of 330.

The basic variants

35. Essentially, *Elida Gibbs* was concerned with two variants of that basic chain, and both have been discussed in the present case.

36. The first is where A issues a 'money-off' voucher (it will be simplest to postulate the face value of the voucher as being 11) to D and at the same time promises that he will reimburse that face value of that voucher to C if C accepts it from D in part-payment of A's goods. In this variant, the net amounts paid and received by B are not affected.

18 — Less input tax on any items used for the purposes of his supply, but it will be simpler to assume for present purposes that there are none.

37. In the second, A issues a 'cash-back' voucher (which will generally be attached to the goods in such a way as to serve also as proof of purchase) to D and reimburses the face value of that voucher (which I shall again assume to be 11) directly to D. In this variant, the net amounts paid and received by B and C are not affected.

38. In both cases, the amount (11) of the refund or reduction from which D benefits concerns the VAT-inclusive price. It may therefore be deemed to comprise a net element of 10 and a VAT element of 1.

39. As I have pointed out above, there is no essential difference between those two variants for present purposes. The specific issue in this case concerns the transaction between A and B, and whether A's taxable amount (and consequently the amount of his output tax) may be reduced without affecting the amount of input tax which B may deduct.

The competing approaches

40. The Commission essentially takes a global view of the situation when assessing the effect of *Elida Gibbs*.

41. It argues that where the manufacturer has sold an item to an intermediary at a price of 110 including tax (100 net), and later makes a promotional reimbursement of 11 including tax (10 net), the taxable amount must be 100 – 10 = 90, and the tax 10 – 1 = 9. This applies regardless of whether the 11 was reimbursed or discounted to the same intermediary, to another intermediary further removed in the chain of supply or to the final purchaser. To make the manufacturer accountable for a greater sum would not be compatible with the principle of neutrality.

42. In addition, where the final consumer has obtained a reduction or partial reimbursement of the price paid, the total amount of VAT levied may not exceed the proportion of the price actually paid (that is to say, after deduction of the reduction or reimbursement) which represents VAT at the applicable rate. Thus, where a consumer buys an item at a tax-inclusive price of 330 (300 net) [19] against which he receives a reduction or reimbursement of 11, making a definitive tax-inclusive total of 319 (290 net), the total amount of VAT levied must be 29 (10% of 290). It is thus contrary to the Sixth Directive to levy a total of 30 in those circumstances.

43. In contrast to the Commission, the German and United Kingdom Govern-

19 — I am adjusting the figures used by the Commission to fit my basic example given above.

ments take a step-by-step approach to each transaction in the chain of supply, arguing that neutrality, certainty and effective control are ensured only when each trader in the chain deducts from his output tax exactly the amount of VAT which was passed on to him in the form of input tax; any adjustment made must thus concern both sides of a transaction. Where a sum of money changes hands outside a transaction in the chain, it can have no effect on the amount of tax accounted for in respect of that transaction.

44. The two governments put forward a number of specific objections to the approach taken by the Commission (and by the Court in *Elida Gibbs*), which I shall examine in turn below. They may be grouped in three categories — discrepancies in accounting, loss of tax revenue and distortion of competition — but are presented, like the Commission's arguments, in terms of the basic principles of the VAT system.

45. However, the contrasting approaches suggest that, in the types of voucher scheme in issue, it may not be possible to reconcile all of those principles entirely. Whilst such reconciliation should clearly be achieved wherever possible, it is not easy, as Advocate General Fennelly noted in his Opinion in *Kuwait Petroleum*,[20] to extract 'a completely coherent set of rules which it is possible to apply with total confidence to every promotion scheme devised by the ingenuity of commerce'.

The competing principles

46. Both sides stress the neutrality of VAT as far as traders are concerned — the actual burden of the tax should be borne only at the final consumption stage and tax levied at earlier stages in the chain should be passed along to that final stage.

47. However, they take different views of the essential requirements for that neutrality. On the one hand (the point of view favoured by the Commission), such a principle implies that a taxable person must not be accountable for tax on a sum greater than that which he has finally actually received in respect of the transaction, and that the total tax levied on the chain of supply as a whole must be the relevant proportion of the final net price. On the other (the point of view favoured by

20 — Case C-48/97 *Kuwait Petroleum* [1999] ECR I-2323, at paragraph 44 of the Opinion.

Germany and the United Kingdom), it implies that the amount deducted in respect of each transaction must correspond exactly to the amount charged on the previous transaction.

48. In the normal course of events (the basic chain I have described above) those two implications both hold true and are totally compatible.

49. In the variants in issue, however, the fact that a price reduction is made, after the supply takes place, in the form of a payment by A to either C or D cannot easily be taken into account without compromising one implication or the other.

50. If A (who has paid the reduction) is allowed to reduce his taxable amount accordingly, his output tax will no longer correspond to B's input tax; B will be able, unless his own tax position is adjusted, to deduct from his output tax an amount greater than that which has been accounted for on his inputs. But if A is not allowed to do so, he will be accountable for tax on a sum greater than that which he effectively received and the total amount of VAT levied in respect of all the transactions in the chain will be greater than the appropriate rate for the price finally paid by D.

51. This case concerns the taxable amount in respect of A's sale to B. That amount is, under Article 11(A)(1)(a) of the Sixth Directive, the consideration obtained by the supplier. As was stressed in *Elida Gibbs*,[21] that consideration is the value actually received in each specific case. The Court was not innovating when it made that statement, but recalling consistent case-law going back to 1981, and the rule has again been reaffirmed since.[22] In the present case, it is clear that, thus defined, the consideration obtained by A, once the promotional payment has been made, is less than the amount initially paid to him by B.

52. In addition, the nature of VAT is that it represents a defined proportion of the value added at each stage in the chain and, at the final consumption stage, that same proportion of the overall value of the chain of supply. In the words of Article 2 of the First Directive, it is 'a general tax on consumption exactly proportional to the price of the goods and services, whatever the number of transactions which take place in the production and distribution process before the stage at which tax is charged'. In the present case, once the promotional payment has been made, the

21 — At paragraph 27 of the judgment.

22 — See, for example, Case C-258/95 *Fillibeck* [1997] ECR I-5577, paragraph 13 of the judgment, and most recently the judgment of 29 May 2001 in Case C-86/99 *Freemans*, paragraph 27.

overall value of the chain of supply is less than the unreduced value of the supply by C to D.

53. Bearing the above considerations in mind, I turn to the detailed objections put forward by the German and United Kingdom Governments.

Discrepancies in accounting and control

54. It may be helpful to return at this point to the simplified model chains set out above, to examine exactly what happens if Germany's approach is followed and what happens if the Commission's approach is followed.

55. In the 'money-off' variant, D pays C the sum of 319 in cash, together with a voucher for 11, and A pays C the sum of 11 in exchange for the voucher. In Germany's view, that has no effect on any of the VAT (10 + 10 + 10) levied at the three stages in the chain, since it is separate from any of those three transactions. In the Commission's view, the payment reduces A's taxable amount by 10 and thus the amount of his output VAT by 1, but has no effect on the taxable amount or amount of tax in the second and third transactions — or, indeed, on the amount of input tax deductible by B in respect of the first transaction; the total VAT levied is thus 9 + 10 + 10.

56. In the 'cash-back' variant, A pays D the sum of 11 in respect of D's purchase from C at a tax-inclusive price of 330. Again, in Germany's view, that has no effect on any of the three transactions. In the Commission's view, the only effect is again to reduce A's taxable amount by 10 and his output tax by 1; there is no change to the amount of input tax deductible by either B or C.

57. The reason the result is the same under each approach in both variants is that the 'leapfrogging' payment is simply moved one stage nearer to or further away from the first transaction, but there is always at least one trader in the chain who neither receives nor makes the payment. It seems to be common ground that without such 'leapfrogging' — if A sold directly to C who sold to D, and D paid in part with a

voucher later redeemed by A to C;[23] or if the voucher used by D was redeemed first by B to C and then by A to B; or if A sold directly to D and later refunded part of the purchase price — all the taxable amounts would fall to be adjusted.

58. However, in the type of 'leapfrogging' case in issue, the approach taken by the Court in *Elida Gibbs* and defended by the Commission in the present case means that A's taxable amount corresponds to the value actually received by him and the amount of VAT received by the tax authorities is exactly proportional to the final value of the chain of supply, whereas the approach taken by Germany and the United Kingdom leads to neither of those results.

59. On the other hand, the *Elida Gibbs* approach leads to a situation in which A, having originally charged VAT of 10 to B (which B has deducted, when accounting to the tax authorities, from the output tax he charged on his sale to C), is then allowed to reduce that amount to 9 retroactively without affecting B's entitlement to deduct 10. Germany and the United Kingdom consider that to be an unacceptable discrepancy, entailing a gap in the way in which the tax is accounted for and collected.

23 — That is to say, in the situation under consideration in *Yorkshire Cooperatives*; see note 16.

60. I am not convinced that the discrepancy is unacceptable. Value added tax is what it says — a tax on the value added at each stage. At each stage, the amount payable to the tax authorities is based on the difference between inputs and outputs. The actual value of the transactions, although relevant to verifying whether the total amount of tax has been correctly levied, does not affect that difference. From that point of view, it seems to me immaterial whether, if A's output tax is retroactively adjusted, B's input tax is also adjusted or not, provided that the difference between B's input and output taxes amounts to tax at the correct rate on the *value* actually *added* by B. An artificial adjustment of the intermediate transactions, which might be possible under Article 20(1) of the Sixth Directive but which all parties agree would be a very cumbersome operation, is simply not necessary to achieve the correct result.

61. Three detailed arguments, however, must be dealt with under this heading.

62. First, the German Government argues that since, under Article 21(1)(c) of the Sixth Directive, any person who mentions VAT on an invoice is liable to pay that tax, no adjustment can be made to a supplier's taxable amount without rectifying the invoice.

63. However, I do not consider that Article 21(1)(c) should be read as requiring such a result. That provision is concerned with ensuring that when tax is invoiced tax is accounted for, not with calculating the amount of that tax. The central aim is to ensure that amounts deducted as input tax on the basis of invoices balance back along the chain of supply with the amounts paid as output tax. That aim is not thwarted by an adjustment which, although not passed on to all the other transactions in the chain, has no effect on such overall balance.

64. Article 21(1)(c) has been interpreted by the Court principally in two cases: *Genius Holding*[24] and *Schmeink & Cofreth*.[25] Neither of those cases concerned the point in issue in the present case, but it is clear from both judgments that the Court was concerned primarily with the possibility of fraud or, more generally, loss of tax revenue. In *Schmeink* in particular, it did not take a rigorous approach to the provision but considered that its purpose, even as regards fraud, was simply to ensure proper collection of tax due. The Court also expressly accepted (in *Genius*) that the amount of tax deductible by B need not be the same as that which A is liable to pay under Article 21(1)(c) and (in *Schmeink*) that the provision does not preclude subsequent rectification of the amount payable by A on the basis of the invoice, provided that there is no risk of any loss in tax revenue.

65. I shall deal more fully with the issue of loss of tax revenue below[26] but I do not consider there is any risk of such loss in the hypotheses I have outlined above.

66. Second, Germany and the United Kingdom argue that a refund paid by A to D (or to C) should be regarded as consideration obtained from a third party, and thus as part of the taxable amount under Article 11(A)(1)(a), rather than as a price reduction after the supply takes place, giving rise to a reduction in the taxable amount under Article 11(C)(1). Germany claims that, as regards the supply by C to D, A is no more a party to the transaction than D's dear old grandmother would be, if she advanced part of the price; the United Kingdom compares the situation to A standing outside C's shop, handing banknotes to those who have bought his goods.

67. I consider that analysis to be correct, *in so far as the transaction between C and D*

24 — Case 342/87 *Genius Holding* [1989] ECR 4227.

25 — Case C-454/98 *Schmeink & Cofreth and Strobel* [2000] ECR I-6973.

26 — See paragraphs 75 to 95.

is concerned. Either (in the 'money-off' situation) D pays 319 to C together with a voucher for 11 which A then redeems to C, or else (in the 'cash-back' situation) he pays the full price of 330 and later receives 11 from A. In the first case, A is a third party to the transaction between C and D, paying part of the consideration, in the second he is entirely extraneous to the transaction. In both cases, the correct amount of VAT to be levied in respect of the retail sale is 30 (10% of the final net sales price received by C) minus C's input tax of 20.

68. However, the application of Article 11(A)(1)(a) to that transaction does not preclude the application of Article 11(C)(1) to A's own taxable amount, which relates to a different transaction. It is the price of that first supply that has been reduced. Article 11(C)(1), moreover, refers only to reduction of the supplier's taxable amount, not of the recipient's input tax. Although it will normally be the case that a reduction affects both sides of a transaction, there is nothing to preclude its application to only one side when only one side is affected.

69. Thus, I do not see any conflict between the two provisions in their application to the types of scheme envisaged here, or between their application and the approach advocated by the Commission.

70. Third, the German Government points out that the reduction of taxable amount provided for in Article 11(C)(1) is subject to 'conditions which shall be determined by the Member States'. Does that entitle a Member State to impose the condition that there can be no adjustment unless A's invoice is rectified, and that in that case B's input tax must be reduced?

71. In *Molenheide*,[27] the Court held that

'whilst it is legitimate for the measures adopted by the Member States to seek to preserve the rights of the Treasury as effectively as possible, they must not go further than is necessary for that purpose. They may not therefore be used in such a way that they would have the effect of systematically undermining the right to deduct VAT, which is a fundamental principle of the common system of VAT established by the relevant Community legislation.

... the principle of proportionality is applicable to national measures... adopted by a Member State in the exercise of its powers relating to VAT, since, if those measures go further than necessary in order to attain their objective, they would undermine the

27 — Joined Cases C-286/94, C-340/95, C-401/95 and C-47/96 *Molenheide and Others* [1997] ECR I-7281, paragraphs 47 and 48 of the judgment.

principles of the common system of VAT and in particular the rules governing deductions which constitute an essential component of that system.'

72. Those statements refer specifically to the right to deduct VAT, but I consider that the right to deduct is simply one aspect of the overarching right not to be required to pay more tax than should be levied having regard to the value of one's transactions. The right to have one's output tax established on the correct basis (following retroactive adjustment where the basis has changed) is another aspect, at least equally important, and the same principles must apply.

73. In the light of my view on the correct approach to the chain of transactions in schemes of the kinds in issue, I consider that a requirement that the retroactive adjustment be passed along the whole chain in order to qualify for a reduction does go further than is necessary to attain the objective of protecting the rights of the tax authorities. It cannot therefore be justified on the basis of the Member States' powers under Article 11(C)(1) of the Sixth Directive.

74. That is not to negate the effect of that provision by denying Member States any power to determine conditions for the adjustment to be made. I consider, however, that the type of condition envisaged relates rather to ensuring that no reduction is granted unless it is justified, and might include, for example, requirements relating to proper documentary evidence of payments made.

Loss of tax revenue

75. Both Germany and the United Kingdom claim that the Commission's approach entails a loss of tax revenue.

76. It must be borne in mind here that tax revenue is not lost merely because it is lacking. Tax revenue is lost only where it should have been collected but was not.

77. In the simplified model I have used, the German Government's approach involves levying VAT of 10 on the supply by A to B and 30 on the whole chain of transactions in question. The approach followed by the

Court in *Elida Gibbs* and defended by the Commission in the present case means that the amounts levied are only 9 and 29 respectively.

78. In my view, analysis of the transactions shows that in the normal course of events 9 and 29 are the proper amounts of tax to be levied, having regard to the actual value received by A and the total economic value of the chain. The difference between those amounts and the 10 and 30 which the German tax authorities would like to levy is not a 'loss' of tax revenue.

79. However, Germany has identified two situations in which that normal course of events does not run true. The Commission retorts that those situations are extremely rare in practice. Be that as it may, they cannot be dismissed out of hand. In relation to a third allegation, however, the German position is in my view quite mistaken.

— Exempt exports

80. Under Article 15 of the Sixth Directive, a number of supplies made outside the Community are exempt from VAT. Under Article 17(3)(b), all input tax in respect of such supplies must be deducted or refunded. The German Government points out that, if C or D is outside the Community, B or C, as the case may be, will be entitled to a refund/deduction of the full input tax of 20 which has already been borne by the item supplied; however, if A subsequently makes a promotional payment of 11 reducing the cost to D and is allowed to reduce his output tax concomitantly by 1, a total of 21 will be repaid by the tax authorities where only 20 had been collected.

81. That would indeed amount to a loss of tax revenue.

82. The Commission objects that voucher scheme reimbursements involving exports are practically non-existent. However, the German Government referred at the hearing to promotional cash payments, of non-negligible sums, made by car manufacturers to final purchasers, including those outside the Community. Such situations should therefore be taken into consideration, although it seems to me that they can be dealt with adequately without upsetting the approach taken in *Elida Gibbs*.

83. If, in the normal intra-Community situation, A may be allowed to adjust his output tax downwards on making a pro-

motional payment to or on behalf of D, that is because the price paid by D is inclusive of VAT, so that any reduction in it may also be deemed to include a proportion of VAT. Where on the other hand an item is exported from the Community free of VAT in accordance with Articles 15 and 17(3)(b) of the Sixth Directive, no Community VAT is included in any price charged at that or any subsequent stage in the chain. Thus any payment made by A to a subsequent recipient outside the Community cannot be deemed to include any amount of VAT which could give rise to a reduction in A's output tax.

84. It should not be prohibitively difficult to ensure that A cannot deduct what would be a fictitious amount of VAT from his output tax in such cases. In order to make such a deduction in the normal course of events, A must at the very least keep proper accounts which show where payments have been made. Where voucher schemes are applied outside the Community, in the case of 'money-off' vouchers, arrangements must be made with foreign retailers; in both 'money-off' and 'cash-back' schemes, payments in order to be any kind of incentive to purchase must be made in a non-Community currency. Both those factors should make control by the revenue authorities relatively easy to achieve.

85. Thus it seems that the kind of conditions envisaged by Article 11(C)(1) of the Sixth Directive are appropriate and sufficient to prevent any unjustified claims or loss of tax revenue.

86. The German Government also claims that the same problem would arise in the case of exempt transactions within the Community — if, say, the supply by C to D were an exempt transaction, whereas the supply by A to B had been a taxable transaction.

87. In such cases, C will not have been able to deduct any input tax but the price of the final transaction is none the less deemed not to include any VAT. The answer is however the same: since D's purchase price does not include VAT, any reduction or partial repayment of that price cannot include any VAT either and A cannot adjust his output tax.

88. In any event, the nature of voucher schemes is such [28] that it is very difficult to see any likelihood of their being used in relation to transactions which are or may be exempted from VAT under Article 13 of the Sixth Directive.

28 — See my remarks in paragraph 31 above.

— Payments made to a 'final' consumer who is a taxable person

89. The second type of situation to which the German Government refers is where D, who benefits from the price reduction offered by A, is not a true final consumer but a taxable person who uses the item acquired for the purpose of his own taxable outputs. In the scenario to which it objects, D acquires an item at a price of 330, including tax, uses the item for the purpose of his own outputs, and thus deducts input tax of 30 from his output tax. However, if he receives a promotional payment of 11 from A and A is allowed to reduce his own output tax by 1 on that account, D will have been allowed to deduct an amount of VAT which is neither due nor paid.

90. Again, the scenario set out involves a true loss of tax revenue.

91. Again, the Commission objects that such scenarios are extremely uncommon in practice and it may be right — up to a point. If D uses A's goods to more than a fairly marginal extent for his own taxable outputs, he is less likely to source them through intermediaries — he will presumably seek to obtain them at the lowest cost possible, ideally directly from A. However, it is not difficult to imagine that a manufacturer of goods used by, say, small artisans may sell only through wholesalers but may none the less operate a 'cash-back' scheme to reward artisans who purchase those goods.

92. However, again it does not seem to me to be unduly difficult to counteract the kind of loss of tax revenue envisaged. First of all, I disagree with the German Government's view that D is entitled to deduct the full input tax of 30 invoiced to him by C from his own output tax. Once it is accepted that A may reduce his output tax by 1, it must also be accepted that D's input tax is deemed to be reduced by 1 when he receives A's promotional payment of 11. If D is a taxable person, he must keep proper accounts of his inputs and outputs, and failure to record such promotional payments will amount to a fraud.

93. The German Government may fear that such frauds will be difficult to detect, and the requirement to account for promotional payments difficult to enforce. However, that will normally only be the case in exceptional circumstances. Taxable persons generally do not obtain their supplies item by item at retail outlets — a practice which is likely to increase their costs,

compared to purchasing in larger quantities from wholesalers or similar specialist suppliers, to a greater extent than will usually be offset by exploiting any VAT loophole involving the use of 'cash-back' or 'money-off' vouchers. In normal circumstances, controls should not be too difficult to put in place. Where 'cash-back' vouchers are concerned, A's accounts must presumably record any payments made to D. In the case of 'money-off' schemes, which are in any event unlikely to contain a 'leapfrogging' element, C could be required to mention on any invoice to D the fact that a voucher was accepted in part-payment for the goods.

— Double deduction of VAT

94. In addition, the German Government puts forward a further way in which, it claims, tax revenue is lost. In the case of 'money-off' vouchers, it argues, the fact that the net value of the voucher cannot be included in C's taxable amount, as confirmed by the Court in *Boots* and *Argos*,[29]

29 — Case 126/88, cited above in note 10, and Case C-288/94 *Argos Distributors* [1996] ECR I-5311.

coupled with the reduction of A's taxable amount, would lead to a double deduction and a loss of tax revenue.

95. Here, I believe the German Government to be mistaken in referring to *Boots* and *Argos* in the present context, as those cases did not concern 'leapfrogging' payments of the kind in issue. As the Commission points out, in the type of situation with which we are concerned, the net value of the voucher should be included in C's taxable amount. C actually receives that amount from A (as consideration obtained from a third party, in accordance with Article 11(A)(1)(a)), so that there is only a single deduction. This does not conflict with the approach taken in different economic circumstances in *Boots*, where the value of the voucher was not to be included in the retailer's taxable amount because it was a reduction granted by the retailer himself, or in *Argos*, where the voucher was redeemed directly by the manufacturer in exchange for the goods he supplied.

Distortion of competition

96. Finally, the German Government alleges that the *Elida Gibbs* approach

distorts competition in two types of case in that the tax treatment of voucher schemes (which use only A's own financial resources) is more favourable than that of other promotional schemes from which other operators may benefit.

97. I am not convinced that any tax incentive to operators to use their own resources rather than to deal with others would necessarily be a distortion of competition, but it might admittedly entail less trade rather than more. In any event, it seems to me either that no such incentive exists or that its effect is likely to be negligible; where it exists, it appears justified by the provisions of the Sixth Directive.

— Comparison with advertising

98. The German Government argues that the aim of voucher schemes operated by manufacturers is to increase sales without reducing retailers' takings on each sale. They are promotional measures undertaken at the manufacturer's choice and expense and as such are alternatives to advertising campaigns. If the manufacturer is allowed to reduce his taxable amount in the case of a voucher scheme, he will be more likely to make that choice, thus distorting competition to the detriment of advertising agencies.

99. The Commission points out that, with regard to the choice between a voucher scheme and advertising, the German Government bases its argument on figures which confuse tax-inclusive and tax-exclusive prices.

100. I agree with the Commission. If A decides to pay 11 to D, and is allowed to reduce his output tax by 1, every time D buys one of his products, that is no different, as regards VAT, from a situation in which he decides to spend the same amount on advertising his products. If A spends 11 on advertising services, that sum will include VAT of 1 which is, from A's point of view, input tax which he may deduct from his output tax. In both situations, although the mechanisms are different, the result is that A pays 1 less in output tax. For A, the VAT position is thus entirely neutral as regards the choice of promotional method, and there is no financial incentive for him to choose one method rather than the other — and thus no apparent distortion of competition.

101. The tax authorities will indeed receive slightly less overall if he chooses to use a voucher scheme but, unless A's resentment is so great that he systematically chooses the solution least advantageous to them whilst maintaining his own position, there is no VAT reason for him to eschew the services of advertising agencies. His decision is far more likely to be taken on the basis of the expected effects on sales.

— Comparison with free gift schemes

102. The German Government argues that allowing A to reduce his output tax as a result of promotional payments of the kinds in issue would give rise to a divergence of treatment between such voucher schemes and the type of 'free gift' scheme considered by the Court in *Kuwait Petroleum*. [30]

103. In that case, a petrol company offered customers a stamp with every 12 litres of fuel purchased. Once a certain number of stamps had been collected, they could be exchanged for 'free gifts' from a special catalogue. The Court held that the fact that no charge was made for the 'gifts' could not be regarded as constituting a rebate or price discount within the meaning of Article 11(A)(3)(b) of the Sixth Directive, and that the supply of those 'gifts', unless they were of small value, must be treated as a supply made for consideration and thus a taxable transaction. [31]

104. Thus, such a supplier is required to account for VAT on the value of the supply of the 'gifts', but is also entitled to deduct the input tax incurred on their acquisition. The result would appear to be neutral from the VAT point of view; since no value is added the two amounts will cancel out completely.

105. According to the German Government's argument, if A decides on a 'free

30 — Cited above in note 20.

31 — In accordance with Article 5(6) of the Sixth Directive, which states: 'The application by a taxable person of goods forming part of his business assets for his private use or that of his staff, or the disposal thereof free of charge or more generally their application for purposes other than those of his business, where the value added tax on the goods in question or the component parts thereof was wholly or partly deductible, shall be treated as supplies made for consideration. However, applications for the giving of samples or the making of gifts of small value for the purposes of the taxable person's business shall not be so treated'.

gift' scheme, he purchases the 'gifts' at a net price of 10, on which he will be charged 1 in VAT. He then supplies them to D in a transaction which is deemed to be for consideration. Since no value has been added, the deemed consideration will still be 10 and the output VAT 1. After deduction of the input tax, the net effect on A's VAT will be 0. If he decides on a 'cash-back' or 'money-off' scheme, he offers D a discount or refund of 11, made up of a net price reduction of 10 and a corresponding VAT reduction of 1. The net effect on his VAT, in accordance with *Elida Gibbs*, will be a reduction of his output tax by 1.

106. There is indeed a difference in fiscal treatment here, but as the Commission points out that difference in treatment is inherent in the provisions of the Sixth Directive. It is clear from 11(A)(3)(b) and (C)(1) that discounts and rebates are not to be included in the taxable amount, whether allowed at the time of supply or subsequently. It is also clear from those provisions and from Article 5(6), as interpreted by the Court in *Kuwait Petroleum*, that the supply of goods (such as 'free gifts') free of charge for business purposes is a supply for consideration, the taxable amount being their cost price, and there is no discount or rebate in such circumstances. The two types of scheme fall under different provisions, which explains the difference in treatment. As the Commission pointed out at the hearing, one scheme involves supplying more goods at the same price, the other involves supplying the same goods at a lesser price.

107. Furthermore, I consider that the German Government has not established that such difference in treatment will lead to any distortion of competition. It is true that if A were led by fiscal considerations to favour 'money-off' or 'cash-back' rather than 'free gift' schemes, suppliers of items used as 'free gifts' would do less business. However, A will presumably choose between different types of promotional scheme in the light of their net cost to him and their effect on sales; he will choose the scheme which encourages D to buy most at the least cost to him (A). There is no reason to suppose that D will always find a scheme offering a tax-inclusive reduction or refund of 11 more attractive than one offering a 'free gift' whose tax-inclusive value is 11.

Final considerations

108. The arguments in this case are not unevenly balanced. The Commission has

put forward convincing reasoning to support the view that, even had the Court not delivered its judgment in *Elida Gibbs* in those terms, the VAT on A's supply to B should, on the principles of the Sixth Directive, take account of the reduction paid out by A to C or D, and the total amount of VAT levied on the whole chain of supply should be proportional to the amount actually paid by the final consumer. The German and United Kingdom Governments have pointed to structural and practical problems in that approach, which cannot be dismissed out of hand.

109. I none the less consider that the Commission's point of view should prevail.

110. First and foremost, I take the view that, in the event of an otherwise irreconcilable difference, the requirement that the amount of VAT levied should be the correct proportion of the actual value finally received by the supplier (and, for the chain as a whole, of the final price) should be given greater weight than structural requirements. In other words, achievement of the end is more important than implementation of the means designed to achieve it.

111. Furthermore, the structural and practical problems in question are not insuperable. I have suggested certain solutions in the course of this Opinion and it appears from what has been said in the course of the pleadings and at the hearing that the legislation of all the Member States has now been brought into line with the judgment in *Elida Gibbs*, with the sole exception of Germany. Only one other Member State has considered that the difficulties involved in that alignment warranted intervention in Germany's support in the present case.

112. In those circumstances, it seems to me that the interpretation adopted by the Court in *Elida Gibbs* should not be overturned without some overriding justification. The concerns put forward by Germany and the United Kingdom, while real, are not such as to convince me that the present situation is irreconcilable with the fundamental principles of the VAT system or gives rise to insoluble problems in preventing any unjustified loss of tax revenue. That being so, I consider that it would in any event be wholly disproportionate to require — as would be the case if *Elida Gibbs* were overturned — all the remaining Member States to amend anew their VAT legislation, which appears to be operating satisfactorily.

Conclusion

113. I am accordingly of the opinion that the Court should

(1) declare that, by failing to adopt provisions enabling a supplier's basis of assessment to be adjusted when he redeems vouchers accepted in part payment of his goods by a subsequent trader, even when he did not supply the goods directly to that trader, the Federal Republic of Germany has failed to fulfil its obligations under Article 11 of the Sixth VAT Directive;

(2) order the Federal Republic of Germany to bear the costs of the proceedings, except those of the United Kingdom, which must bear its own costs.