JUDGMENT OF THE COURT (First Chamber)

27 September 2001 *

In Case C-16/00,

REFERENCE to the Court under Article 234 EC by the tribunal administratif de Lille (France) for a preliminary ruling in the proceedings pending before that court between

Cibo Participations SA

and

Directeur régional des impôts du Nord-Pas-de-Calais,

on the interpretation of Article 4(1) and (2), Article 13B(d) and Article 17(2)(a) and (5) of the 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),

* Language of the case: French.

THE COURT (First Chamber),

composed of: M. Wathelet, President of the Chamber, P. Jann and L. Sevón (Rapporteur), Judges,

Advocate General: C. Stix-Hackl,

Registrar: D. Louterman-Hubeau, Head of Division,

after considering the written observations submitted on behalf of:

— Cibo Participations SA, by M. Pourbaix, avocat,

— the French Government, by K. Rispal-Bellanger and S. Seam, acting as Agents,

— the Commission of the European Communities, by E. Traversa, C. Giolito and H. Michard, acting as Agents,

having regard to the Report for the Hearing,

after hearing the oral observations of Cibo Participations SA, the French Government and the Commission at the hearing on 14 December 2000,

after hearing the Opinion of the Advocate General at the sitting on 6 March 2001,

gives the following

Judgment

1 By judgment of 6 January 2000, received at the Court on 19 January 2000, the tribunal administratif de Lille (Administrative Court, Lille) referred to the Court for a preliminary ruling under Article 234 EC three questions on the interpretation of Article 4(1) and (2), Article 13B(d) and Article 17(2)(a) and (5) of the 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').

2 Those questions were raised in proceedings between Cibo Participations SA ('Cibo') and the Directeur régional des impôts du Nord-Pas-de-Calais (Regional Director for Taxes, Nord-Pas-de-Calais) concerning the question whether, and if so, to what extent, a holding company may deduct value added tax ('VAT') charged on services purchased in the context of the acquisition of shareholdings in its subsidiaries.

Relevant Community legislation

3 Article 2(1) of the Sixth Directive provides that the supply of goods or services effected for consideration within the territory of the country by a taxable person acting as such is subject to VAT. Under Article 4(1) of the Sixth Directive any person who independently carries out any economic activity specified in Article 4(2) is a taxable person. 'Economic activities' are defined in Article 4(2) as comprising all activities of producers, traders and persons supplying services

including the exploitation of tangible or intangible property for the purpose of obtaining income therefrom on a continuing basis.

4 Article 13B(d)(5) of the Sixth Directive provides as follows:

'Without prejudice to other Community provisions, Member States shall exempt...:

...

(d) the following transactions:

...

(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)'.

5 Article 17 of the Sixth Directive, headed 'Origin and scope of the right to deduct', provides, in paragraph 2 (a), that '[i]n 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... value added tax due or paid in respect of goods or services supplied or to be supplied to him by another taxable person'.

6 As regards goods and services used by a taxable person both for transactions in respect of which VAT is deductible and for transactions in respect of which it is not deductible, the first subparagraph of Article 17(5) of the Sixth Directive provides that 'only such proportion of the value added tax shall be deductible as is attributable to the former transactions'. The second subparagraph of Article 17(5) states that '[t]his proportion shall be determined, in accordance with Article 19, for all the transactions carried out by the taxable person'.

7 Article 19(1) and (2) of the Sixth Directive provides:

'1. The proportion deductible under the first subparagraph of Article 17(5) shall be made up of a fraction having:

— as numerator, the total amount, exclusive of value added tax, of turnover per year attributable to transactions in respect of which value added tax is deductible under Article 17(2) and (3),

— as denominator, the total amount, exclusive of value added tax, of turnover per year attributable to transactions included in the numerator and to transactions in respect of which value added tax is not deductible. The

Member States may also include in the denominator the amount of subsidies, other than those specified in Article 11A(1)(a).

The proportion shall be determined on an annual basis, fixed as a percentage and rounded up to a figure not exceeding the next unit.

2. By way of derogation from the provisions of paragraph 1, there shall be excluded from the calculation of the deductible proportion, amounts of turnover attributable to the supplies of capital goods used by the taxable person for the purposes of his business. Amounts of turnover attributable to transactions specified in Article 13B(d), in so far as these are incidental transactions, and to incidental real estate and financial transactions shall also be excluded....'

The facts in the main proceedings and the questions referred for a preliminary ruling

8 Cibo is a holding company which owns significant shareholdings in three undertakings specialising in bicycles. It was created by the company Compagnie d'importation des laines ('CIL'), its majority shareholder.

9 It is apparent from the judgment of the Administrative Court, Lille, that Cibo has challenged before that court a demand to pay VAT arising from the refusal of the tax authorities to allow Cibo to deduct VAT, for the period from 2 November 1993 to 31 December 1994, in respect of the supply of various services for which

it was invoiced by third parties in connection with the acquisition of shares in its subsidiaries. The services in question included the auditing of the companies, assistance with the negotiation of the purchase price of the shares, organising the take-over of the companies and legal and tax services.

10 In support of its application for deduction of VAT, Cibo has pointed out that its chairman became the chairman of the three subsidiaries, that it provides services to those subsidiaries against payment, that CIL makes available, against payment, qualified staff to work in its subsidiaries in general, administrative, financial, commercial and technical management, and that the subsidiaries were invoiced for those services on a flat-rate basis of 0.5% of their turnover. Cibo maintains that it is thus involved in the management of its subsidiaries and that, consequently, the expenditure linked to its acquisition of shares falls within the scope of VAT as general expenses, given that it pertains to the holding company's general business.

11 According to the national court, the French tax authorities reply that Cibo derives most of its turnover from the receipt of dividends. Moreover, it conducts no commercial transactions in its own name and the companies within the group remain legally independent. Apart from its financial role, Cibo does no more than act as consultant and direct group policy, in respect of which it receives remuneration. The French authorities submit that, consequently, Cibo is neither directly nor indirectly involved in the management of its subsidiaries. The expenditure arising from its acquisition of shareholdings has no connection with the services which it provides to its subsidiaries. It merely relates to its ownership of shares and receipt of dividends, which fall outside the scope of VAT.

12 In the event that Cibo were nevertheless to be regarded as being involved in the management of its subsidiaries, the French tax authorities maintain that the dividends must be associated with the company's economic activity and thus with

its income falling within the scope of VAT, but that, given that they are exempted in accordance with Article 13B(d) of the Sixth Directive, a pro-rata deduction should be made.

13 Those were the circumstances in which the Administrative Court, Lille, resolved to stay proceedings and refer the following questions to the Court of Justice for a preliminary ruling:

'1. What are the criteria for establishing "involvement"? Can it be inferred from the provision of paid services or the running of a group of companies by its holding company, or *de facto* management precluding independence on the part of a subsidiary, or some other factor?

2. Where there is involvement, does the receipt of dividends remain outside the scope of value added tax for any reason other than economic activity, in that such receipts are not the consideration for the supply of goods or services or, having regard to the fact that expenditure is incurred in connection with the acquisition of shares the direct purpose of which is to enable participation in economic activity, do dividend receipts fall within the scope of value added tax and, if so, are they exempt under Article 13B(d)(1) of the Sixth Directive or taxable?

3. If the receipt of dividends does remain outside the scope of value added tax, what are the implications for the right to deduct:

— does no right remain to deduct tax on expenditure incurred in acquiring shares, given that that expenditure does not relate to a taxable transaction,

— or is deduction allowed under the heading of general costs?'

The questions referred for a preliminary ruling

The first question

14 By its first question, the national court essentially asks what are the criteria for establishing whether the involvement of a holding company in the management of companies in which it has acquired a shareholding constitutes an economic activity within the meaning of Article 4(2) of the Sixth Directive.

Observations submitted to the Court

15 Cibo argues that the acquisition of shares in an undertaking may entail involvement in the management of the undertaking and thus amount to an economic activity falling within the scope of VAT in two situations. The first is where essentially all the share capital is acquired and the shareholder takes on responsibility for its subsidiary's destiny, has a hand in its management and appoints its directors, albeit without encroaching on its legal personality. In such a case, the shareholder will most likely be prompted to provide its subsidiary with services against payment. The second situation is similar to the first, except that

the holding company does encroach upon the normal running of the subsidiary by providing *de facto* management.

16 The French Government's opinion on the matter is that involvement means the exercise of a decisive influence on the management of a subsidiary. If the decisions of a subsidiary are dictated by an undertaking which pursues a similar or complementary company object because it has, in law or in fact, a majority of the voting rights, that implies involvement. Involvement may also be established on the basis of a body of evidence derived from analysing, subject to review by the court having jurisdiction in taxation matters, the legal, financial, company and administrative relations of the undertakings concerned. The simple fact that services are provided to a subsidiary against payment does not establish involvement.

17 The Commission maintains that the proper approach to the questions referred for a preliminary ruling must proceed from a consideration of how the transactions may be defined in terms of Article 4 of the Sixth Directive, read together with Article 2 thereof. It observes that Cibo is a mixed holding company inasmuch as, in addition to managing its portfolio, it carries out distinct advisory and managerial tasks for its subsidiaries, for which it receives remuneration. It is necessary to determine, for each item of expenditure incurred by such a holding company, whether the item in question is connected with transactions falling outside the scope of the Sixth Directive, or with transactions which do fall within that scope but are exempt, or with transactions which fall within the directive's scope and are not exempt.

Findings of the Court

18 The Court has consistently held that Article 4 of the Sixth Directive must be interpreted as meaning that a holding company whose sole purpose is to acquire holdings in other undertakings and which does not involve itself directly or

indirectly in the management of those undertakings, without prejudice to its rights as a shareholder, does not have the status of taxable person and has no right to deduct tax under Article 17 of the Sixth Directive (Case C-60/90 *Polysar Investments Netherlands* [1991] ECR I-3111, paragraph 17, and Case C-142/99 *Floridienne and Berginvest* [2000] ECR I-9567, paragraph 17).

19 It is clear from case-law that that conclusion is based, amongst other things, on the finding that the mere acquisition and holding of shares in a company is not to be regarded as an economic activity, within the meaning of the Sixth Directive, conferring on the holder the status of a taxable person. The mere acquisition of financial holdings in other undertakings does not amount to the exploitation of property for the purpose of obtaining income therefrom on a continuing basis because any dividend yielded by that holding is merely the result of ownership of the property (see the judgments in Case C-333/91 *Sofitam* [1993] ECR I-3513, paragraph 12, and in Case C-80/95 *Harnas & Helm* [1997] ECR I-745, paragraph 15).

20 However, the Court has held that it is otherwise where the holding is accompanied by direct or indirect involvement in the management of the companies in which the holding has been acquired, without prejudice to the rights held by the holding company as shareholder (*Polysar*, paragraph 14, and *Floridienne and Berginvest*, paragraph 18).

21 It is clear from paragraph 19 of the judgment in *Floridienne and Berginvest* that direct or indirect involvement in the management of subsidiaries must be regarded as an economic activity within the meaning of Article 4(2) of the Sixth Directive where it entails carrying out transactions which are subject to VAT by virtue of Article 2 of that directive, such as the supply by a holding company such as Cibo of administrative, financial, commercial and technical services to its subsidiaries.

22 The answer to the first question referred for a preliminary ruling must therefore be that the involvement of a holding company in the management of companies in which it has acquired a shareholding constitutes an economic activity within the meaning of Article 4(2) of the Sixth Directive where it entails carrying out transactions which are subject to VAT by virtue of Article 2 of that directive, such as the supply by a holding company to its subsidiaries of administrative, financial, commercial and technical services.

The third question

23 By its third question, which it is appropriate to consider before the second, the national court essentially asks whether a holding company may deduct VAT charged on expenditure incurred in respect of various services obtained in connection with the acquisition of a shareholding in a subsidiary.

Observations submitted to the Court

24 Cibo argues that a company that is involved in the management of its subsidiaries generates taxable receipts from the services which it provides to its subsidiaries. It states that it is clear from the judgment in Case C-4/94 *BLP Group* [1995] ECR I-983, which concerned a mixed holding company that had disposed of shares in a subsidiary, that VAT charged on services provided in the context of such a transaction may not be deducted in so far as the transaction constitutes an exempt transaction and the services have a direct and immediate link with it. The purchaser of shares who, as purchaser, carries out no taxable or exempt transaction, ought therefore to be able to deduct VAT on services of the same type, which would fall under the heading of general expenses.

25 The French Government takes the view that, since an undertaking which acquires, holds or disposes of shares in another undertaking in the management of which it is directly involved, is a taxable person for the purposes of VAT by virtue of Articles 2 and 4 of the Sixth Directive, expenditure incurred in connection with the acquisition of such shareholdings must be regarded as relating to the general business of the undertaking, which is to carry out transactions in respect of which VAT is deductible and to receive exempt dividends in respect of which it is not deductible.

26 The Commission submits that there is no right of deduction of tax chargeable on expenditure incurred in connection with the acquisition of shares in so far as such expenditure does not relate to any transaction falling within the scope of VAT.

Findings of the Court

27 It should be observed at the outset that the deduction system is meant to relieve the trader entirely of the burden of the VAT payable or paid in the course of all his economic activities. The common system of VAT consequently ensures complete neutrality of taxation of all economic activities, whatever their purpose or results, provided that they are themselves subject in principle to VAT (Case C-98/98 *Midland Bank* [2000] ECR I-4177, paragraph 19, and Case C-408/98 *Abbey National* [2001] ECR I-1361, paragraph 24).

28 Article 17(5) of the Sixth Directive, in the light of which Article 17(2) must be interpreted, lays down the rules applicable to the right to deduct VAT where the VAT relates to input transactions used by the taxable person 'both for transactions covered by paragraphs 2 and 3, in respect of which value added tax is deductible, and for transactions in respect of which value added tax is not

deductible', limiting the right of deduction to that portion of the VAT which is attributable to the former transactions. The use of the words 'for transactions' in Article 17(5) shows that, in order to give rise to the right to deduct under paragraph 2, the goods or services acquired must have a direct and immediate link with the output transactions in respect of which VAT is deductible, and that the ultimate aim pursued by the taxable person is irrelevant in this respect (see *BLP Group*, paragraphs 18 and 19, *Midland Bank*, paragraph 20, and *Abbey National*, paragraph 25).

29 According to settled case-law, Article 2 of the 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, hereinafter 'the First Directive') and Article 17(2), (3) and (5) of the Sixth Directive must be interpreted as meaning that, in principle, the existence of a direct and immediate link between a particular input transaction and a particular output transaction or transactions in respect of which VAT is deductible is necessary before the taxable person is entitled to deduct input VAT and in order to determine the extent of such entitlement (*Midland Bank*, paragraph 24, and *Abbey National*, paragraph 26).

30 It should also be borne in mind that, according to the fundamental principle which underlies the VAT system, and which follows from Article 2 of the First Directive and Article 2 of the Sixth Directive, VAT applies to each transaction by way of production or distribution after deduction of the VAT directly borne by the various cost components (*Midland Bank*, paragraph 29, and *Abbey National*, paragraph 27).

31 It follows from that principle, as well as from the rule that, in order to give rise to the right to deduct, the goods or services purchased must have a direct and immediate link with the output transactions in respect of which VAT is deductible, that there was a right to deduct the VAT borne by those goods or services because the expenditure incurred in acquiring them was a component of

the cost of those output transactions. The expenditure must therefore form part of the costs of the output transactions in respect of which VAT is deductible which use the goods and services acquired (*Midland Bank*, paragraph 30, and *Abbey National*, paragraph 28).

32 Clearly, there is no direct and immediate link between the various services purchased by a holding company in connection with its acquisition of a shareholding in a subsidiary and any output transaction or transactions in respect of which VAT is deductible. The amount of VAT paid by the holding company on the expenditure incurred for those services does not directly burden the various cost components of its output transactions in respect of which VAT is deductible. That expenditure does not form part of the costs of the output transactions which use the services.

33 On the other hand, the costs of those services are part of the taxable person's general costs and are, as such, cost components of an undertaking's products. Such services therefore do, in principle, have a direct and immediate link with the taxable person's business as a whole (see *BLP Group*, paragraph 25, *Midland Bank*, paragraph 31, and *Abbey National*, paragraphs 35 and 36).

34 In this connection, it is clear from the first paragraph of Article 17(5) of the Sixth Directive that, where a taxable person uses goods and services in order to carry out both transactions in respect of which VAT is deductible and transactions in respect of which it is not, he may deduct only that proportion of the VAT which is attributable to the former.

35 The answer to the third question referred for a preliminary ruling must therefore be that expenditure incurred by a holding company in respect of the various services which it purchased in connection with the acquisition of a shareholding in a subsidiary forms part of its general costs and therefore has, in principle, a direct and immediate link with its business as a whole. Thus, if the holding

company carries out both transactions in respect of which VAT is deductible and transactions in respect of which it is not, it follows from the first paragraph of Article 17(5) of the Sixth Directive that it may deduct only that proportion of the VAT which is attributable to the former.

The second question

36 By its second question, the national court seeks, essentially, to establish whether the receipt of dividends falls within the scope of VAT.

Observations submitted to the Court

37 Cibo argues that the receipt of dividends can never fall within the scope of VAT as defined by the Sixth Directive. Nor does it matter, in its submission, whether or not the holding company in question involves itself in the management of its subsidiaries. Firstly, dividends are not the consideration for any given act or transaction performed by the shareholder and are unconnected with the business of management that may be undertaken by the shareholder in a case of involvement. Secondly, dividends are merely a consequence of the ownership of shares.

38 The French Government submits that the receipts of a holding company, and in particular dividends, fall within the scope of VAT where they are derived from

shareholdings in an undertaking in whose management the holding company is involved. Such receipts are necessarily derived from the exploitation of property for the purpose of obtaining income therefrom on a continuing basis within the meaning of Article 4(2) of the Sixth Directive. The fact that the receipt of dividends is, by nature, contingent is irrelevant.

39 Nevertheless, whilst dividend receipts do fall within the scope of VAT, they are exempt under Article 13B(d)(5) of the Sixth Directive. Thus, given that they fall within the scope of VAT but do not amount to transactions in respect of which VAT is deductible, they should be included solely in the denominator used for calculating the deductible proportion under Article 17(5) and Article 19(1) of the Sixth Directive.

40 According to the Commission, dividend receipts cannot be regarded as consideration for management undertaken by a holding company where there is no real, direct link between the two (see Case C-16/93 *Tolsma* [1994] ECR I-743, paragraphs 13 and 14). In a case such as that of the main proceedings, there is no such direct link.

Findings of the Court

41 The Court has already had occasion to hold that, since the receipt of dividends is not the consideration for any economic activity, it does not fall within the scope of VAT. Consequently, dividends resulting from shareholding fall outside the

deduction entitlement (*Sofitam*, paragraph 13, and *Floridienne and Berginvest*, paragraph 21).

42 Certain features of dividends account, in particular, for their exclusion from VAT. First, it is not in dispute that the existence of distributable profits is generally a prerequisite of paying a dividend and that payment is thus dependent on the company's year-end results. Second, the proportions in which the dividend is distributed are determined by reference to the type of shares held, in particular by reference to classes of shares, and not by reference to the identity of the owner of a particular shareholding. Lastly, dividends represent, by their very nature, the return on investment in a company and are merely the result of ownership of that property (*Polysar*, paragraph 13, and *Floridienne and Berginvest*, paragraph 22).

43 In view, specifically, of the fact that the amount of the dividend thus depends partly on unknown factors and that entitlement to dividends is merely a function of shareholding, the direct link between the dividend and a supply of services, which is necessary if the dividends are to constitute consideration for the services, does not exist even where the services are supplied by a shareholder who is paid dividends (*Floridienne and Berginvest*, paragraph 23).

44 In the circumstances, it is appropriate to emphasise that, since the receipt of dividends does not fall within the scope of VAT, dividends paid by subsidiaries to their holding company which is a taxable person in respect of other activities and which supplies management services to those subsidiaries must be excluded from the denominator of the fraction used to calculate the deductible proportion under Article 19 of the Sixth Directive (*Floridienne and Berginvest*, paragraph 32).

45 The answer to the second question is therefore that the receipt of dividends does not fall within the scope of VAT.

Costs

46 The costs incurred by the French Government and by the Commission, which have submitted observations to the Court, are not recoverable. Since these proceedings are, for the parties to the main action, a step in the proceedings pending before the national court, the decision on costs is a matter for that court.

On those grounds,

THE COURT (First Chamber),

in answer to the questions referred to it by the tribunal administratif de Lille by judgment of 6 January 2000, hereby rules:

1. The involvement of a holding company in the management of companies in which it has acquired a shareholding constitutes an economic activity within the meaning of Article 4(2) of the 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, where it entails carrying out transactions which are subject to value added tax by virtue of Article 2 of that directive, such as the supply by a holding company to its subsidiaries of administrative, financial, commercial and technical services.

2. Expenditure incurred by a holding company in respect of the various services which it purchases in connection with the acquisition of a shareholding in a subsidiary forms part of its general costs and therefore has, in principle, a direct and immediate link with its business as a whole. Thus, if the holding company carries out both transactions in respect of which value added tax is deductible and transactions in respect of which it is not, it follows from the first subparagraph of Article 17(5) of the Sixth Directive 77/388 that it may deduct only that proportion of the value added tax which is attributable to the former.

3. The receipt of dividends does not fall within the scope of value added tax.

Wathelet Jann Sevón

Delivered in open court in Luxembourg on 27 September 2001.

R. Grass

Registrar

M. Wathelet

President of the First Chamber