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By PwC Deutschland | 14. Juli 2011

Purchase of bad debts not subject to VAT?

An ECJ advocate general has suggested the purchase of a bad debt portfolio be seen as such and therefore as exempt from VAT. If, however, it is a debt collection service, the VAT basis is the difference between the purchase price and the subsequent collections.

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A German bank sold a portfolio of debts from private customers secured by mortgages on crisis-hit housing for just over one-half of their face value. In each case, the mortgage had fallen in and the full debt was currently due, following debtor default on the repayment instalments. The buyer, a financial services company, clearly considered itself better able than the bank to pursue defaulters ruthlessly, presumably because it would not need to protect future business relations with the debtors as customers and because it would not be exposed to the same public pressures when evicting the previous owners from the properties. The tax office saw the transaction as a debt collection service for the bank and demanded VAT on the difference between the selling price of the portfolio and its “economic value”. This latter was a notional amount based on the collection expectation discounted over the estimated time needed to collect. The taxpayer saw the transaction as a simple purchase of debt and as such, VAT-free. The question turns on the interpretation of the relevant clauses in the Sixth Directive and this brought the case before the ECJ.

The advocate general accepts that the bank could well have enjoyed a service in that it was relieved of the undoubtedly distasteful burden of debt collection from the impoverished. However, it had actually sold its debts as they stood together with all relevant documentation for pursuit of the debtors, but without granting the buyer any right of recourse, or otherwise accepting any responsibility for future developments. The price had been calculated on the buyer’s specific assessment of his chances and risks of collection and therefore corresponded to the market value of the debts. Nothing in the price was attributable to a service element; thus there was no basis for charging VAT.

However, the advocate general went on to add that if the court cannot accept this view, the only other possibility is to regard the transaction as the taxable service of debt collection. Since there can be no question of estimating the consideration for a service rendered, the basis for VAT can only be the difference between the amount paid for the portfolio and the amount ultimately collected from the debtors. The advocate general accepts that this will delay the VAT assessment, but adds that „consideration can accrue over time”. However, he does not go into further detail and does not go on to discuss the various other questions requiring resolution before an actual assessment can be raised.

The ECJ case reference is C-93/10 *GFKL* opinion of July 14, 2011.

Schlagwörter

bad debt, debt collection, mortgage