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Organisational integration of VAT group must be enforceable by parent

The Supreme Tax Court has held that a subsidiary is too independent to join a VAT group if its sole director is able to block his own removal from office.

A senior member of the management team of a trading entity entered into a special purpose joint venture with his employer. They formed a GmbH for the venture, the company holding 51% of the shares and the individual 49%. However, resolutions appointing and removing directors, and agreements on their remuneration, required the approval of both founding members. The individual was appointed the GmbH's sole director and elevated to the position of deputy director of the parent. The parent then sought to bring the subsidiary into its VAT group on the basis that the two businesses were integrated, organisational (management) integration being ensured by the discipline on the subsidiary's managing director in his capacity as a senior employee of the parent. The tax office rejected this approach because the common management necessary for management integration meant that the two entities had to have at least one common director.

The lower tax court agreed with the tax office' conclusion, but disagreed with the reasoning. Management integration was feasible as long as the director of the subsidiary held a senior management position with the parent. He did not, though, have to be a director of both companies. On the other hand, the company, as majority shareholder, would be unable to impose its will on the subsidiary where that company's minority shareholder was its sole managing director.

The Supreme Tax Court has now rejected the reasoning of the lower tax court (and also that of the tax office), but has found its own grounds for rejecting the VAT group. Its position is that the managing director of the subsidiary cannot be removed from office without his own approval as a founding shareholder. Conflicts between the two managements cannot therefore be resolved by parental action on its own, but only by compromise. Thus, the managerial will of the subsidiary is not totally subordinate to that of the parent.

The upshot as summarised by the court is that managerial integration will be assumed if the sole director of the subsidiary holds a leading managerial position with the parent, provided the parent holds far-reaching powers of direction over the management of the subsidiary and has the right to appoint and remove the subsidiary's director(s). However, the court has explicitly left open, the question of whether it continues to adhere to its own older case law to the effect that it is sufficient demonstration of management integration to show that the subsidiary cannot, in the circumstances, form its own will independent of that of the parent.

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