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By PwC Deutschland | 26. April 2012

# Sale of bad debts without recourse not a provision of services

**The Supreme Tax Court has held that the sale of currently due, but doubtful, debts at their agreed market value and without further recourse to, or obligations towards, the seller is a VAT-free sale of debts, rather than a taxable debt collection.**

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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 disguised 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. Since the question turned on the interpretation of the relevant clauses in the Sixth Directive the Supreme Tax Court brought the case before the ECJ who in its judgement of October 2011 decided that the ‘supply of services effected for consideration’ requires the existence of a direct link between the service provided and the consideration received. Since the buyer received no consideration from the bank, he therefore it did not carry out an economic activity or effect a supply of services within the meaning of the relevant sections in the Sixth Directive.

Following the verdict of the ECJ, the Supreme Tax Court in the end confirmed the view of the taxpayer and ruled that a sale of debts at an agreed valuation and without recourse back to the seller is not a disguised debt collection service. Over and under recoveries compared with the written down sales value (on average some 60% of the nominal) were for the sole account of the purchaser. He had purchased assets with the intention of realisation. He was under no further duties towards the seller, but the latter was also free of all further obligations towards him and towards the mortgage debtors. The court also emphasized, that the buyer - in light of the services being non-taxable - could not claim recovery of those input VAT which is attributable and related to either the purchase of debts or the debt collection. (mh)

Supreme Tax Court judgment V R 18/08 of January 26, 2012 - published on March 7, 2012

**Schlagwörter**

Sale of bad debts, debt collection, doubtful debts, without recourse