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By PwC Deutschland | 08. Februar 2019

European Court of Justice: Deductible input VAT of a branch located in another Member State

In its judgment in Morgan Stanley (C-165/17) on 24 January 2019, the ECJ ruled on the ratio of deductible input tax in relation to the internal supplies of a French branch to its head office, a financial service provider in the UK.

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In determining the level of deductible input VAT on supplies received by the branch and applied by it to provide internal services to the parent company established in another Member State, a specific ratio for the deduction of input VAT must be applied which, takes into account the turnover of the parent company.

Background

Morgen Stanley, a financial service provider operated a Paris branch, as a fixed establishment, which was subject to VAT in France.

During the course of certain tax audits, it was established that the branch carried out both banking and financial transactions on behalf of local clients, in respect of which it had opted to be liable to VAT, as well as internal services to its head office in the UK, in return for which it received transfers. The branch deducted all of the input VAT on expenditure attributable to both categories of services.

The tax authorities allowed only a proportional deduction on the input VAT on expenditure attributable to the internal services and to the mixed services according to specific keys.

The appeal reached the Conseil d'État (Council of State,)which decided to stay the proceedings and to refer the following questions to the ECJ for a preliminary ruling:

- In circumstances where expenditure of a branch established in one Member State is exclusively used for the transactions of its principal establishment established in another Member State, must the Member State in which the branch is registered (i) apply to that expenditure the branch's deductible proportion, determined according to the transactions carried out in the Member State in which it is registered and according to the rules applicable in that State, or (ii) apply the proportion applicable to the principal establishment, or (iii) deduct a specific proportion combining the rules applicable in the Member States in which the branch and the principal establishment are registered?
- What rules should be applied in the specific case where expenditure borne by the branch is used both for transactions in the Member State where it is registered and for transactions of the principal establishment, particularly as regards the concept of general costs and the proportion of tax deductible?

Decision

The ECJ decided that the French branch could not calculate the deductible input VAT purely on the basis of its own output transactions.

Following settled case law (TGE Gas Engineering, C-16/17), the Court stated that a principal establishment and its branch constituted a single taxable person for VAT purposes, unless it could be established that the branch carried out an independent economic activity. It,therefore, followed that where the internal supplies of the branch to the principal establishment are linked to the transactions of the principal establishment ("linked transactions"), the turnover of the principal establishment must be taken into account when

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calculating the deductible input VAT.

More specifically, the ECJ held that, in relation to branch expenditure for goods and or services linked exclusively to mixed transactions (i.e. those subject to VAT and those VAT exempt) performed by the principal establishment in the other Member State, a proportional deduction should be applied. This should be calculated from a fraction the denominator of which is formed by the turnover, exclusive of VAT, made up of all transactions linked to the expenditure and the numerator of which is formed by the taxable transactions in respect of which VAT would also be deductible if they had been carried out in the Member State in which that branch is registered.

In relation to the deductible proportion applicable to the general costs of the branch, which were used for both transactions of the branch and transactions of the principal establishment in the other Member State, the denominator of the fraction should be made up of all linked transactions carried out by both the branch and the principal establishment, and the numerator of that fraction, should be made up of the taxed transactions carried out by the branch and those taxed transactions carried out by the principal establishment, in respect of which VAT would also be deductible if they had been carried out in the State in which the branch concerned is registered.

Source European Court of Justice decision of 24 January 2019, Morgan Stanley International plc (C-165/17)

Schlagwörter

branch, input VAT deduction