Court of Justice of the European Union
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Press and Information

Judgment in Case C-388/11
Le Crédit Lyonnais v Ministre du Budget, des Comptes Publics et de la Réforme de l'Etat

A company whose principal establishment is in a Member State may not take into account, in order to calculate its deductible proportion of VAT, the turnover of its branches established abroad

The Sixth VAT Directive does not provide for the application of 'a worldwide proportion'

Following an examination of its accounts, the bank Le Crédit Lyonnais (LCL), which has its principal establishment in France and branches abroad, was the subject of two adjustment notices. The French tax administration assessed it for arrears, inter alia, of VAT in respect of the period between 1 January 1988 and 31 December 1989, complaining that it took into account the amount of interest on loans granted to its branches established outside France in order to calculate the deductible proportion of VAT applicable to the bank.

LCL brought three objections claiming the refund of VAT which the bank considered it had overpaid in respect of the years 1988 to 1990 (almost €31.7 million). Since the tax administration rejected those objections, LCL brought an action before the French administrative courts, maintaining that, while the amount of interest invoiced by the principal establishment to the branches could not be taken into account on the ground that its principal establishment, together with its foreign branches, all formed part of one and the same entity, the income from the transactions which the branches carry out with third parties should be regarded as their own income and be taken into account in calculating the deductible proportion applied to it ('worldwide turnover').

Since its action and the appeal were rejected, LCL brought proceedings before the Conseil d'État (Council of State) (France) which decided to ask the Court of Justice a question concerning the interpretation of the Sixth VAT Directive[1]. The question at issue is whether a company whose principal establishment is situated in a Member State and which has branches abroad must, when complying with its tax obligations vis-à-vis the Member State of the principal establishment – to the extent that it carries out transactions in respect of which VAT is deductible and transactions in respect of which it is not – take into account or not, in order to calculate its deductible proportion of VAT, its total turnover, that is to say include both that of the principal establishment and that of its various branches.

In its judgment today, the Court notes, first, that the deduction system laid down in the directive 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 those activities are subject to VAT. In particular, where the VAT relates to goods or services used by the taxpayer both for transactions in respect of which VAT is deductible and for transactions in respect of which it is not, only such proportion of the VAT is deductible as is attributable to the former taxable transactions. The right to deduct is quantified according to a proportion fixed in accordance with the directive[2]. In so far as the calculation of the deductible proportion constitutes an element of the deduction system, the manner in which that calculation must be carried out falls within the scope of

[1] 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).
[2] Article 19 of Directive 77/388/EEC.

the national VAT legislation to which an activity or transaction must be linked for tax purposes (territoriality principle). It is therefore for the Member States' tax authorities to lay down the method for determining the right to deduct, permitting them to provide for determination of a separate proportion for each sector of business or deduction on the basis of the use made of all or part of the goods and services for a specific activity, or they may even exclude the right of deduction in certain circumstances.

The Court also makes clear that the method of repayment of VAT (by deduction or by refund) depends solely on the place where the taxable person is established (principal establishment but also any fixed establishments situated in the other Member States). Thus, a company which has its principal establishment in one Member State and a fixed establishment in another Member State must be considered, by virtue of that fact, as being established in the last-mentioned Member State for the activities carried out there and can no longer claim a refund of the VAT. It is for that fixed establishment to seek, from the tax authorities of that State, deduction of VAT in respect of the acquisitions made there.

Since the Court has held that the fixed establishment situated in a Member State and the principal establishment situated in another Member State constitute a single taxable person subject to VAT, it follows that **a taxpayer is subject, in addition to the system which applies in the State of its principal establishment, to as many national systems of deduction as there are Member States in which it has fixed establishments**.

As the methods of calculation of the proportion constitute a fundamental element of the deduction system, account cannot be taken, in the calculation applicable to the principal establishment of a taxpayer established in a Member State, of the turnover of all of the taxable person's fixed establishments in the other Member States.

Furthermore, the Court replies, second, that the directive must be interpreted as meaning that, **in determining the deductible proportion of VAT applicable to it, a company, the principal establishment of which is situated in a Member State, may not take into account the turnover of its branches established in third States.**

There is no support in the directive for a finding that the fact that a taxable person has a fixed establishment outside the EU can affect the deduction system to which that taxable person is subject in the Member State in which its principal establishment is situated. The Court thus rejects LCL's argument according to which a company which has a branch in a third State must, for VAT purposes, be treated in the same way as a company which has a subsidiary in that State. In fact, according to the Court, those different possibilities reflect situations which are clearly different and cannot therefore be treated in the same way by the tax system.

The Court holds, third, that the **directive does not permit a Member State to adopt a rule for the calculation of the deductible proportion per sector of business** of a company subject to tax which authorises that company to take into account the turnover of a branch established in another Member State or in a third State.

The concept of 'sectors of business' refers not to geographic areas but to different forms of economic activities such as the activities of producers, traders and persons supplying services.

NOTE: A request for a preliminary ruling allows the courts and tribunals of the Member States, in disputes which have been brought before them, to refer questions to the Court of Justice about the interpretation of European Union law or the validity of a European Union act. The Court of Justice does not decide the dispute itself. It is for the national court or tribunal to dispose of the case in accordance with the Court's decision, which is similarly binding on other national courts or tribunals before which a similar issue is raised.

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