

Case C-59/20

Summary of the request for a preliminary ruling pursuant to Article 98(1) of the Rules of Procedure of the Court of Justice

Date lodged:

4 February 2020

Referring court:

Bundesfinanzgericht (Federal Finance Court, Austria)

Date of the decision to refer:

29 January 2020

Appellant:

DBKAG

Defendant authority:

Finanzamt Linz (Tax Office, Linz)

The subject matter and legal basis of the dispute in the main proceedings and the reference for a preliminary ruling

Exemption from value added tax ('VAT') of an outsourced service in connection with the management of special investment funds in accordance with Article 135(1)(g) of Directive 2006/112/EC, in the form of licensing of a calculation software used to provide part of the management tasks

Question referred

Must Article 135(1)(g) of Directive 2006/112/EC be interpreted as meaning that, for the purposes of the tax exemption provided for by that provision, the term "management of special investment funds" also includes the granting by a third-party licensor to an investment management company ('IMC') of a right to use specialist software specifically designed for the management of special investment funds where, as in the case in the main proceedings, that specialist software is intended exclusively to perform specific and essential activities in connection with the management of the special investment funds but runs on the technical

infrastructure of the IMC and can perform its functions only subject to the minor participation of the IMC and subject to ongoing recourse to market data provided by the IMC?

Provisions of EU law cited

Article 44, 135(1)(g) and 196 of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax

Council Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities ('UCITS') in the version in force at the material time (see Annex III Part A of Directive 2009/65/EC)

National legislation cited

Paragraphs 3a(6), 6(1) no. 8(i), 19(1) and 20(1) of the Umsatzsteuergesetz 1994 (German Law on Turnover Tax 1994, BGBl. [Federal Law Gazette] No 663/1994, in the version BGBl. I No 24/2007)

The Investmentfondsgesetz 1993 (German Law on Investment Funds 1993, 'InvFG 1993', BGBl. 532/1993, in the version of BGBl. I, No 69/2008)

Court of Justice case-law relied on

Judgment of 4 May 2006, Case C-169/04, Abbey National plc; judgment of 7 March 2013, Case C-275/11, GfBk Gesellschaft für Börsenkommunikation mbH; judgment of 13 March 2014, Case C-464/12, ATP PensionService A/S; judgment of 9 December 2015, Case C-595/13, Fiscale Eenheid X NV cs; judgment of 5 June 1997, Case C-2/95, SDC; judgment of 13 December 2001, Case C-235/00, CSC; judgment of 26 May 2016, Case C-607/14, Bookit Ltd; judgment of 25 July 2018, Case C-5/17, DPAS Ltd; judgment of 3 October 2019, Case C-42/18, Cardpoint GmbH; judgment of 6 October 1982, Case C 283/81, CILFIT

Summary of the facts and procedure

- 1 DBKAG provides tax-free management of special funds within the meaning of Article 135(1)(g) of Directive 2006/112/EC. In a license agreement dated 11 December 2018, SC GmbH, domiciled in Germany, granted DBKAG an indefinite right of use of the SC software in order to carry out key calculations for the management activities of risk management and performance measurement in return for payment of a one-off license fee. SC guarantees, for a period of 12 months from delivery of the system, that the software has the contractually agreed quality if used in accordance with its intended purpose. In accordance with

the agreement, the SC software is suitable only in combination with DBKAG's other software.

- 2 In other agreements dated 11 December 2008 (service agreement, service and maintenance agreement) various services to be provided by SC in order to support DBKAG, for instance with the implementation of the system or the training of DBKAG employees, were agreed for an indefinite time. In addition to specified services, SC also undertook to remedy any faults in the system by providing software updates.
- 3 SC is only liable for the technical development and/or implementation of the specifications made by DBKAG and, subsequently, the technical operation of the software in order to ensure that the software in question is actually able to provide the agreed service, namely the calculation of risk and performance indicators. Given that the two modules developed by SC have been adjusted to the parameters specified by DBKAG, SC is not liable for any incorrect results that are attributable to the parameters and/or market data supplied by DBKAG; instead, SC is liable, apart from the merely technical aspects, in particular for the preparation of correct calculations of the key performance indicators. DBKAG had no direct influence on the calculations made by the SC software. Under the agreement, SC was liable to DBKAG for any loss or damage caused intentionally and (limited to a certain amount) for grossly negligent conduct and the infringement of intellectual property rights. In that regard, SC may also be liable in the event that administrative penalties are imposed on DBKAG for a breach of statutory provisions as a result of, for instance, incorrect programming or technical faults.
- 4 The right of use granted is restricted in terms of time in that SC provides significant services by way of contractually agreed service and maintenance activities for the use of the software, and a use of the software is no longer possible if those additionally agreed services are no longer requested and paid for. In the event that the cooperation with SC is terminated, the DBKAG must delete all copies of the software and the other related data without delay.
- 5 As part of the preparatory work for the use of SC software, DBKAG was required to adapt the IT environment for software and hardware to the requirements of the SC software. As a next step, DBKAG laid down the parameters vis-à-vis SC (e.g. functions of the software, calculation methods etc.). Before the SC software was able to fulfil its functions, the DBKAG manually incorporated certain values into its own database. This manual preparatory work on the part of DBKAG is also regularly carried out, in particular if details of securities are amended. Part of the data is also imported automatically from the fund's accounting records. The preparatory work accounts for approximately 10% of the daily work of the risk management department. Subsequently, the SC software automatically and independently carries out the daily risk management calculations and the weekly or ad hoc performance calculations.

- 6 Via interfaces to other DBKAG modules the current price data and values required for the calculations are automatically imported into the SC software on a daily basis. The calculations made by the SC software itself do not involve any input from DBKAG. The SC program will also, where necessary, autonomously send warnings to the appropriate employees of DBKAG. After the technical calculation processes have taken place, the calculated risk and key performance data is recorded directly by the SC software in a DBKAG database. DBKAG itself then submits reports to the fund managers and/or reports required by statute to the authorities.
- 7 By way of conclusion, the modules developed by SC ensure that the risk and key performance indicators necessary for the management of special investment funds are calculated within the specified deadlines and thus enable DBKAG to comply with its statutory obligations and the market requirements in connection with risk management and performance measurement.
- 8 In the course of a tax inspection carried out at DBKAG, during which the specific circumstances in which the service was provided were discovered, the tax office found that the grant of the right of use was taxable, and in the subsequent tax proceedings which are now in dispute issued a tax demand for VAT for the service received, which has transferred to DBKAG under the reverse charge system. The questions referred to the Court of Justice in the request for a preliminary ruling were raised by the judge in charge of the appeals brought against the decisions of tax office to the Bundesfinanzgericht (Federal Finance Court).

Principal arguments of the parties in the main proceedings

- 9 According to the tax office, the DBKAG provided the management activities of managing risk and measuring performance itself with the aid of the acquired right of use of the software, and the fact that the use of the software was tolerated could not be reinterpreted as the supply of active management activities. SC did not owe anything other than toleration of the use of the software. All the data and values necessary for the calculations were automatically imported from DBKAG databases or manually inserted by DBKAG employees. The way the services were invoiced also ran counter to the argument that SC was providing active services. At most, tolerance of the use of the software may amount to the provision of technical assistance which was not specific and essential to the management of a special fund. Given the essential contributions made by DBKAG to the two service elements, under no circumstances did SC autonomously provide risk management and performance calculations as a distinct whole. Without the participation of DBKAG, the SC software was not able to carry out the calculations in question. It was also clear from the provisions on liability that SC was liable only for the development of software in accordance with the contract and the subsequent assignment of use, but not for the performance of certain management activities.

- 10 By contrast, **DBKAG** considers that, from an economic point of view and in terms of content, the key parts of the two specific and essential management activities ‘risk and performance calculation’ were in actual fact provided by the SC software and therefore by SC in automated form. SC had provided an outsourced tax-free service for the management of special investment funds within the meaning of Article 135(1)(g) of Directive 2006/112/EC. The VAT assessment had to be undertaken independently of any assessment for purposes of civil law. Tolerance of use only constituted the way in which the services were provided and not their actual content, which was purchased in addition. These automated services provided by the software replaced services which had previously been provided by DBKAG employees. The data made available to DBKAG were accessed automatically by the SC software and incorporated into the program. The fact that the DBKAG carried out certain non-essential elements of the service itself was irrelevant in accordance with the Court’s judgment in GfBK, in which even the fact that the final decision regarding the proposed purchases and sales lay with the customer did not affect the outcome. Furthermore, following that judgment, it was likely that a mere intrinsic connection of the outsourced activity to the exempt management of special investment funds was sufficient for the exemption to apply. SC provided the management activities outsourced to it by way of a whole package consisting of the grant of use of the software and the other service and maintenance activities to be paid for separately and, in principle, for an indefinite period.

Summary of the reasons for the reference for a preliminary ruling

- 11 The Court of Justice of the European Union has previously examined the interpretation of the exemption provided for in Article 135(1)(g) of Directive 2006/112/EC on the management of special investment funds as defined by the Member States on several occasions and has held that management activities transferred to a third-party manager may also fall within the exemption where those services fulfil the specific, essential functions of the management of special investment funds and, viewed broadly, form a distinct whole (see the judgments cited above). However, given the different views regarding the determination of the identity of the service provider, the different interpretation of the scope of the criterion of distinctiveness advocated by the parties in the pending administrative legal proceedings and the possible contradiction between the applicability of criteria for interpretation that narrow down the applicability of the exemption as against the rather broad objective of the exemption provision, the referring court is of the view that justified doubts remain as to the interpretation of the term ‘management of special investment funds’ in conformity with EU law.
- 12 Risk management and performance calculation on the basis of the provisions of the Investmentfondsgesetz 1993 (Law on Investment Funds 1993) constitute, in principle, specific and essential elements of the management of a special investment fund which may, in principle, be outsourced as a tax-exempt management activity, provided that the requisite conditions are met in accordance

with the case-law of the Court of Justice. The parties also agree on the fact that, if the conditions are met, an outsourced service could also be provided by electronic and automated means. Similarly, according to the tax authority, the two SC programs constitute a software that has been specifically adapted to the investment funds business, which takes due account of the complex requirements laid down by law in those areas. On the other hand, the question arises as to whether the licensor or the licensee itself provides the services in question by means of the licensed software and whether, in the event that the services are attributed to the licensor, the services provided for the management of a special investment fund are specific, essential and sufficiently distinct within the meaning of the interpretation previously adopted by the Court of Justice, taking into account the specific circumstances of the case in the main proceedings. While it is true that the calculations and information obtained by means of the licensed software constitute fundamental basics of the two performance elements, the latter are essentially provided as a combination of services provided by DBKAG and SC.

- 13 According to the rules applicable in this case under both the UCITS Directive 85/611/EEG and the transposition of this Directive into national law by way of the Investmentfondsgesetz 1993, it is undisputed that the two management elements of risk management and performance calculation, considered as a whole, have the following specific and legally required functions: (1) continuous measurement and monitoring of the risks inherent in the individual positions and the overall investment profile, (2) meeting reporting and information obligations towards authorities, (3) preparation of the annual report on activities with a comparative overview over the last 5 years detailing performance and (4) meeting information obligations towards investors. DBKAG performs those functions partly with its own staff, its own software, its own or purchased data and also the use of the SC software.
- 14 The aforementioned judgments in SDC, CSC, Bookit Ltd, DPAS Ltd and Cardpoint GmbH concerned exempt financial services, such as transactions concerning payments and transfers or transactions in certain securities, which are specifically mentioned in the applicable VAT Directive. By contrast, in the present case the applicability of the exemption for the transaction ‘management of special investment funds defined as such by the Member States’, which is significantly broader, is in dispute. In that regard, the Court of Justice states, for instance (see paragraph 66 of SDC) that a service specific to a transaction concerning transfers must have the effect of transferring funds and entail changes in the legal and financial situation. The Court’s statements as to the specific nature of the actual financial services cannot therefore unreservedly be applied to the wider ‘management of special investment funds’, in the sense that a service can only be specific if it has a direct impact on the financial situation of the fund (portfolio management in the strict sense). By the Court expressly not accepting, in Abbey National, the argument of the Commission and the United Kingdom that a restrictive interpretation of the concept of ‘management of special investment funds’ was required, the management of a special investment fund is not, in

principle, limited to portfolio management in the strict sense. The Court's statements in that regard concerning the specific nature of the exempt financial services specifically listed cannot therefore be applied to the management of special investment funds. The exemption is not limited to the 'collective investment of capital raised from the public' but to the 'management of a special investment fund'. As regards general statements regarding the exemption of an outsourced service or the possibility of also providing services by electronic means it is, however, possible to have recourse to the judgments cited above. In particular, the question remains as to whether the passive tolerance of the use of the software already constitutes the risk management and performance measurement activity and whether that activity is a distinct whole.

- 15 The objective of the exemption clause, which must be taken into account for the purposes of interpretation, is to facilitate investment in securities for small investors by means of investment undertakings. It is intended to ensure that the common system of VAT is fiscally neutral as regards the choice between direct investment in securities and investment through undertakings for collective investment. Activities specific to and typical of the management of special investment funds must therefore be capable of being outsourced without incurring VAT in order to avoid accidental increases in costs. Thus, in *GfBk* (paragraph 31), the Court of Justice held that an undertaking which provides the exempt service connected to the management through their own staff must not be given an advantage over an undertaking that outsources such services. Questions are raised by the fact that according to the case-law of the Court exemption provisions 'however' (*Abbey National* paragraph 70) must generally be interpreted narrowly and that, therefore, any criteria set by the Court which might restrict the exemption (specificity, essential character and distinctiveness of the service) might run counter to the objective of the exemption which needs to be taken into account.

Management activity by licensor or by licensee

- 16 DBKAG argues that the specific manner in which the service was performed, electronically, automatically or manually, did not affect the application of the exemption. The mere fact that a service was performed entirely by electronic means did not in itself prevent the exemption from applying. On the other hand, if the service only involved the technical and electronic assistance of the person carrying out the essential activities specific to the exemption, the exemption would not be applicable. That conclusion, however, followed from the nature of the service and not from the way in which it was performed (*SDC* paragraph 37).
- 17 According to the judgement in *Abbey National*, paragraph 66 et seq., the management of special investment funds is defined according to the nature of the service provided and not by reference to the identity of the service provider or recipient of the service. In *Bookit*, the Court of Justice added (paragraph 52) that the fact that such a service is provided by electronic means, and in particular the fact that the transmission of the settlement file entails the automatic triggering of

the payments or transfers under consideration, cannot alter the nature of the service provided and, therefore, does not affect the application of the exemption at issue.

- 18 The question referred to the Court of Justice arises, in particular, because in the main proceedings in SDC (in accordance with paragraph 8 et seq.) the service provider did not grant its customers a right of use in a software and SDC provided the services in question by electronic means through its software. It is also apparent from the facts of Bookit that Bookit provided its services without transferring rights to use a software to its customer. By contrast, in the present case, SC tolerated the use of the software by the customer DBKAG in return for a one-off license fee. The question therefore arises whether, in those circumstances, SC itself actually supplies a management activity for special investment funds. In the view of the referring court, it is only after that fundamental question has been answered that it is possible to examine whether the other criteria are met.

Is the service specific, essential and, viewed broadly, a distinct whole

- 19 In the view of the referring court, the aforementioned functions of the service elements of risk management and performance measurement are, in principle, specific to the management of a special fund. In any event, those services are closely linked to the management of the fund, have a direct impact on the financial situation of the fund and have (or allow) a significant and direct impact on the assessment of financial risks or investment decisions.
- 20 In any event, the calculations of the SC software constitute an essential basis for the fulfilment of the aforementioned functions of risk management and performance management which are required by law (see Directive 85/611/EEC). Ultimately, however, the two software modules perform functions 1 and 2 autonomously and provide DBKAG with the main calculation results for functions 3 and 4 to enable it to perform its management tasks. On account of the liability for the functions performed and the distinctiveness of the outsourced management activity in question required by the Court of Justice, the question arises whether the provision of individual service elements can be exempted for the specific functions of risk management and performance improvement.

Regarding liability

- 21 The service exempted under the Directive must be distinguished from the supply of a mere physical or technical service. To that end the national court must, in particular, examine the extent of the liability of the supplier of services vis-à-vis the customer, in particular the question whether that liability is restricted to technical aspects or whether it also extends to the specific functions of the exempt transaction that were taken on (judgments in Bookit, paragraph 40, and DPAS, paragraph 36).
- 22 If one were to assume that risk analysis and performance measurement are specific elements of the management of a special investment fund, it is necessary

to determine the functions that those elements must perform or the results which characterise those functions and whether SC's liability also extends to the results that are specific for each function. The provider of the outsourced risk management and performance measurement service should therefore be liable for the aforementioned essential functions of risk analysis and performance measurement.

- 23 At least inter partes, SC is liable for the first two DBKAG functions. As regards points 3 and 4, SC may be liable given that, in order to perform those functions, DBKAG relies on the key performance indicators obtained by the SC software.
- 24 In the three relevant judgments in *Abbey National*, *GfBk* and *Fiscale Eenheid*, the Court did not address the issue of liability as understood here. It has addressed that aspect in judgments which concerned the exempted financial services specifically designated. In *GfBk*, the Court concluded that the exemption was applicable even though the final liability had remained with the IMC. It therefore seems doubtful whether the question of liability is relevant at all in the circumstances of the present case and, if it is, whether SC's responsibilities are sufficient within the meaning of the case-law of the Court of Justice.

Regarding the required distinctiveness

- 25 According to the referring court, the question whether SC's contribution to the management activities of risk management and performance measurement has an sufficiently high degree of distinctiveness within the meaning of the existing case-law of the Court of Justice in the light of the overall content of the management activities in question and the applicability of the exemption has not been settled.
- 26 In her Opinion in *Abbey National* of 8 September 2009 (point 98 et seq.) the Advocate General explained what is meant by 'viewed broadly, a distinct whole': An argument in favour of a specific and essential management element forming a distinct whole is if not just individual ancillary operations but, so to speak, an inclusive service was taken on. That means that the necessary distinctiveness is attained if the third party takes on a bundle of services which forms an essential part of all the functions arising in the management of the fund.
- 27 According to the tax office, the SC software fulfils at most a partial aspect of the management activity of risk management and performance measurement and, under no circumstances did the SC software take on this management activity in the form of an inclusive service. By contrast, DBKAG claims that, because of the failure to adopt the criterion of sufficient distinctiveness in the judgment of the Court of Justice in *GfBk*, it must be held that the Court does not attach overriding importance to that criterion. In its view, it is essential that the service provider provides its own distinguishable service, which has an intrinsic connection to a management company's own activity. Moreover, the bulk of the service elements in question, namely the calculation of risk and key performance indicators, were

carried out by the SC software. In the light of GfBk, the provision of insubstantial contributions by DBKAG cannot be harmful.

- 28 According to the referring court, it is very clear from in the Court's judgments on the outsourcing of financial services, which were handed down after GfBk (Bookit, DPAS, Fiscale Eenheid, Cardpoint) that the Court of Justice continues to rely on the 'viewed broadly, form a distinct whole' criterion for purposes of applying the exemption to an outsourced activity. According to paragraphs 38 to 41 of Bookit, paragraph 34 of DPAS and paragraph 71 of Fiscale Eenheid, the functional aspects of the activity are decisive. In order to be classified as a transaction for the management of a special investment fund a service must, viewed broadly, form a distinct whole which fulfils the specific, essential functions of the management of a special investment fund. However, the referring court is unclear on how far the distinctiveness of an outsourced management activity has to go in order for it to 'viewed broadly, form a distinct whole'.
- 29 The question arises whether the provision of part of the services concerned is sufficiently distinct and therefore, viewed broadly, forms a distinct whole. If, viewed broadly, a distinct whole is still required, the question arises whether, given the cooperation between DBKAG and SC described above, the service provided by SC is sufficiently distinct within the meaning of the interpretation previously adopted by the Court of Justice.
- 30 Answering the questions regarding the interpretation of Article 135(1)(g) of Directive 2006/112/EC, in particular as regards the scope of the term 'management of a special investment fund', is of fundamental relevance for the decision of the Bundesfinanzgericht in the pending dispute as regards the question of whether the grant of the right of use of the software in question is taxable or exempt from tax. The Bundesfinanzgericht (Federal Finance Court) does not take the view that no doubts remain regarding the interpretation of EU law in the present case, particularly in view of the facts described above which deviate from previous decided cases. Furthermore, in the interests of neutral competition within the European Union, there is an interest in the speedy clarification of the interpretation of the relevant provision of the Directive.