OPINION OF ADVOCATE GENERAL FENNELLY
delivered on 7 November 1996 *

1. This preliminary reference raises essentially the question whether the mere acquisition and holding of bonds can be regarded as an economic activity for the purposes of the Community value added tax (hereinafter 'VAT') regime. In the event of the Court answering this question affirmatively, the questions referred also raise the issue of the extent of the right to deduct VAT on inputs incurred in pursuit of such an activity, in circumstances where such inputs may also be attributable to other activities which fall outside the scope of the VAT Community system.

I — Legal and factual context

The relevant Community and national legislation

2. The scope of the Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of assessment (hereinafter 'the Sixth Directive') [1] is set out in Article 2:

'The following shall be subject to value added tax:

1. the supply of goods or services effected for consideration within the territory of the country by a taxable person acting as such ... .

... .'

3. Article 4(1) provides that '"Taxable person" shall mean any person who independently carries out in any place any economic activity specified in paragraph 2, whatever the purpose or results of that activity'. The concept of an 'economic activity' is defined

* Original language: English.

1 — OJ 1977 L 145, p. 1.

in turn in the following terms by Article 4(2):

'The economic activities referred to in paragraph 1 shall comprise all activities of producers, traders and persons supplying services including mining and agricultural activities and activities of the professions. The exploitation of tangible or intangible property for the purpose of obtaining income therefrom on a continuing basis shall also be considered an economic activity.'

4. Article 13, which is one of the central articles of the Sixth Directive dealing with VAT exemptions, provides, at part B, that 'Member States shall exempt the following under conditions which they shall lay down for the purpose of ensuring the correct and straightforward application of the exemptions and of preventing any possible evasion, avoidance or abuse:

(d) the following transactions:

1. the granting and negotiation of credit and the management of credit by the persons granting it;

... .

5. transactions, including negotiation, excluding management and safekeeping, in shares, interests in companies or associations, debentures and other securities, excluding:

— documents establishing title to goods,

— the rights or securities referred to in Article 5(3).'

5. The origin and scope of the right to deduct is regulated by Article 17. The general principle set out in Article 17(2) provides that the right of a taxable person to deduct 'from the tax which he is liable to pay' will only arise in respect of inputs incurred on 'the goods and services [that] are used for the purposes of his taxable transactions'. Nevertheless, under Article 17(3), Member States are obliged to 'grant to every taxable person the right to a deduction or refund of the value added tax referred to in [Article 17(2)] in so far as the goods and services are used for the purposes of', *inter alia*:

'(c) any of the transactions exempted under Article 13B(a) and (d), paragraphs 1 to 5, when the customer is established outside the Community or when these transac-

tions are directly linked with goods intended to be exported to a country outside the Community.'

6. The first subparagraph of Article 17(5) provides that, as regards those goods and services that 'are used by a taxable person both for transactions covered by paragraphs 2 and 3, in respect of which value added tax is deductible, and for transactions in respect of which value added tax is not deductible, only such proportion of the value added tax shall be deductible as is attributable to the former transactions'. The second subparagraph states that the 'proportion' referred to in the first paragraph 'shall be determined in accordance with Article 19'. Article 19 sets out the rules governing the determination of the fraction that is to be used for calculating that deductible proportion.

7. In its reference in the present case, the Hoge Raad der Nederlanden (Supreme Court of the Netherlands) states that the relevant provisions of the Wet op de Omzetbelasting 1968 [2] (Turnover Tax law, hereinafter 'the Law'), namely, *inter alia*, Articles 7(1) and 11(1)(j)(i) concerning, respectively, the concept of a trader and the granting of credit, must, 'following the adjustment of the Law as of 1 January 1979 to suit the Sixth Directive', be interpreted as having 'the same meaning as the corresponding terms' defined in Articles 4, 13B and 17 of that Directive.

2 — *Staatsblad* 1968, p. 329.

Factual circumstances and procedure

8. At the origin of the proceedings before the national court is a rectified assessment to VAT of Harnas & Helm, a limited partnership (*een commanditaire vennootschap*) based in Amsterdam, which is the appellant in the main proceedings, in the amount of HFL 124 517 for the period 1 January 1987 to 1 March 1991 (hereinafter 'the relevant period'). This assessment was initially upheld, following an administrative appeal brought by Harnas & Helm (hereinafter 'the interested party' or 'the appellant'), by the relevant tax authorities, whose decision was then upheld on appeal by the Gerechtshof, Amsterdam (Regional Court of Appeal, Amsterdam) on 2 March 1994. The interested party subsequently appealed on a point of law against that judgment to the Hoge Raad der Nederlanden (hereinafter 'the national court'). The national court provides the following description of the basis of the appeal.

9. The appellant held during the relevant period shares and bonds issued in the United States of America and Canada, whose value at the end of that period amounted approximately to US $130 000 000, and on which it received dividends and interest respectively. In 1984 the interested party had made an interest-bearing loan, of an unstated amount, to an undertaking called All American Metals. This loan was redeemed on 16 April 1987. On 1 July 1992, the appellant lent CAN $50 000 to Opticast International Corporation. In its tax declaration the interested

party had sought to deduct the turnover tax charged to it. [3] However, the tax authorities took the view that, as of 17 April 1987, the appellant could no longer be regarded as being a trader within the meaning of Article 7 of the Law and, accordingly, they assessed it to the amount of VAT deducted by the appellant during the relevant period, namely HFL 124 517.

10. On appeal the Gerechtshof, Amsterdam found that the business of the interested party comprised, during the relevant period, the holding of shares and bonds issued by public bodies and companies in the United States of America and Canada. [4] It held, in accordance with prevailing social notions, that the procurement of bonds could not be classified as the granting of credit, however much the bond issue supplied the borrowing requirements of the debtor: since, firstly, by opting for a bond issue, a borrower intends to create a security of such a nature that it is likely to generate a wide range of interest on the financial market by facilitating each potentially interested party easily to invest and reinvest his money whenever he wishes, in circumstances where the attendant risk is spread and, secondly, it is irrelevant whether the bonds are acquired by subscription on issue or, as in this case, bought on the stock exchange.

11. That court went on to hold that, in the light of the Court's judgment in *Polysar Investments Netherlands*, [5] the mere acquisition and retention of bonds could not be regarded either as an economic activity or as the exploitation of property for the purpose of obtaining income therefrom on a continuous basis, since the interest yielded on a bond results merely from the ownership of that bond. It concluded that, during the relevant period, the interested party did not perform any economic activities within the meaning of Article 4(2) of the Sixth Directive, and could not thus be regarded as a taxable person under Article 4(1) or as a trader pursuant to Article 7 of the Law.

12. In its appeal to the national court, the interested party contested the view that the acquisition of bonds could not be categorized as the granting of credit. In this respect, while contending that neither the Law nor the Sixth Directive contains any formal provisions relating to the granting of credit, it submitted that, under section 4 of Decree No 282-15703 of the Staatsecretaris

3 — At the hearing counsel for the Netherlands informed the Court that, on the basis of the information available to the Dutch Government, the monies invested by the appellant were internal to the partnership and not those of third parties. However, it did not effect its own investments but, rather, entrusted this work to a professional asset-management undertaking. It appears that it was on the invoices for professional services of this asset manager that the disputed VAT inputs of the interested party arose.

4 — The Dutch word for 'bonds' that is used by the national court in its order for reference is '*obligaties*', which is also the word used in the Dutch text of Article 13B(d)(5) of the Sixth Directive. Although the English version of Article 13B(d)(5) actually employs the word 'debentures', the use in the present case of the word 'bonds' in English would not appear to be inappropriate, since it is probably in more frequent usage in the United States and Canada for referring to the sorts of intangible assets at issue. While 'debenture' is defined as 'an acknowledgement of indebtedness' in the *Oxford English Reference Dictionary* (Second Edition, 1996), it is salutary to recall that Grove J. in *Re Florence Land Co., ex p. Moor*, 10 Ch. D. 530, described it as 'a word which has no definite signification in the present state of the English language'. 'Bond' is equally a word of broad import.

5 — See Case C-60/90 [1991] ECR I-3111 (hereinafter '*Polysar*').

van Financiën of 9 November 1982, [6] the interest received on bonds forming part of a personal portfolio of investments must, unlike that obtained through dividends received on holdings of shares, be treated as consideration for the purposes of VAT. Furthermore, the appellant contended that its activities, viewed as whole, were economic and consisted of the exploitation on a continuing basis of several assets, and that the services it provided comprised, *inter alia*, the granting of credit.

13. The national court, having regard to the relevance of Articles 4, 13B and 17 of the Sixth Directive for determining the appeal, decided, by an order registered at the Court on 17 March 1995, that the following four questions should be referred to the Court:

'1) Are the mere acquisition of ownership in and the holding of bonds — claims embodied in marketable securities —, activities which are not subservient to any other business activity, and the receipt of income therefrom to be regarded as economic activities within the meaning of Article 4(2) of the Sixth Directive?

2) If that question has to be answered in the affirmative, should those activities be regarded as transactions, within the meaning of Article 13B(d)(1) or (5) of the Sixth Directive, which, in so far as they relate to bonds issued by a body established outside the Community, confer an entitlement to deduct the input tax imposed on the possession and management of the bonds as a result of Article 17(3)(c) of the Sixth Directive?

3) If Question 2 has to be answered in the affirmative, in the event that a taxable person carrying out the activities referred to in the foregoing questions is also the holder of shares, which, according to that which the Court of Justice held in particular in its judgment of 22 June 1993 in Case C-333/91 *Satam SA*, [7] fall outside the scope of value added tax, can the input tax charged to that taxable person be deducted in full or is the input tax relating to the possession of the shares debarred from being deducted?

4) If Question 3 must be answered in the latter sense, according to what yardstick must the amount disqualified from deduction be calculated?'

6 — *Vakstudie Nieuws* 1982, p. 2281.

7 — See *Sofitam SA (formerly Satam SA)* v *Ministre Chargé du Budget* [1993] ECR I-3513 (hereinafter '*Sofitam*').

II — Observations submitted to the Court

14. Written and oral observations were submitted by the Kingdom of the Netherlands, the French Republic and the Commission.

III — Analysis

15. By its first question the national court identifies clearly the key issue in this case as being whether the mere acquisition of ownership in and the holding of bonds for the purpose of enjoying income therefrom constitutes an economic activity for the purposes of the Sixth Directive. If this question were to be answered affirmatively, it would be necessary to assess whether a right to deduct arises (Question 2) and, if so, whether that right is affected by income derived from holding shares, other than as part of an economic activity (Questions 3 and 4). In the event of the activities of the interested party during the relevant period not being regarded as economic for VAT purposes, they would fall outside the scope of the Sixth Directive and no question of a right to deduct could arise.

A — *The first question*

(i) Summary of the observations

16. The Netherlands and the Commission support the view adopted in the main proceedings by the Gerechtshof, Amsterdam. They submit that the activity of acquiring and holding bonds or debentures cannot be regarded as an economic activity within the meaning of the Sixth Directive; in their view that activity is similar to that of acquiring and holding shares, which was held, in itself, not to constitute an economic activity by the Court in *Polysar*. The receipt of interest, as opposed to dividends, does not, in their opinion, distinguish the activity in question from that of a shareholder, since the interest earned, like dividends, merely results from ownership of the relevant bonds. Besides, in contrast to income derived from the ownership of tangible property, which arises on the active exploitation of such property as occurred in *Van Tiem*, [8] the holder of bonds may passively derive income solely by virtue of its title to the bonds.

17. The Netherlands submits that the acquisition and holding of bonds should be

8 — Case C-186/89 [1990] ECR I-4363.

regarded as a form of investment having simply the character of personal wealth management. The holding of some investments in the form of securities cannot, from an economic perspective, be regarded as the provision of credit. When a financial institution lends money to a client, it clearly provides a service; no such service is provided upon the acquisition of bonds; the bondholder performs the role of a purchaser *vis-à-vis* the issuer of the bonds.

18. In so far as the Court also held in *Polysar* that, wherever the acquisition of a holding of shares 'is accompanied by direct or indirect involvement in the management of the companies in which the holding has been acquired' [9] it would constitute an economic activity, the Commission observes that, in contrast to most types of shares, a bond confers no right of control or say in the undertaking which issues it and, thus, the mere fact of holding it cannot, *a fortiori*, constitute an economic activity. Moreover, the Commission contends that the holding of bonds should be equated with being a shareholder and not with the grant of credit, since, having regard to the wording of Article 13B(d) of the Sixth Directive, the two former activities are classified together under paragraph 5 [10] whilst the latter is treated separately at paragraph 1. [11]

19. In the alternative, the Netherlands submits that if a holder of bonds satisfies the criterion of 'involvement' articulated by the Court in *Polysar* then its activities should be classified as economic for the purposes of the Sixth Directive and, as a taxable person, it would then be liable for VAT on all the receipts generated through that holding. If this were the case, the Netherlands suggests that the activity of the holding company should be classified either as the granting of credit within Article 13B(d)(1), or as a transaction in bonds coming within Article 13B(d)(5).

20. France submits by reference, in particular, to *Van Tiem*, which concerned the exploitation of immovable property (viz. the grant of building rights over part of a building plot), that the acquisition and holding of bonds and the receipt of income therefrom ought to be regarded as an economic activity for the purposes of the Community VAT regime. France argues, in effect, that a subscriber to a bond becomes the owner of intangible movable property which it exploits by receiving a regular income in return for the funds represented by the bond, which have effectively been lent to the issuer of the bond; Article 4(2) of the Sixth Directive makes no distinction between the exploitation of tangible or intangible property.

21. Although France recognizes that the Court in *Polysar* held that a related activity

9 — Paragraph 14 of the judgment.

10 — While the Dutch text of Article 13B(d)(5), cited by the Commission in its written observations, refers to '*obligaties en andere waardepapieren*', the English text mentions 'debentures and other securities'; in this respect, see footnote 4 above.

11 — Points 1 and 5 are quoted in paragraph 4 above.

— the simple acquisition and holding of shares — did not constitute an economic activity, it submits that the permanence of the income which attaches to the holding of a bond distinguishes that income from that derived from holding shares. France contends that the purchase and holding of bonds involves the provision of a service similar to the lending of money, an activity in which the appellant also appears to have engaged. [12]

(ii) Consideration of Question 1

22. In the alternative, counsel for France submitted orally that, if the Court were to interpret Article 4(2) of the Sixth Directive as excluding the mere acquisition and holding of bonds from the concept of 'economic activities', such an exclusion should not be based on the 'involvement' criterion enunciated in *Polysar*. Since bonds by their very nature do not normally give rise to any right of participation in the management of the issuer, the application of such a criterion would, he submitted, be inappropriate.

23. It must be recalled, in the first instance, that the Court has consistently held that Article 4 of the Sixth Directive confers 'a very wide scope on value added tax, comprising all stages of the production, distribution and the provision of services'. [13] It has held that even acts preparatory to the future exploitation of property may constitute an economic activity. [14] Furthermore, the Court has held that 'the term "exploitation" refers to all transactions, whatever may be their legal form, by which it is sought to obtain income ... on a continuing basis'. [15] I share the view, expressed by Advocate General VerLoren van Themaat in relation to the concept of a taxable person under Article 4 of the Second Council Directive, [16] that 'it is not the *aim* but rather the *nature* of the activities in question which is relevant' when determining what constitutes an economic activity. [17]

24. Attention should be focused on the economic and commercial substance of transactions that are alleged to constitute an economic activity, as opposed to the formal financial or commercial classification

12 — The separate treatment in Article 13B(d)(1) and (5) of transactions involving the granting of credit and those affecting bonds is, France submits, irrelevant, since the purpose of that provision is merely to enumerate exemptions from VAT.

13 — See, *inter alia*, *Van Tiem*, paragraph 17 of the judgment.

14 — See Case 268/83 *Rompelman* v *Minister van Financiën* [1985] ECR 655, where it was held that the purchase of the future title to two showroom-type premises, then still under construction, together with a usufructuary interest in the land pertaining thereto with the intention of subsequently letting them to traders could constitute an economic activity.

15 — *Van Tiem*, paragraph 18 of the judgment.

16 — Directive 67/228/EC on the harmonization of legislation of Member States concerning turnover taxes — Structure and procedures for application of the common system of value added tax; OJ, English Special Edition 1967 (I), p. 16.

17 — See Case 89/81 *Staatssecretaris van Financiën* v *Hong Kong Trade* [1982] ECR 1277, p. 1293 (emphasis in original).

(namely, in this case, as bond or share acquisitions and holdings) of those activities. It follows, in my opinion, that a person who, like the appellant, deals in bonds may only be considered to be carrying on an economic activity if he is pursuing a business or commercial purpose; in this respect he must provide services to his customers as opposed merely to being a consumer of services.

25. In this respect, it is noteworthy that in *Rompelman*, whilst the Court was satisfied that a declared intention to let future property could constitute 'a sufficient ground for assuming that the acquired property is to be used for a taxable activity', it none the less pointed out 'that it is for the person applying to deduct VAT to show that the conditions for deduction are met and in particular that he is a taxable person'. [18] The Court continued: [19]

'Therefore, Article 4 does not preclude the revenue authorities from requiring the declared intention to be supported by *objective* evidence such as proof that the premises which it is proposed to construct are specifically suited to *commercial* exploitation.'

26. In *Polysar* the Court was concerned with a claim by a pure holding company that dividend income received from its holdings of shares should be regarded for VAT purposes as obtained in the pursuit of an economic activity. Recalling its dictum in *Van Tiem* as to the wide scope of VAT, the Court stated that 'it does not follow from that judgment ... that the mere acquisition and holding of shares in a company is to be regarded as an economic activity, within the meaning of the Sixth Directive, conferring on the holder the status of a taxable person'. [20] The Court explained this interpretation of the scope of the principle expressed in *Van Tiem* in the following terms: [21]

'The *mere acquisition* of financial holdings in other undertakings does not amount to the exploitation of property for the purpose of obtaining income therefrom on a continuing basis because any dividend yielded by that holding is *merely* the result of *ownership* of the property.'

The Court, however, did not exclude the possibility that the holding of shares may constitute an economic activity, '... where the holding is accompanied by direct or indirect involvement in the management of the companies in which the holding has been

18 — Paragraph 24 of the judgment.
19 — Ibid. (emphasis added).
20 — *Polysar*, paragraph 13 of the judgment.
21 — Ibid. (emphasis added).

acquired, without prejudice to the rights held by the holding company as shareholder.' [22]

27. The Court was clearly influenced by the view of Advocate General Van Gerven, who had advised that both *Rompelman* and *Van Tiem* 'were concerned not only with an investment, that is to say the acquisition of property ... but also with the property acquired subsequently being made available to a third party for consideration'. [23] He then drew a distinction between the acquisition of property, on the one hand, and its being made available, on the other, for the purposes of determining whether such property has been exploited: [24]

'The mere acquisition of a holding in a company does not entail making it available in that way. The dividends which may subsequently be payable to the shareholder are, in my view, not to be regarded as 'income ... on a continuing basis' from the 'exploitation' of property; they are merely benefits which the owner may receive from property and which are yielded by the mere holding thereof.'

He felt that any other conclusion would lead to 'any holder of shares or securities' being regarded as a taxable person, and that the position should only be different where the activities involved: [25]

'... go beyond the activities of *a normal investor in connection with the usual management of his assets*, for instance where a company regularly buys and sells shares as profit-making transactions. In such a case, repeated transactions which involve buying and selling may be regarded as economic activities'.

28. In its observations, France submits that any distinction that exists between the acquisition and exploitation of shares should not be applied to bonds. At the hearing, counsel for France stated that Article 4(2) of the Sixth Directive neither distinguishes between the exploitation of tangible or intangible property nor requires the exploitation of property as a precondition for the characterization of its ownership as an economic activity. He pointed out that mere possession of capital does not yield income of its own accord; it will only do so when decisions are made and effected regarding how it may most advantageously be used.

22 — *Polysar*, paragraph 14 of the judgment.

23 — *Polysar*, cited in footnote 5 above, [1991] ECR I-3111, p. I-3125.

24 — Ibid.

25 — Loc. cit., footnote 23 above (emphasis added).

29. The very nature of the many types of intangible property and the variety of ways in which it can be exploited make it difficult to draw direct comparisons with the physical consequences attendant upon the exploitation of tangible property. The physical nature of the effects of the purchase of a plot of land and the grant of a right *in rem* over that land to a third party, such as in *Van Tiem*, is indisputable, whereas the effects of the activities of a person who, for example, simply buys and holds bonds, may only, in effect, be reflected in the figures appearing in the respective bank accounts of the purchaser and issuer of the bonds. However, I do not think such a difference should, *per se*, preclude the activities of a person who deals in bonds, like those of a dealer in shares, from constituting economic activities for the purposes of the Sixth Directive.

30. I do not think that the Court in *Polysar* interpreted the concept of the exploitation of intangible property more narrowly than it had previously interpreted the corresponding concept of the exploitation of tangible property in *Rompelman* and *Van Tiem*. In my opinion, it merely ruled that the acquisition of shares, which by its very nature carries with it the opportunity of earning dividends, could not be regarded, in itself, as an *economic* exploitation for the purposes of Article 4(2) of the Sixth Directive; in other words, while the receipt of a dividend cheque may differ little in financial terms from the receipt of a rent cheque from a tenant, the economic nature of the underlying activities which produce such receipts is different.

31. This interpretation is confirmed, in my view, by the subsequent judgment of the Court in *Sofitam*. The Court confirmed that a company shareholder which merely holds shares in other undertakings cannot be regarded as a taxable person for VAT purposes because 'the simple acquisition of financial holdings in other undertakings does not constitute an *economic* activity in the sense of the Sixth Directive'. [26] The Court, in my opinion, did not state that the acquisition of shares was intrinsically not an economic activity in the sense of having no connection either generally with the economy or, more specifically, with the pursuit of trade. I think, instead, that the Court meant that the mere act of acquisition and ownership of shares was insufficiently connected with the pursuit of a trade to constitute an economic activity under the Sixth Directive.

32. France seeks to distinguish the activities of acquiring and holding shares from those of acquiring and holding bonds. In my opinion, such a distinction would be neither logical, just nor convenient. The VAT classification of the activities of a private investor, or of those of a person whose activities are

26 — *Sofitam*, paragraph 12 of the judgment (emphasis added).

analogous to such an investor, should not depend merely on the form of investment. The scope of the Community VAT system should not depend on the precise form of investment. There is a fine line between certain holdings of shares and bonds on modern financial markets. Shares may be simple ordinary shares participating in the profits of the enterprise. There are also many forms of participation in the profits of quoted companies. They include, for example, preference shares with a fixed interest rate, which are in practice difficult to distinguish from loan stock. Debentures and many forms of convertible shares or stock may be held. It would be both difficult and unreal to seek to distinguish activities which are essentially those of a private investor according to whether his holdings are composed of pure loan stock or ordinary shares.

33. The Commission referred at the hearing to the recent judgment of the Court in *Wellcome Trust*. [27] In that case the Court was asked essentially 'to ascertain whether the concept of economic activities, within the meaning of Article 4(2) of the Directive, is to be interpreted as including an activity, such as ... the purchase and sale of shares and other securities by a trustee in the course of the management of the assets of a charitable trust'. [28] Wellcome Trust, the appellant taxpayer in the main proceedings, argued that, by its investment activities and in particular the sale of 288 million of its shares in the Wellcome Foundation, which, as Advocate General Lenz pointed out, 'was the largest non-government sale carried out in the United Kingdom', [29] it should be regarded as engaged in an economic activity. The Trust accepted that investments made by 'ordinary investors do not come within the scope of VAT', but claimed that the situation was different where 'an investor regularly makes investments for the purpose of generating revenue or increasing its capital', and that it was 'irrelevant whether the purpose or object of an economic activity is trading or investment'. [30] This argument was not accepted by the Court.

34. Although the Court stated that 'the Trust does not have the status of a professional dealer in securities in the United Kingdom', it continued by ruling that 'that fact does not necessarily mean that an activity, such as that at issue in the main proceedings, consisting in the acquisition and sale of shares and other securities cannot, in some cases, be treated as an economic activity within the meaning of Article 4 of the Directive'. [31] It pointed out that the case-law [32] established 'that mere exercise of the right

27 — Case C-155/94 [1996] ECR I-3013..

28 — Paragraph 21 of the judgment.

29 — See paragraph 4 of the Opinion.

30 — See paragraphs 23 and 25 of the judgment.

31 — Paragraph 31 of the judgment.

32 — Reference was made to the *Polysar* and *Sofitam* cases.

of ownership by its holder cannot, in itself, be regarded as constituting an economic activity'. [33] The Court drew no distinction between the acquisition and sale of holdings of shares; the exercise of such activities could not in themselves be regarded as economic for the purposes of the Sixth Directive. [34] Referring to *Polysar*, the Court then qualified this principle in the following terms: [35]

'It is true that, by virtue of Article 13B(d)(5) of the Directive, transactions in shares, interests in companies or associations, *debentures* and other securities may fall within the scope of VAT. This will be the case, in particular, where such transactions are effected as part of a *commercial share-dealing activity* or in order to secure a direct or indirect involvement in the management of the companies in which the holding has been acquired.'

35. The Court held that it was clear that the Trust was 'forbidden precisely to engage in such activities', since it was obliged 'to avoid engaging in trade' when carrying out its activities. [36] Counsel for France asserted at the hearing that the approach adopted by the Court in *Wellcome Trust* was really 'an ad hoc solution' tied to the particular circumstances of the case. I cannot accept this interpretation. Advocate General Lenz, while accepting that the Trust 'endeavours to secure the highest possible dividends in order to maximize the money available for its essential task of furthering medical research', [37] clearly explained the distinction to be drawn when he stated: [38]

'This, however, is not analogous to the activity of a dealer in shares. A dealer in shares is not primarily concerned with managing assets; rather, he endeavours to make profits through buying and selling shares and engaging in risky investments and speculation. He does not acquire shares with the principal aim of securing the highest possible dividends, but rather in order to resell them at as high a price as he can secure.'

The Court shared his view that the portfolio-management activities of the Trust were similar to those of a private individual managing his assets, and that such a person cannot be regarded as exercising an economic activity within the meaning of the Sixth Directive. [39]

33 — Paragraph 32 of the judgment.

34 — See paragraph 33 of the judgment.

35 — *Wellcome Trust*, paragraph 35 of the judgment (emphasis added).

36 — Ibid.

37 — *Wellcome Trust*, paragraph 19 of the Opinion.

38 — Ibid.

39 — See paragraph 36 of the judgment and paragraph 19 of the Opinion.

36. The decision of the Court in *Wellcome Trust* did not follow from the exclusively charitable nature of the Trust's activities. The principles established by the Court are of broader import. Indeed, it could be argued that the specific reference to 'debentures and other securities' by the Court puts the matter beyond doubt. [40] However, the Court, in enumerating, *inter alia*, the types of circumstances in which transactions in debentures and other securities may in principle be subject to VAT, was careful to use the words '*in particular*'. [41] I do not therefore share the concern underlying France's alternative submission, in this case, to the effect that, in any event, the application of the 'involvement' criterion to bonds would be inappropriate. If an undertaking such as the interested party, which engages in acquiring and holding bonds, does not confine its activities to pure investment activities, such as may be carried out by any private investor, but instead effects those activities as part of a commercial bond-dealing operation, or otherwise by way of trade, then that undertaking would clearly be economically exploiting the intangible property rights that it enjoys in its holdings of such bonds. This interpretation would set at rest some of the doubts which troubled counsel for France at the hearing regarding possible fiscal distortions from the different treatment of straightforward lending and the purchase of bonds. A bank, in lending, is clearly engaged in an economic activity; i. e. the placement for consideration of funds at the disposal of the borrower. Equally, so is a commercial dealer in any bonds or securities.

37. However, on the basis of the facts as stated in the order for reference and the information provided by the Netherlands at the hearing, it does not appear that the appellant engages, save perhaps on a purely occasional basis, in any activities other than those of overseeing the investment, by the professional asset manager whose services it engages, of the private capital brought by the partners to their limited partnership. Such activities can only, in my opinion, be assimilated with the management (to employ the words of the Court in *Wellcome Trust*) of 'an investment portfolio in the same way as a private investor'. [42]

38. Furthermore, counsel for France contended orally that the reasoning adopted recently by the Court in *Régie Dauphinoise* v *Ministre du Budget* is applicable to the acquisition and holding of bonds. [43] It is important to recall precisely the factual situation at issue in *Régie Dauphinoise*. Régie Dauphinoise (hereinafter 'Régie') was involved principally in the management of property, whereby it managed let property on behalf of the owners and acted as a manager of condominiums. In the course of carrying out this business it received advances

40 — See paragraph 35 of the judgment quoted in paragraph 34 above.

41 — *Wellcome Trust*, paragraph 35 of the judgment (emphasis added).

42 — Paragraph 36 of the judgment.

43 — Case C-306/94 [1996] ECR I-3695 (hereinafter '*Régie Dauphinoise*').

from the persons whose properties it managed. These advances were paid into a bank account operated by Régie, which then invested them with financial institutions on its own account. Régie did, however, become the owner of the sums invested, albeit subject to a contractual obligation ultimately to repay the relevant principal amounts. France asserts that in *Régie Dauphinoise* the Court held that, as distinct from the receipt of dividends, interest received on financial investments cannot be excluded from the scope of VAT; since it results not merely from proprietorship of the placements, but instead constitutes consideration for placing capital at the disposal of third parties, which, in that case, were the financial institutions through which Régie made its investments.

39. The Court accepted that the placements by Régie could 'be regarded as services supplied to those institutions, consisting in the loan of money for a fixed period, duly remunerated by the payment of interest' [44] and, moreover, that 'unlike the receipt of dividends by a holding company ... interest received by a property management company on placements made for its own account of sums paid by co-owners and lessees cannot be excluded from the scope of VAT, since the interest does not arise simply from the ownership of the asset, but is the consideration for placing capital at the disposition of a third party'. [45] The Court was nevertheless careful to distinguish the activities of an undertaking like Régie from simple 'placements made with banks by the manager of a condominium' who was not 'acting as a taxable person'. [46] Accordingly, it concluded that: [47]

'... in the case at issue in the main proceedings, the receipt, by such a manager, of interest resulting from the placement of monies received from clients in the course of managing their properties constitutes the direct, permanent and necessary *extension* of the taxable activity, so that the manager is acting *as a taxable person* in making such an investment'.

40. In my opinion, it is clear that the Court was satisfied that the investment activities of Régie effectively constituted part of a broader business activity or, as Advocate General Lenz aptly put it, that it was satisfied that '[Régie] invests money which it holds on the basis of its economic activity'. [48] The distinction from *Wellcome Trust* was clear: in that case 'there was no visible economic activity on the basis of which the trust company could have received the money'. [49] In this case, and subject, of course, to the reservation that it is ultimately for the national court to make all relevant findings of fact, there is no evidence before the Court to suggest that the bond activities of the appellant constitute 'the direct, permanent

44 — Paragraph 16 of the judgment.

45 — Paragraph 17 of the judgment.

46 — Paragraph 18 of the judgment.

47 — Paragraph 18 of the judgment (emphasis added).

48 — Paragraph 20 of the Opinion.

49 — See the Opinion of Advocate General Lenz, loc. cit., ibid.

and necessary extension' of any other 'taxable activity'. Therefore, I am satisfied that the transactions effected by the interested party should be equated with those of a private person managing his own assets. Since there is no economic activity for the purposes of the Sixth Directive, the relevant transactions therefore fall outside the scope of the Community VAT system and, consequently, no question of a right to deduct arises. If the Court accepts this recommendation, there would be no need to consider the remaining questions.

B — *The second question*

41. In the event of the Court deciding that the acquisition and holding of bonds in circumstances such as those involved in the main proceedings are, contrary to the view I have expressed, sufficient to constitute the exercise of an economic activity for the purpose of Article 4(2) of the Sixth Directive, it would, however, be necessary to consider whether a right to deduct arises. [50]

42. The right of a taxable person to deduct the VAT paid on the goods and services which he has consumed for the purposes of his business is predicated, under Article 17, on the existence of a concomitant liability to pay VAT on the goods and/or services provided in the course of that business. Since the acquisition and holding of bonds may, if it falls within the scope of the VAT system, either be regarded under Article 13B(d), paragraph 1 as 'the granting and negotiation of credit', or, possibly, under paragraph 5 as analogous to 'transactions ... in ... debentures and other securities', it will constitute an activity that is exempted from VAT and no right to deduct will consequently ensue. However, Article 17(3)(c) provides for a derogation from this principle in the case of a limited number of exempted transactions, including those enumerated in Article 13B(d), paragraphs 1 to 5, 'where the customer is established outside the Community'.

43. It is clear from the order for reference that the bonds at issue in this case are issued by public bodies and companies established outside the Community. Thus, if the requirement set out in the first sentence of Article 17(3)(c) is satisfied, whereby the disputed VAT inputs must relate 'to goods and services' that 'are used for the purposes of' the relevant taxable but exempt transactions, the appellant should be entitled to exercise

50 — It would seem, from the description of the findings of the Gerechtshof, Amsterdam and from the questions contained in the order for reference (see paragraphs 11 and 13 above), that, as far as the national court is concerned, no question arises in this case as to whether the appellant could be regarded, under Articles 2 and 4(1), as having acted both as a taxable person and independently in carrying out its activities.

the right to deduct. [51] In consequence, I would therefore recommend that the Court give an affirmative answer to the second question, in the event that it needs to be answered.

C — *The third and fourth questions*

44. As these questions are closely related, they may conveniently be answered together. Having regard to the designation of the activities of the appellant set out in the order for reference, it is not altogether clear whether it also holds shares or, furthermore, derives dividend income therefrom. [52] In the circumstances, there may be a doubt as to whether the Court can provide a useful answer to that question. [53] In my opinion, the duty of cooperation which governs the relationship between national courts and the Court in Article 177 proceedings obliges the Court to refuse to answer questions referred only in circumstances where it is very clear that no genuinely useful answer can be given. [54] That is plainly not the case with the third and fourth questions referred in this case by the national court.

45. The nature of bonds is such that some of those held by the appellant might conceivably have taken the form of convertible loan stock and subsequently have been converted into shares during the relevant period. Alternatively, the national court may have in mind some information made available to the Gerechtshof, Amsterdam regarding entirely separate holdings of shares held by the appellant. Indeed, it does not seem unlikely that a limited partnership that held US $130 000 000 worth of bonds during the relevant period might also have owned some shares. It is noteworthy that the appellant, in its appeal to the national court, described its activities as comprising the exploitation on a continuing basis of *several* assets, some of which might, at the relevant time, have consisted of shares. This is, of course, all speculative, but I do not think that it should be

51 — If the information provided by the Netherlands at the hearing is correct, namely that the alleged VAT inputs originated in payments made by the appellant to the undertaking which managed its financial activities, then it would appear that the required link between those inputs and the VAT-exempt transactions between the appellant and its third-country customers would be present in this case. However, it is for the national court ultimately to make any outstanding findings of fact that may prove necessary in this respect. See further the discussion, arising out of the third and fourth questions referred by the national court, at paragraphs 48 to 54 below.

52 — The national court simply asks in its question whether, 'in the event' (*'dan ingeval'*) of a taxable person carrying out the activities ascribed to the interested party also being a shareholder, the input tax paid can still be deducted in full.

53 — The Court has, for example, consequent upon its judgment in Joined Cases C-320/90, C-321/90 and C-322/90 *Telemarsicabruzzo* v *Circostel and Others* [1993] ECR I-393, where it ruled that 'the need to provide an interpretation of Community law which will be of use to the national court makes it necessary that the national court define the factual and legislative context of the questions it is asking or, at the very least, explain the factual circumstances on which those questions are based' (paragraph 6 of the judgment), adopted a number of orders in which it has declined to answer questions referred where those conditions are not met; see, *inter alia*, Case C-101/96 *Italia Testa* [1996] ECR I-3081.

54 — See, in this respect, paragraph 29 of my Opinion in Case C-105/94 *Angelo Celestini* v *Saar-Sektkellerei Faber* [1997] ECR I-2971, I-2974.

assumed that the national court would have referred the question unless it felt that some issue arose before it concerning the apportionment of the appellant's VAT inputs between VAT-exempt and VAT-liable transactions. I would therefore propose that, in the event of the Court answering affirmatively the first two questions, it should also answer the third and fourth questions.

46. The national court refers in its third question to the judgment in *Sofitam*. It may, in my opinion, be assumed, from the description of the activities of the interested party provided in the order for reference, that the national court has formed the view that, if the appellant does engage in shareholding activities, those activities are not such as to involve it in the management of the companies in which the shares are held, or, at least, such as may otherwise be regarded as economic. They must therefore be regarded as falling outside the scope of the Community VAT system. In such circumstances the Court held in *Sofitam* that: [55]

'Since the receipt of dividends is not the consideration for any economic activity within the meaning of the Sixth Directive, it does not fall within the scope of VAT. Consequently, dividends resulting from holdings fall outside the deduction entitlement.'

As such dividend income falls outside the scope of the Community VAT system, the Court continued in *Sofitam* by stating that:

'... [they] must be excluded from the calculation of the deductible proportion referred to in Articles 17 and 19 of the Sixth Directive, if the objective of wholly neutral taxation ensured by the common system of VAT is not to be jeopardized'. [56]

It is therefore clear that whatever income the appellant derives from its holdings of shares, such income cannot affect the deductible proportion of its VAT inputs.

47. It is still necessary to determine the extent of the right to deduct in circumstances such as those raised by the national court in its third and fourth questions.

48. Article 17(2) of the Sixth Directive provides unambiguously that a taxable person shall only be entitled to deduct VAT inputs from the tax which he is liable to pay 'in so

55 — Paragraph 13 of the judgment.

56 — Paragraph 14 of the judgment.

far as the goods and services are used for the purposes of his taxable transactions'. Article 17(3) is equally unequivocal: the right to deduct that is exceptionally permitted in respect of the transactions listed in paragraphs (a) to (c) only arises 'in so far as the goods and services', on which the claimed right to deduct is based, 'are used for the purposes of' those transactions. This interpretation of Article 17 is confirmed by the approach of Advocate General Van Gerven in *Polysar*. Referring to Article 17(2), he stated: [57]

'... a *taxable person* is entitled to deduct the value added tax he has paid in respect of goods and services supplied *if and in so far as* those goods and services are subsequently for the purposes of taxable transactions .... The same holds true in the case of (in principle taxable) activities which the Directive exempts from value added tax'.

49. The Netherlands, supported on this point by France in its oral observations, submits that the approach adopted by the Court in *BLP Group* provides a useful comparison for this case. [58] In that case the Court had to consider whether a taxable person, who pays VAT on services received for the purpose of effecting a transaction that is exempt from VAT (i.e. the sale of shares in a company), may, nevertheless, deduct those VAT inputs from the VAT payable on its taxable transactions (namely the provision of management services to subsidiary companies), in circumstances where the exempt transaction was effected in order to reduce indebtedness to its bankers arising from its taxable transactions. Referring to Article 17(3)(c), the Court stated that 'it is only by way of exception that the Directive provides for the right to deduct VAT on goods or services used for exempt transactions'. [59] If it were otherwise, the Court continued, national tax authorities: [60]

'... when confronted with supplies which, as in the present case, are not *objectively linked* to taxable transactions, would have to carry out inquiries to determine the intention of the taxable person. Such an obligation would be contrary to the VAT system's objective of ensuring legal certainty and facilitating application of the tax by having regard, save in exceptional cases, to the objective nature of the transaction in question'.

50. It follows, in my opinion, that in so far as some of the disputed inputs in this case relate entirely to the share-holding activities

57 — *Polysar*, [1991] ECR I-3111, p. I-3128 (emphasis in original). See also the Explanatory Memorandum issued by the Commission in respect of its revised proposal for the directive where it stated that 'the principle has been maintained that value added tax on goods and services used for the purposes of non-taxable or exempt transactions (except for transactions effected abroad or exports) should not be taxable'; Bulletin of the EC, Supp. 11-73, p. 18.

58 — Case C-4/94 [1995] ECR I-983.

59 — Paragraph 23 of the judgment.

60 — Paragraph 24 of the judgment (emphasis added).

of the appellant, they must be excluded from the calculation of its deductible amount.

51. In this case, however, a further question arises: to the extent that the disputed VAT inputs may actually concern services which are provided to the taxable person in relation *both* to its non-taxable and taxable but exempt transactions, by what yardstick must the inputs which are to be disqualified from the deduction allowed be calculated? The Netherlands and France submit essentially, by analogy with Article 19 of the Sixth Directive, that a pro rata method of calculating the deductible proportion should be applied.

52. I do not think that this question can be answered directly by reference to Articles 17(5) and 19, though, as will appear, I think that they must be applied by analogy. The factual circumstances at issue in the main proceedings were not envisaged by the draftsmen of Article 17(5), which assumes that a taxable person will have VAT inputs related to goods and services used for the purposes of both taxable and exempt transactions. In this case, however, the national court's questions address a factual situation where the taxable person has incurred inputs which relate both to exempt and non-taxable transactions.

53. In my opinion, it follows clearly from the interpretation of Article 17 of the Sixth Directive outlined in paragraphs 48 and 49 above that a taxable person, such as the appellant, who incurs VAT inputs paying for professional services rendered in respect both of the economic activity (if so classified by the Court) of acquiring and holding bonds and the non-economic activity (for VAT purposes) of merely holding shares, can, where the bonds are issued by customers established outside the Community, only deduct that proportion of those inputs which may properly be assigned to the economic activity. Although Article 18 does not prescribe any particular formalities for the exercise of the right to deduct permitted by Article 17(3), every taxable person is obliged by Article 22(2) of the Sixth Directive to 'keep accounts in sufficient detail to permit application of the value added tax and inspection by the tax authority'. Moreover, Article 22(4) requires 'every taxable person' to 'submit a return within an interval to be determined by each Member State', which 'may not exceed two months following the end of each tax period', the duration of which is to be determined by each Member State, although it may not 'exceed a year'.

54. It follows, in my opinion, that the taxable person who seeks to rely on Article 17(3)(c) in circumstances where some of its VAT inputs related to non-taxable activities is obliged to establish, to the satisfaction of the relevant tax authorities, the proportion of those inputs which it claims are attributable to taxable, but exempt transactions, figuring in Article 13B(a) and (d), paragraphs 1 to 5. [61]

61 — See, in respect of the evidential obligations of taxable persons claiming the right to deduct, paragraph 24 of the judgment in *Rompelman*, which is quoted in paragraph 25 above.

IV — Conclusion

55. Accordingly, I am of the opinion that the first question referred by the Hoge Raad der Nederlanden should be answered as follows:

(1) The mere acquisition of ownership in and the holding of bonds, and the receipt of income therefrom, cannot, where they are not the direct, permanent and necessary extension of another business or commercial activity, be regarded as economic activities within the meaning of Article 4(2) of the Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of assessment.

If, however, the Court considers that the activities specified in respect of my proposed answer to the first question should be regarded as economic activities for the purposes of Article 4(2) of the Sixth Council Directive, I recommend that the second, third and fourth questions referred by the national court be answered as follows:

(2) Article 17(3)(c) of the Sixth Council Directive confers a right on a taxable person to deduct VAT inputs incurred on services provided to him in so far as they are used by that person for the purposes of acquiring ownership in and holding bonds, and obtaining income therefrom, so long as those bonds are issued by public bodies or companies who are established outside the Community.

(3) A taxable person carrying on the activities described in the preceding answers who also engages in the activity of acquiring holdings of shares which falls outside the scope of VAT and whose VAT inputs relate both to his bond and share-holding activities, is only entitled to exercise the right to deduct conferred by Article 17(3)(c) of the Sixth Council Directive in respect of the proportion of the inputs which relate to the first-mentioned bond activities, in so far as he is capable of demonstrating the relationship to the satisfaction of the appropriate tax authorities.