JUDGMENT OF THE COURT (Fifth Chamber)

20 June 2002 *

In Case C-287/00,

Commission of the European Communities, represented by G. Wilms and K. Gross, acting as Agents, with an address for service in Luxembourg,

applicant,

v

Federal Republic of Germany, represented by W.-D. Plessing and T. Jürgensen, acting as Agents,

defendant,

APPLICATION for a declaration that, by exempting from value added tax the research activities of public-sector higher-education establishments pursuant to Paragraph 4(21a) of the Umsatzsteuergesetz (Law on Turnover Taxes) of 27 April

* Language of the case: German.

1993 (BGBl. 1993 I, p. 565), as amended by Paragraph 4(5) of the Umsatzsteuergesetz-Änderungsgesetz of 12 December 1996 (BGBl. 1996 I, p. 1851), the Federal Republic of Germany has failed to fulfil its obligations under Article 2 of the 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),

THE COURT (Fifth Chamber),

composed of: P. Jann, President of the Chamber, S. von Bahr (Rapporteur), D.A.O. Edward, A. La Pergola and C.W.A. Timmermans, Judges,

Advocate General: F.G. Jacobs,
Registrar: R. Grass,

having regard to the report of the Judge-Rapporteur,

after hearing the Opinion of the Advocate General at the sitting on 13 December 2001,

gives the following

Judgment

1 By application lodged at the Court Registry on 20 July 2000, the Commission of the European Communities brought an action pursuant to Article 226 EC for a declaration that, by exempting from value added tax ('VAT') the research activities of public-sector higher-education establishments ('State universities') pursuant to Paragraph 4(21a) of the Umsatzsteuergesetz (Law on Turnover Taxes) of 27 April 1993 (BGBl. 1993 I, p. 565), as amended by Paragraph 4(5) of the Umsatzsteuergesetz-Änderungsgesetz of 12 December 1996 (BGBl. 1996 I, p. 1851; 'the UStG'), the Federal Republic of Germany has failed to fulfil its obligations under Article 2 of the 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, the 'Sixth Directive').

Legal framework

Community legislation

2 Article 2(1) of the Sixth Directive makes subject to VAT the supply of goods or services effected for consideration within the territory of the country by a taxable person acting as such.

3 Under Article 4(1) of that directive 'taxable person' is to mean any person who independently carries out any economic activity specified in Article 4(2). The notion of 'economic activities' is defined in Article 4(2) as encompassing all activities of producers, traders and persons supplying services, and also the exploitation of tangible or intangible property for the purpose of obtaining income therefrom on a continuing basis.

4 The first subparagraph of Article 4(5) of the Sixth Directive provides that States, regional and local government authorities and other bodies governed by public law are not to be considered taxable persons in respect of the activities or transactions in which they engage as public authorities, even where they collect dues, fees, contributions or payments in connection with these activities or transactions.

5 Article 13(A)(1) of that directive, which lays down exemptions for certain activities in the public interest, provides:

'Without prejudice to other Community provisions, Member States shall exempt the following under conditions which they shall lay down for the purpose of ensuring the correct and straightforward application of such exemptions and of preventing any possible evasion, avoidance or abuse:

...

(i) children's or young people's education, school or university education, vocational training or retraining, including the supply of services and of

goods closely related thereto, provided by bodies governed by public law having such as their aim or by other organisations defined by the Member State concerned as having similar objects'.

National legislation

6 Paragraph 4(21a) of the UStG exempts from VAT 'transactions effected by public-sector higher-education establishments in connection with research activities. Research activities shall not include activities confined to the application of established knowledge, the administration of research projects or activities not related to research'.

Pre-litigation procedure

7 Considering that the VAT exemption under Paragraph 4(21a) of the UStG was contrary to Community law, on 6 November 1998 the Commission sent a letter of formal notice to the Federal Republic of Germany.

8 In that letter, after having recalled the content of Paragraph 4(21a) of the UStG, the Commission stated that a State university is a taxable person for VAT purposes in so far as it is not acting as a public authority, but is effecting transactions for consideration and that the research activities carried out by a taxable person are, in the light of the Sixth Directive, taxable, non-exempt

transactions. It also recalled the wording of Article 2(1) of the Sixth Directive and stated that, given that research activities are not exempt, in particular under Article 13 of the Sixth Directive, it considered that, by exempting from VAT the activities of State universities, the Federal Republic had failed to fulfil its obligations under Article 2(1) of the Sixth Directive.

9 Since the German Government did not reply to the letter of formal notice, although it requested, and was granted, an extension until mid-March 1999 of the period within which to reply, the Commission issued a reasoned opinion by letter of 26 August 1999, calling on the Federal Republic of Germany to take the measures necessary to comply with it within two months of its notification.

10 In the reasoned opinion, after having pointed out that, under Paragraph 4(21a) of the UStG, the research activities of State universities are exempt from VAT and cited Article 2(1) of the Sixth Directive, the Commission repeated in point 3 of that opinion that a State university is a taxable person for VAT purposes in so far as it is not acting as a public authority, but is effecting transactions for consideration and that the research activities carried out by a taxable person are, in the light of the Sixth Directive, taxable, non-exempt transactions. According to the Commission, by exempting from VAT those activities of State universities, the Federal Republic of Germany had failed to fulfil its obligations under Article 2(1) of the Sixth Directive. Finally, the Commission recalled that, in accordance with Article 226 EC, it had informed the German Government of that breach of Community law by its letter of formal notice of 6 November 1998.

11 By letter of 4 April 2000, the German Government replied to the reasoned opinion, but that reply did not satisfy the Commission which brought the present proceedings.

Admissibility

Arguments of the parties

12 The German Government argues that the Commission's action is inadmissible for two reasons.

13 First, the Commission did not observe the pre-litigation procedure, as required by Article 226 EC. Contrary to the requirements derived from the Court's case-law (see, in particular, Case C-96/95 *Commission* v *Germany* [1997] ECR I-1653, paragraphs 22 and 24, and Case C-328/96 *Commission* v *Austria* [1999] ECR I-7479, paragraph 34), the reasoned opinion, of only seven sentences, did not contain either a complete exposition of the facts or a detailed and cogent legal analysis of the subject-matter of the dispute, but essentially simply repeated the contents of the letter of formal notice.

14 Second, the German Government submits that in the originating application the subject-matter of the proceedings is broader than is clear from the reasoned opinion, which is contrary to the principle of continuity between the pre-litigation stage and the action, which is a specific expression of the right to be heard (see Case C-274/93 *Commission* v *Luxembourg* [1996] ECR I-2019, paragraph 11).

15 In that regard, the German Government contends that, in the originating application, the Commission no longer bases its action solely on an infringement

of Article 2 of the Sixth Directive, as in the reasoned opinion, but also invokes Article 13(A) of the Sixth Directive. The Commission's argument, in so far as it is based on that provision, is an essential aspect of its action and is therefore a new complaint. Article 2 of the Sixth Directive defines only the basis of assessment for VAT, that is, the categories of turnover which must in principle be incorporated into the system of VAT, but it does not follow directly from that provision that the types of turnover there described are taxable. That liability to tax follows solely from the specific criteria for exemption from tax laid down in Article 13 et seq. of the Sixth Directive.

Findings of the Court

16 According to settled case-law, the purpose of the pre-litigation procedure is to give the Member State concerned an opportunity, on the one hand, to comply with its obligations under Community law and, on the other, to avail itself of its right to defend itself against the complaints made by the Commission (see, in particular, *Commission* v *Germany*, cited above, paragraph 22, and Case C-439/99 *Commission* v *Italy* [2002] ECR I-305, paragraph 10).

17 The proper conduct of that procedure constitutes an essential guarantee required by the Treaty not only in order to protect the rights of the Member State concerned, but also so as to ensure that any contentious procedure will have a clearly defined dispute as its subject-matter (see Case C-1/00 *Commission* v *France* [2001] ECR I-9989, paragraph 53).

18 It follows, first, that the subject-matter of the proceedings under Article 226 EC is delimited by the pre-litigation procedure governed by that provision. Accordingly, the application must be based on the same grounds and pleas as the reasoned opinion (see, in particular, *Commission* v *Italy*, cited above, paragraph 11).

19 Second, the reasoned opinion must contain a cogent and detailed exposition of the reasons which led the Commission to the conclusion that the Member State concerned had failed to fulfil one of its obligations under the Treaty (see, in particular, *Commission* v *Italy*, paragraph 12).

20 In the present case, it must be pointed out first that, throughout the procedure which began with the sending of the letter of formal notice, the infringement with which the Federal Republic of Germany is charged has remained the same, namely the exemption from VAT of the research activities of State universities under Paragraph 4(21a) of the UStG. In that regard, it is clearly indicated in that letter that the Commission considers that those activities are taxable transactions under Article 2(1) of the Sixth Directive and that they are not exempt.

21 Second, the Commission did not alter the subject-matter of the dispute by changing the grounds of the declared infringement. Admittedly, it is only in its application that the Commission sets out explicitly its arguments to show that Article 13(A)(1)(i) of the Sixth Directive is not applicable in this case. The fact remains, however, that in its letter of formal notice the Commission had already stated that, in its submission, the research activities of those establishments are not exempt, 'in particular under Article 13 of the Directive'. In that respect, it is important to note that the reasoned opinion makes express reference to the letter of formal notice.

22 It must therefore be considered that, in the reasoned opinion, the Commission defined in sufficiently precise terms the alleged infringement and the reasons for which it considers that the Federal Republic of Germany has failed to fulfil its obligations under the Sixth Directive.

23 Moreover, it is common ground that there was no reply to the letter of formal notice, although the Commission granted the German Government an extension of the period within which to reply. If the Government had replied to that letter, the Commission would have been in a position to set out in detail in the reasoned opinion the complaints which it had already raised in more general terms in the letter of formal notice. In a situation such as that arising from the silence of the German Government, the Commission cannot be criticised for having essentially repeated in almost identical terms in the reasoned opinion the contents of the letter of formal notice.

24 Furthermore, although the Commission relied specifically on Article 13(A)(1)(i) of the Sixth Directive for the first time in the application, it was merely replying to a ground of defence raised also for the first time by the German Government in response to the reasoned opinion and, in so doing, it amended neither the definition nor the basis of the alleged infringement (see, to that effect, Case 211/81 *Commission* v *Denmark* [1982] ECR 4547, paragraph 16).

25 Therefore, the reasoned opinion defines the alleged infringement in a sufficiently precise manner and the arguments put forward by the Commission in its application, according to which Article 13(A)(1)(i) of the Sixth Directive is not applicable to the present proceedings, cannot be deemed to alter the subject-matter of the alleged infringement.

26 It follows that the application is admissible.

Substance

Arguments of the parties

27 The Commission argues that the activity in question in the present case is based on a private contract relating to a research project between the relevant State university and a contracting body, which determines, *inter alia*, the type and scope of the services as well as the consideration for them. When they carry out that activity, State universities thus apply the same rules as a private company. Consequently, the exception laid down in the first subparagraph of Article 4(5) of the Sixth Directive, relating to the activities or transactions engaged in by bodies governed by public law acting as public authorities, is not applicable, so that those establishments are in principle regarded as taxable persons within the meaning of that directive in relation to research contracts.

28 Since they are carried out for consideration on the basis of commissioning contracts, those research activities of State universities are supplies of services subject to VAT, in accordance with Article 2 of the Sixth Directive. That provision defines taxable matters by specifying the activities which, in principle, are subject to VAT. Where the transactions of bodies governed by public law do not fall within the exercise of public authority, the obligation of Member States to make such transactions subject to VAT thus arises directly from Article 2 of the Sixth Directive.

29 Moreover, an exemption for State universities' research contracts cannot be granted under Article 13(A) of the Sixth Directive.

30 As the Court has consistently held, it is clear from the scheme of the Sixth Directive that the terms used to specify the exemptions referred to in Article 13(A) thereof are to be strictly construed. That provision does not exempt from VAT every activity performed in the public interest, but only those which are listed and described in great detail in it (see Case C-149/97 *Institute of the Motor Industry* [1998] ECR I-7053, paragraphs 17 and 18, and Case C-384/98 *D.* [2000] ECR I-6795, paragraphs 19 and 20.)

31 Article 13(A)(1)(i) of the Sixth Directive does not make any reference to the research activities of State universities which are exempt from VAT under Paragraph 4(21a) of the UStG. In addition, it is clear from the case-law cited in the previous paragraph that the definition of 'supply of services closely related to university education' for the purposes of Article 13(A)(1)(i) of the Sixth Directive covers the supply of services or of goods directly necessary for education, such as the provision of teaching materials. The fact that research activities for the benefit of private persons may be of assistance to education is not sufficient, however, to establish the existence of a legal relationship between education and the activities in question which is as close as that required by that provision.

32 Furthermore, in respect of the German Government's argument according to which the exemption in question permits fiscal simplification and avoids administrative costs, the Commission recalls that, as regards the opening words of Article 13(B) of the Sixth Directive, which are identical to those of Article 13(A)(1), the Court has held that the conditions for exemptions laid

down by Member States cannot define the content of the exemptions provided for (see Case C-468/93 *Gemeente Emmen* [1996] ECR I-1721, paragraph 19).

33 The German Government maintains that the action is unfounded, in the first place because Article 2 of the Sixth Directive is neither an obligation nor a prohibition. That provision, which provides that the transactions mentioned are to be 'subject' to VAT, does no more than define the basis of assessment, that is, what is taxable ('Steuerbarkeit'), and not liability to tax ('Steuerpflichtigkeit') (see Case C-158/98 *Coffeeshop 'Siberië'* [1999] ECR I-3971, paragraphs 14, 21 and 23). It is not possible to infringe a provision which contains only a mere definition. The liability to tax of the activities referred to in Article 2 is possible only where that provision is read in conjunction with Article 13(A) of the Sixth Directive, which sets out the criteria for the exemptions laid down for certain activities. Therefore the complaint advanced by the Commission in its application cannot be upheld.

34 Second, the German Government argues that the application is unfounded because the exemption from tax of the research activities of State universities is justified under Article 13(A)(1)(i) of the Sixth Directive.

35 In that respect, it argues that research is a service closely related to education in State universities. Research and teaching activities in those establishments cannot be separated. Those establishments indeed need research in order to succeed in their teaching since it allows them to develop and convey knowledge. Contrary to the Commission's claims, the collaboration between State universities and the commercial world, in the context of research activities financed by funds from third parties, is not only of assistance to higher education, but absolutely essential, in the same way as teaching material.

36 In universities, teaching is not a scientific activity detached from any aim, but above all it makes it possible to gain a qualification with a view to exercising a professional activity in the economy, which also corresponds to the purpose of studies as defined in Paragraph 7 of the Hochschulrahmengesetz (framework law on higher education establishments) of 9 April 1987 (BGBl. 1987 I, p. 1170) in the version of 19 January 1999 (BGBl. 1999 I, p. 18). In the course of their day-to-day work, university teachers can ensure the required link between higher education and professional life only by maintaining such a link themselves. For that reason, it is not possible to give up research projects under contract and in collaboration with the commercial sector.

37 As for the objective of simplifying the payment of VAT, the German Government asserts that it is not a justification for the exemptions, but an additional aspect which appeared in the context of a criterion for exemption. If such a criterion is applicable, in the present case that in Article 13(A)(1)(i) of the Sixth Directive, fiscal simplification measures can be taken into consideration. The expression 'the supply of services and of goods closely related thereto' should therefore also be interpreted having regard to fiscal simplification. In that respect the German Government relies on the close connection between research and teaching as well as the inefficiency and bureaucratic complications which would be generated by the distinction between areas subject to VAT and areas exempt from VAT in State universities.

Findings of the Court

38 First, the German Government's argument according to which Article 2 of the Sixth Directive does not contain a definition of liability to VAT must be

dismissed. As the Court recalled in Case 203/87 *Commission* v *Italy* [1989] ECR 371, paragraph 2, that provision defines the transactions which are to be subject to VAT as 'the supply of goods or services effected for consideration within the territory of the country by a taxable person acting as such' and 'the importation of goods'.

39 The Sixth Directive provides for exemptions from VAT for certain categories of those transactions, in particular in Title x thereof, which includes Article 13. In so far as an exemption is not provided for by the Sixth Directive, it constitutes a derogation from the general rule set out in Article 2 thereof. Such a derogation can comply with Community law only if it is authorised in accordance with the provisions of that directive (see, to that effect, Case 203/87 *Commission* v *Italy*, cited above, paragraph 10).

40 Therefore, national legislation exempting transactions from VAT, which is neither covered by an exemption laid down in the Sixth Directive nor authorised in accordance with an exception provided for by that directive, constitutes an infringement of Article 2 thereof.

41 Second, it is significant that the German Government does not deny that, when they carry out the research activities in question in the present case, State universities must, in principle, be regarded as taxable persons within the meaning of Article 4(1) of the Sixth Directive and nor does it claim that Article 4(5) is applicable to such activities.

42 The dispute is therefore concerned exclusively with the question whether research activities carried out for consideration by State universities constitute services

which are 'closely related' to university education within the meaning of Article 13(A)(1)(i) of the Sixth Directive and which must as such be exempt from VAT under that provision.

43 In that connection, the terms used to specify the exemptions provided for by Article 13 of the Sixth Directive are to be interpreted strictly, since they constitute exceptions to the general principle that VAT is to be levied on all services supplied for consideration by a taxable person (see, in particular, Case 348/87 *Stichting Uitvoering Financiële Acties* [1989] ECR 1737, paragraph 13; *Institute of the Motor Industry*, paragraph 17, and *D.*, paragraph 15).

44 It is settled case-law that those exemptions constitute independent concepts of Community law whose purpose is to avoid divergences in the application of the VAT system from one Member State to another (see, in particular, Case C-349/96 *CPP* [1999] ECR I-973, paragraph 15, and Case C-240/99 *Skandia* [2001] ECR I-1951, paragraph 23).

45 It must also be remembered that the aim of Article 13(A) of the Sixth Directive is to exempt from VAT certain activities which are in the public interest. That provision does not however provide exemption from the application of VAT for every activity performed in the public interest, but only for those which are listed and described in great detail in it (see, in particular, *Institute of the Motor Industry*, paragraph 18).

46 Also, Article 13(A)(1)(i) of the Sixth Directive does not contain any definition of the concept of services 'closely related' to university education.

47 Nevertheless, that concept does not require an especially strict interpretation since the exemption of the supply of services closely related to university education is designed to ensure that access to the benefits of such education is not hindered by the increased costs of providing it that would follow if it, or the supply of services and of goods closely related to it, were subject to VAT (see, by analogy, in relation to Article 13(A)(1)(b) of the Sixth Directive, Case C-76/99 *Commission* v *France* [2001] ECR I-249, paragraph 23). However, if the undertaking by State universities of research projects for consideration is made subject to VAT, that does not have the effect of increasing the cost of university education.

48 In addition, contrary to the German Government's arguments, although the undertaking of such projects may be regarded as of great assistance to university education, it is not essential to attain its objective, that is, in particular, the teaching of students to enable them to pursue a professional activity. Indeed, many universities achieve this aim without carrying out research projects for consideration and there are other ways to ensure a link between university education and professional life.

49 Therefore, the undertaking by State universities of research projects for consideration cannot be regarded as an activity closely related to university education for the purposes of Article 13(A)(1)(i) of the Sixth Directive.

50 In relation to the German Government's argument concerning the simplification of the payment of VAT, it should be recalled that, according to settled case-law, although the introductory sentence of Article 13(A)(1) of the Sixth Directive states that Member States are to lay down the conditions for exemptions in order to ensure the correct and straightforward application of the exemptions and to

prevent any possible evasion, avoidance or abuse, those conditions cannot affect the definition of the subject-matter of the exemptions envisaged (see, in particular, Case C-124/96 *Commission* v *Spain* [1998] ECR I-2501, paragraphs 11 and 12, and Case C-76/99 *Commission* v *France*, cited above, paragraph 26).

51 Therefore, in a situation such as that in the present case, in which the national legislation in question does not satisfy the exemption criteria laid down in Article 13(A)(1)(i) of the Sixth Directive, the fact that it is said to constitute a measure for fiscal simplification is irrelevant.

52 It must therefore be concluded that, by exempting from VAT the research activities carried out for consideration by State universities pursuant to Paragraph 4(21a) of the UStG, the Federal Republic of Germany has failed to fulfil its obligations under Article 2 of the Sixth Directive.

Costs

53 Under Article 69(2) of the Rules of Procedure, the unsuccessful party is to be ordered to pay the costs if they have been applied for in the successful party's pleadings. Since the Commission has applied for costs and the Federal Republic of Germany has been unsuccessful, the latter must be ordered to pay the costs.

On those grounds,

THE COURT (Fifth Chamber)

hereby:

1. **Declares that, by exempting from value added tax the research activities carried out for consideration by public-sector higher-education establishments pursuant to Paragraph 4(21a) of the Umsatzsteuergesetz (Law on Turnover Taxes) of 27 April 1993, as amended by Paragraph 4(5) of the Umsatzsteuergesetz-Änderungsgesetz of 12 December 1996, the Federal Republic of Germany has failed to fulfil its obligations under Article 2 of the 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;**

2. **Orders the Federal Republic of Germany to pay the costs.**

Jann von Bahr

Edward La Pergola Timmermans

Delivered in open court in Luxembourg on 20 June 2002.

R. Grass P. Jann

Registrar President of the Fifth Chamber