OPINION OF ADVOCATE GENERAL SHARPSTON
delivered on 14 June 2007 [1]

1. A private limited company, and the individual who is its sole shareholder, sole director and sole employee, are treated by the tax authorities as a single taxable entity for VAT purposes. That is possible only if the individual can first be regarded as a taxable person in respect of his work for the company. The Gerechtshof te Amsterdam (Regional Court of Appeal, Amsterdam) therefore wishes to know whether that work is an 'economic activity' independently carried out within the meaning of the Sixth VAT Directive. [2]

Relevant VAT law

Community legislation

2. At the material time in the main proceedings, Article 2 of the Sixth Directive required that the tax should apply to 'the supply of goods or services effected for consideration within the territory of the country by a taxable person acting as such'. [3]

3. Article 4 provided, in so far as relevant:

'1. "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.

2. The economic activities referred to in paragraph 1 shall comprise all activities of

1 — Original language: English.

2 — 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, amended on numerous occasions but not as regards the provisions cited here). On 1 January 2007, the Sixth Directive was repealed and replaced by Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ 2006 L 347, p. 1).

3 — The same provision is in Article 2(1)(a) of Directive 2006/112.

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. The use of the word "independently" in paragraph 1 shall exclude employed and other persons from the tax in so far as they are bound to an employer by a contract of employment or by any other legal ties creating the relationship of employer and employee as regards working conditions, remuneration and the employer's liability.

... each Member State may treat as a single taxable person persons established in the territory of the country who, while legally independent, are closely bound to one another by financial, economic and organisational links.

...'[4]

Netherlands legislation

4. Under Article 7(1) of the Wet op de Omzetbelasting (Turnover Tax Law) 1968, a trader is 'any person who carries on a business independently'. Under Article 7(2), a 'business' includes both the exercise of a trade or profession and the exploitation of property for the purpose of obtaining income on a continuing basis.

5. Under Article 7(4) of the same Law, traders thus defined, if they are financially, organisationally and economically linked in such a way that they form an entity, are to be treated as a single trader. The decision to treat them in that way is to be taken by the competent tax inspector.

Community case-law

6. In *Heerma*,[5] a reference for a preliminary ruling from the Netherlands Hoge Raad

4 — Provisions substantially reproduced in Articles 9(1), 10 and 11 of Directive 2006/112.

5 — Case C-23/98 [2000] ECR I-419.

(Supreme Court), a farmer had formed a partnership with his wife, to which he had contributed the means of production of his holding. He later built a cattle shed and let it to the partnership for an annual rent. He and the partnership asked to be excluded from the exemption from VAT in respect of that letting. [6]

7. The Court ruled that 'Article 4(1) of the [Sixth Directive] is to be interpreted as meaning that, where a person's sole economic activity, within the meaning of that provision, consists in the letting of an item of tangible property to a company or a partnership, such as a partnership governed by Netherlands law, of which he is a member, that letting must be regarded as an independent activity within the meaning of that provision'.

8. In reaching that view, it noted that 'there is between the partnership and the partner no relationship of employer and employee similar to that mentioned in the first subparagraph of Article 4(4) of the Sixth Directive which would preclude the independence of the partner. On the contrary, the partner, in letting tangible property to the partnership, acts in his own name, on his own behalf and under his own responsibility, even if he is at the same time manager of the lessee partnership. The lease in question was granted neither by the management nor by the representatives of the partnership'. [7]

Netherlands case-law

9. In a subsequent case, [8] the Hoge Raad relied on *Heerma* in order to interpret Article 7(4) of the Wet op de Omzetbelasting in a situation where an individual who was director of a company in which he held 75% of the shares invoiced his management services to the company. It noted that, under Netherlands law, a director was an employee of the company, but that, unlike a normal employee, he was not in a position of subordination vis-à-vis the company. That being so, it considered that the person concerned had necessarily acted in an independent capacity when providing the company with management services. In reaching that view, it relied also on the wording of Article 4(4) of the Sixth Directive, [9] and on the Court's judgment in *Asscher*. [10]

6 — Exemption and optional exclusion therefrom pursuant to Article 13B(b) and 13C(a) of the Sixth Directive.

7 — Paragraph 18 of the judgment.

8 — Judgment No 35 775 of 26 April 2002; see in particular points 3.6 to 3.10.

9 — In particular the words 'creating the relationship of employer and employee'.

10 — Case C-107/94 [1996] ECR I-3089.

10. *Asscher* concerned the Treaty rules on freedom of movement for persons and their effect on income tax provisions. In its judgment, [11] the Court stated that the activity of a person who was director of a (Netherlands) company of which he was also sole shareholder was 'not carried out in the context of a relationship of subordination', so that he was to be treated 'not as a "worker" within the meaning of Article [39 EC] but as pursuing an activity as a self-employed person within the meaning of Article [43 EC]'. The case did not concern the notion of employment in the context of VAT.

The proceedings and the question referred

11. Mr van der Steen ran a one-man business providing cleaning services, in which capacity he was a trader within the meaning of the Wet op de Omzetbelasting.

12. He then set up the private limited company J.A. van der Steen Schoonmaakdiensten BV ('the company'), with himself as sole director and sole shareholder. The company, which was a trader within the meaning of the Wet op de Omzetbelasting, took over his business. He continued to perform all the work of the business, having entered into an oral contract of employment with the company. [12] The company paid him a fixed monthly salary and annual holiday payment, from which it deducted the relevant taxes and social security contributions. There were no other employees.

13. The company later became insolvent. The business was taken over by another company. [13] Mr van der Steen's employment with his own company ceased, and he was then employed by the second company.

14. In the process of settling the VAT accounts of Mr van der Steen and the insolvent company, the tax inspector decided that the two constituted a fiscal entity pursuant to Article 7(4) of the Wet op de Omzetbelasting. In doing so, he referred to the Hoge Raad's judgment No 35 775 and to a decision of the Staatssecretaris van Financiën (State Secretary for Finance) [14] based on that judgment. The latter decision states, in particular, that 'the director of a company of which he holds more than half the shares

11 — At paragraph 26.

12 — If this is literally true, one can only hope he was alone with himself at the time, as the mechanics of concluding such a contract would have appeared rather bizarre to any casual bystander.

13 — The order for reference gives no details, but it seems implicit that Mr van der Steen was neither shareholder nor director of this company. The point is in any event immaterial to the present case.

14 — Decision DBG2002/3677M of 24 July 2002.

qualifies as a trader within the meaning of Article 7 of the Wet op de Omzetbelasting in respect of the activities carried out for the company in return for remuneration. It makes no difference in that regard whether the activities in question were or were not carried out on the basis of a contract of employment entered into with the company'.

15. Mr van der Steen's legal challenge to the inspector's decision is now before the Gerechtshof te Amsterdam, which points out that it is a prerequisite for that decision that Mr van der Steen should qualify as a trader for VAT purposes, but is uncertain whether such an assessment is compatible with Community law.

16. The Gerechtshof therefore requests a preliminary ruling on the question:

'Is Article 4(1) of the Sixth Directive to be interpreted as meaning that if a natural person has the sole activity of actually carrying out all work ensuing from the activities of a private limited company of which he is the sole manager, sole shareholder and sole "member of staff", that work is not an economic activity because it is carried out in the course of the management and representation of the private limited company and thus not in economic dealings?'

17. The Netherlands Government and the Commission have submitted written observations, both to the effect that a person in the situation described is not independently carrying out an economic activity. Mr van der Steen has submitted no observations. No party has requested a hearing and none has been held.

Assessment

18. As the Commission points out, when an entrepreneur sets up a company to carry on his business, the purpose is generally to establish a separate legal persona, distinct from his own. [15] That is particularly useful in limiting his personal liability in respect of the business. [16]

19. Where two separate legal entities exist, it is clear that they may act independently of

15 — The legal provisions governing such companies are to some extent harmonised by the Twelfth Council Company Law Directive 89/667/EEC of 21 December 1989 on single-member private limited-liability companies (OJ 1989 L 395, p. 40).

16 — Compare Article 7 of the same directive, under which '[a] Member State need not allow the formation of single-member companies where its legislation provides that an individual entrepreneur may set up an undertaking the liability of which is limited to a sum devoted to a stated activity'.

each other, and that they may enter into various kinds of legal relationship with each other.

20. For example, in *Heerma*, the farmer and the partnership were separate entities, and it was possible for the farmer to grant to the partnership a lease of immovable property belonging to him. In doing so, the Court decided, he was independently exercising an economic activity for VAT purposes.

21. In the present case, Mr van der Steen and the company were separate entities, and Mr van der Steen was able to — and did — enter into a contract of employment with the company.

22. In so far as the work he provided to the company fell within the scope of that contract of employment, it is in principle excluded from the scope of VAT by the clear terms of Article 4(4) of the Sixth Directive.

23. In that respect, his situation contrasts with that of Mr Heerma, since the leasing and letting of immovable property are activities which do fall within the scope of VAT and are indeed explicitly mentioned in Article 13B(b) and 13C(a) of the Sixth Directive. [17]

24. On that basis, it would appear that the tax inspector's decision contested by Mr van der Steen does not reflect a correct interpretation of Community law. To the extent that it is based on a decision of the Staatssecretaris van Financiën and a judgment of the Hoge Raad, the latter may also reflect an incorrect interpretation.

25. The advantages in excluding employment from the scope of VAT are obvious. If it were not excluded, every employee would have to be registered for VAT and the tax would have to be charged on all salaries. Employers making taxable supplies would admittedly be able to deduct that VAT, but there would be a considerable burden on those making exempt supplies unless a compensatory mechanism were introduced, and such a mechanism would itself be burdensome. By contrast, when employment is excluded from the scope of VAT, the cost of that employment forms part of the value

17 — Article 135(1)(l) and (2) of Directive 2006/112.

added to output supplies. It is thus automatically included in the tax base when those supplies are taxed, but has no effect, in VAT terms, on exempt output supplies. In addition to a considerable saving in administrative work, the neutrality of the tax and its general application to taxable supplies are ensured.

26. Consequently, it is not desirable that an activity which falls within the scope of a contract of employment should be treated as an independent taxable activity.

27. The reasons which led the Hoge Raad and the Staatssecretaris van Financiën to take the view on which the contested decision is based appear to flow from two judgments of the Court — *Heerma* and *Asscher* [18] — and from the nature of the relationship between a company and its directors in Netherlands law.

28. I do not think that the two judgments cited support that view. *Heerma* did not concern a contract of employment but the clearly independent and clearly taxable activity of leasing or letting immovable property. *Asscher* distinguished between employment and self-employment on the basis of the existence or absence of a relationship of 'subordination' but that was, as the Commission points out, in the entirely different context of determining the applicable Treaty article in the field of freedom of movement.

29. It is more difficult for the Court to express a view as regards the relationship between a company and its directors in Netherlands law. [19] From the Hoge Raad's judgment No 35 775, [20] it seems that services provided by a director to the company, in his capacity as director, may be *deemed* to be provided under a contract of employment. If that is so, the judgment may be authority for the proposition that for VAT purposes such services should not automatically be deemed to be so provided. That proposition does not necessarily conflict with the exclusion of *actual* employment from the scope of VAT. It may mean no more than that, when a service would otherwise have been deemed to fall within the scope of a contract of employment, for VAT purposes it should none the less be examined to determine whether it was not in fact provided in the exercise of an independent activity.

18 — See points 6 to 8 and footnotes 5 and 10 above.

19 — See, however, in the context of social security, Case 79/85 *Segers* [1986] ECR 2375 and Joined Cases C-393/99 and C-394/99 *Hervein and Others* [2002] ECR I-2829.

20 — In particular at point 3.8.

30. That said, as the Commission points out, in the present case there is nothing in the case-file to suggest that any of Mr van der Steen's services to the company were provided in the context of anything other than a true contract of employment.

31. It is of course always possible — regardless of any other aspects of the relationship between the parties -– that what appears to be a true contract of employment transpires on closer inspection to be a different kind of arrangement. Again, there is nothing in the case-file to suggest that to be so in the case of Mr van der Steen's contract. Rather, the fact that he received a fixed monthly salary subject to wages tax and social security contributions militates strongly against such an interpretation.

32. I am therefore of the view that services provided to a company by a person in Mr van der Steen's position, as described in the order for reference, fall outside the scope of VAT by virtue of Article 4(4) of the Sixth Directive, and that such a person is not, in respect of such services, a taxable person within the meaning of Article 4(1).

33. A number of additional considerations have been put forward by the Netherlands Government and the Commission.

34. First, the person concerned does not act 'in his own name, on his own behalf and under his own responsibility' [21] when providing his services as employee. He acts in the name, on the behalf and under the responsibility of the company.

35. Second, in his capacity as employee, the person concerned bears no independent economic risk. [22] That risk is borne by the company which enters into contracts with customers and provides them with economic services.

36. Third — at least on the transaction-by-transaction level on which VAT operates — there is no reciprocal performance in which the remuneration received by the provider of the service constitutes the value actually given in return for the service supplied to the recipient. [23] The person concerned receives a fixed amount of salary and holiday pay, regardless of the services actually provided. [24]

21 — *Heerma*, paragraph 18.

22 — Case C-202/90 *Recaudadores de Tributos* [1991] ECR I-4247, paragraph 13; Case C-210/04 *FCE Bank* [2006] ECR I-2803, paragraph 33 et seq.

23 — Case C-16/93 *Tolsma* [1994] ECR I-743, paragraph 14; Case C-174/00 *Kennemer Golf & Country Club* [2002] ECR I-3293, paragraph 39.

24 — There is no indication that such a factor contributed to the company's insolvency in the present case, but the fact that it would have been capable of doing so underlines the distinction between salary received and value given.

37. I am thus confirmed in my view that, since a person in Mr van der Steen's position is not a taxable person with regard to services provided under the contract of employment, he cannot in that regard be treated together with the company as a 'single taxable person' within the meaning of the second paragraph of Article 4(4) of the Sixth Directive or, consequently, as a single trader for the purposes of Article 7(4) of the Wet op de Omzetbelasting.

38. Of course, none of the above considerations affects the possibility that a person who is sole shareholder, sole director and sole employee of a company may also be a taxable person in his own right in the context of other economic activities falling outside the scope of the contract of employment. When such activities involve dealings with the company it may be possible, depending on all the circumstances, for the individual and the company to be treated as a single taxable person. However, those are not the facts as described in the order for reference.

Conclusion

39. In the light of the foregoing considerations, I am of the opinion that the Court should answer the question raised by the Gerechtshof te Amsterdam as follows:

A natural person who supplies services to a taxable person pursuant to a contract of employment is in that context not himself a taxable person within the meaning of Article 4(1) of Sixth Council Directive 77/388/EEC because he is not independently carrying out an economic activity. Such services are, on the contrary, excluded from

the scope of VAT by virtue of Article 4(4) of the same directive. In that regard, it is immaterial whether the employer is a legal person of which the employee is also a shareholder and/or director, or even sole shareholder and sole director, provided that the two parties have separate legal personality with the capacity to enter into a contract of employment between them and have in fact entered into such a contract pursuant to which the services are supplied.