OPINION OF ADVOCATE GENERAL MISCHO

delivered on 23 November 2000 [1]

1. This action by the Commission of the European Communities against the French Republic for failure to fulfil its obligations with regard to the implementation 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] ('the Sixth Directive') once again leads the Court to consider, though in a somewhat unusual way, the question of national administrative practices in regard to the obligations resulting from directives.

2. Generally, a Member State which the Commission alleges has not correctly transposed a directive puts forward as its defence, with more or less conviction, the fact that, even if the national legislature has not acted to implement the directive, the authorities have done everything necessary, usually by issuing a circular, to ensure that the directive is in practice given effect in national law, but the case we have today is the opposite.

3. What the Commission alleges against the French Republic is not at all the absence of legislative provisions correctly transposing the Sixth Directive but the official toleration, at the level of administrative practice, of deviations from the implementing national law, which itself is in complete harmony with the Sixth Directive.

4. Article 2(1) of the Sixth Directive provides:

'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;'

1 — Original language: French.

2 — OJ 1977 L 145, p. 1.

and Article 11A(1)(a) states that:

'1. The taxable amount shall be:

(a) in respect of supplies of goods and services other than those referred to in (b), (c) and (d) below, everything which constitutes the consideration which has been or is to be obtained by the supplier from the purchaser, the customer or a third party for such supplies including subsidies directly linked to the price of such supplies.'

5. The Commission accepts that the French Republic has transposed these measures correctly, since Articles 266-I A and 267-I of the Code général des impôts provide respectively that:

'The taxable amount shall be:

in respect of supplies of goods and services and intra-Community acquisitions, all sums, assets, goods or services received or receivable by the supplier from the purchaser, the customer or a third party for such supplies including subsidies directly linked to the price of such supplies.'

and that:

'The taxable amount shall include:

1. Taxes, duties, levies and charges of any kind, excluding the value added tax itself.

2. Expenses incidental to supplies of goods or services, such as commissions, interest, packing, transport and insurance costs charged to customers.'

6. According to the Commission, the French Republic has nonetheless failed to fulfil the obligations arising from the articles of the Sixth Directive cited above in authorising, by means of an administrative instruction published in the *Bulletin officiel de la direction générale des impôts* of 31 December 1976 making permanent a previous practice, certain taxable persons to exclude the service charges claimed from their customers from the taxable amount for value added tax (hereinafter 'VAT').

7. More specifically, the 'basic documentation' published by the Director-General for Taxation, which taxpayers can rely on to ascertain the exact extent of their tax

liabilities, states that: 'according to the fixed policy of the administration, price supplements charged by way of a tip to customers of commercial undertakings (hotels, restaurants, cafés, brasseries, bars, tea-rooms, hairdressers, clinics, spas, transport and removal businesses, rest and retirement homes, casinos, home delivery services of any kind) constitute part of the price on which value added tax is to be levied', but it is indicated that such increases in the price may be excluded from the taxable amount for VAT if the four following conditions are all satisfied:

(1) the customer is informed at the outset of the existence of a levy having the nature of a gratuity, and of its percentage by reference to the 'service not included' price;

(2) all 'gratuities' are shared among the members of staff who have direct contact with the customer;

(3) the payment is accounted for in a special register signed by each of the beneficiaries, or at least by a staff representative;

(4) the annual return of wages filed by the employer shows the total remuneration actually received by the staff remunerated by gratuities.

8. For the Commission, this tolerance amounts to a system of exemption from VAT contrary to Community law, taking the form of a method of determining the taxable amount which fails to comply with the rules laid down in the Sixth Directive, since part of what is invoiced to the customer, and is thus consideration for the service rendered, escapes the tax.

9. In this respect, the Commission states that its criticism is not directed to what it describes itself as 'extra gratuities', and which the French authorities describe as free gratuities, that is to say money which a customer leaves spontaneously and without obligation to any particular employee.

10. The Commission accepts that these amounts, by contrast with compulsory service charges, do not need to be included in the taxable amount, since they are like the donations made by passers-by to a barrel-organ player in the street, in regard

to which the Court ruled in Case C-16/93 *Tolsma*.[3] In both cases, the payments are entirely gratuitous and uncertain, and it is practically impossible to ascertain their amount.

11. But, in the Commission's opinion, the exclusion of service charges from the taxable amount cannot be justified when they are of a predetermined amount, are compulsory, and do not appear in the exhaustive list of sums not included in the taxable amount found in Article 11A(1) of the Sixth Directive.

12. Moreover, again in the Commission's view, the practice at issue is open to the objection of being contrary to the principle of fiscal neutrality, which underlies the whole of the Community system of VAT, since two taxable persons undertaking exactly the same activity may be taxed differently depending on whether or not their invoices show separately the amounts intended as remuneration for their employees; and this breach of the principle of fiscal neutrality is itself apt to create distortion of competition, since a different tax treatment of activities carried out in identical circumstances necessarily has an effect on the conditions of competition.

3 — [1994] ECR I-743.

13. In the Commission's view, the four conditions laid down in the administrative instruction at issue to enable a supplier to benefit from the exclusion of service charges from the taxable amount are entirely procedural in character and have nothing to do with the criteria for establishing the basis of assessment for VAT, namely the consideration actually received by the supplier of the service. Reference to these conditions introduces an arbitrary element into the determination of the tax burden on the various suppliers in the same sector when there is no justification for treating them differently.

14. The French Government devotes the main part of its defence to a description of the context in which the administrative instruction of 1976 was issued.

15. It explains that the instruction goes back to a ministerial decision in 1923 which accepts that the turnover tax, that is to say the tax which, historically, preceded VAT in the French tax system, should not be applied to receipts of obligatory gratuities by hoteliers and restaurant owners, and by commercial establishments more widely, whenever the whole of the sums received on that account were in fact paid out to staff.

16. Later, for the purpose of fiscal control, a circular in 1928 made the benefit of this

concession dependent on there being a special register showing the collection and redistribution of such sums.

17. According to the French Government, the administrative concession was made permanent by a law of 1933 on staff remuneration, which adopted the principle that gratuities received as remuneration for service as an obligatory percentage added to bills or otherwise, as well as all sums paid to an employer by customers voluntarily in respect of service or handled centrally by him, should be paid entirely to the staff who were in contact with the customers, and to whom the latter generally gave the payments.

18. This law made it possible to provide security for staff remunerated chiefly by gratuities at a time when there was no minimum wage.

19. As to the current situation, the French Government dwells on the fact that only establishments which employ staff who are in direct contact with customers and who are remunerated by means of the service charge included in the price paid by the customer, that is to say principally restaurants and hairdressers, enjoy the concession, and that it has opposed the extension of it to self-service restaurants and fast-food outlets.

20. The Government also points out that the VAT rules applicable to gratuities vary depending on the way in which the service charge is levied, that is, depending on whether prices are displayed as being 'service included' or 'service not included', but the cases of 'service not included' have become marginal since establishments serving meals, food or drinks to be consumed on the premises have, since the publication of a decree in 1987, been required to display their prices as 'service included'.

21. In reply to the criticisms of the Commission about the anti-competitive effect of the concession confirmed by the 1976 administrative instruction and the arbitrary nature of the conditions it imposes, the French Government draws attention to the fact that it is merely a tolerance, that undertakings are free to apply it or not, the rule remaining that contained in Article 266-I A of the Code général des impôts. It adds that undertakings which are not able to benefit from the tolerance are not carrying on business in the same circumstances as those which can, and that conditions which guarantee the payment to employees of sums received and provide a strict framework for the exemption allowed cannot be characterised as arbitrary.

22. In its reply, the Commission is content to observe that the explanations provided by the French Government about the historical context of the disputed tolerance have no relevance in deciding its compatibility with the Community system of VAT.

23. The Commission also points out that, if the exemption from turnover tax for gratuities to staff could, when it was introduced, be justified by the desire not to penalise those establishments which, instead of leaving gratuities to the discretion of customers, chose to levy them compulsorily in order to pay them to their staff for whom it was frequently the only form of remuneration, that is no longer the case today when there is a minimum wage and when sums levied by an employer by way of service charge have to be paid on to employees.

24. It is, indeed, in view of this mismatch between what might have been a justification for the exemption at a given moment, and the present legal context, that the Commission had felt justified in describing the four conditions laid down in the administrative instruction of 1976 as arbitrary.

25. It appears to the Commission that it is equally impossible to sustain the argument that the limited character of the derogation should be taken into account in assessing its compatibility with the Community VAT system.

26. In its rejoinder, the French Government sets out to correct certain errors which it says the Commission has made in its reply. Thus, it is inaccurate to assert that the origin of the tolerance is to be found in a desire not to disadvantage establishments which paid back all gratuities to their staff.

27. In fact, it was the protection of the employees which was sought, and this protection remains of current concern because, notwithstanding the introduction of a minimum wage, the remuneration of employees in direct contact with customers in the restaurant and hairdressing sectors is still today made up in part of gratuities. Abolishing the tolerance might extend the practice of optional gratuities, which would penalise employees in direct contact with customers, particularly in sectors where the publication of prices as 'service included' is not compulsory.

28. Nor can it be claimed, as the Commission does in its reply, that the publication of prices as 'service included' has become the rule.

29. In the hairdressing business, for example, there is no such obligation. For that reason, the distinction between establishments offering 'service included' prices and those with 'service not included' prices retains its importance.

30. The French Government reiterated, once more, the limited character of the derogation criticised. That itself is the

consequence of the strict conditions which must be fulfilled by a supplier taking advantage of it, and is confirmed by the information disclosed by an enquiry conducted by the Ministère de l'Économie, des Finances et de l'Industrie (Ministry for the Economy, Finance and Industry) which shows that in the restaurant sector only a few establishments, principally brasseries which employ a large workforce, avail themselves of it.

impôts, but a mere administrative tolerance which undertakings are free to apply or not.

34. Finally, it points out that the very limited nature of the exemption is such that it falls within the *de minimis* principle.

Analysis

31. We can see at the outset that the exchange of arguments during the written procedure is not much removed from a dialogue of the deaf.

32. The French Government never attempts to demonstrate that the practice in question can be justified by a provision of the Sixth Directive. It points out simply that the practice is of long standing, but is within a strict framework, and has a whole series of advantages as regards the need to guarantee a satisfactory level of income for employees in certain types of establishment.

33. It goes on to emphasise that the exclusion from the taxable amount for VAT accorded to gratuities is not a rule modifying Article 266-I A of the Code général des

35. In this respect, it should be borne in mind firstly that under Article 11A(1)(a) of the Sixth Directive the taxable amount for VAT is made up, for supplies of goods and services, of 'everything which constitutes the consideration which has been or is to be obtained by the supplier from the purchaser, the customer or a third party...'. Moreover, according to the settled case-law reviewed in Case C-258/95 *Fillibeck* [1997] ECR I-5577,[4] the taxable amount for the supply of goods or services is composed of the consideration actually received for that purpose, which is the consideration that is in fact received and not a value estimated on the basis of objective criteria.

36. The total sum appearing on the invoice to the customer constitutes, obviously and in its entirety, the consideration for the service which has been supplied to him by the restaurateur.

4 — Paragraph 13.

37. This consideration, unlike that in certain cases which have been before the Court, presents no difficulty in ascertaining its exact amount because, by definition, it is expressed in monetary terms.

38. And it is beside the point that an apportionment may be made in the invoice between the different elements which, together, have made up the service supplied.

39. In France today separate invoicing for restaurant service is prohibited but, in other Member States, it systematically appears on restaurant bills as a separate item. Could one really suppose that, in those Member States, the taxable amount invoiced by the restaurateur would not include the sum stated to be for service?

40. The customer in a restaurant buys a comprehensive supply, made up of the meal he is going to eat, the use of the table at which he eats it, whatever he needs to eat it with and the service at the table; and the sum of money which he pays is a comprehensive payment for that comprehensive supply. To buy a ready-cooked meal from a caterer is to buy goods, whereas to have lunch in a restaurant is to receive the supply of a service which includes the delivery of goods but which comprises a whole series of other elements which cannot be dissociated from it.

41. If the item for 'service charge' in a restaurant bill were to be considered, having regard to the definition of taxable amount in the Sixth Directive, not to be subject to VAT, there would be nothing to prevent a garage which, in accordance with usual practice, itemises separately the cost of spare parts and the cost of labour, from claiming the right to treat as outside the scope of VAT some, if not all, of the labour in the invoice for the servicing of the vehicle which could be identified as relating to the activity of the employee who dealt with the customer enquiring about the work which he wanted done on his vehicle, and who delivered it to him when the work was finished.

42. I could go on giving examples ad infinitum, but there is no need to do so since it is clear that Article 11A(1)(a) of the Sixth Directive requires that all the elements invoiced to a customer by a supplier are to be considered as making up the precise consideration for the supply made to him.

43. The Commission also, as we have seen, puts forward an argument to the effect that the practice of the French tax administra-

tion undermines fiscal neutrality and leads to distortion of competition.

44. I agree with the Commission that the practice at issue is in breach of the principle of fiscal neutrality which, in the words of the judgment in Case C-216/97 *Gregg* [1999] ECR I-4947, 'precludes, *inter alia*, economic operators carrying on the same activities from being treated differently as far as the levying of VAT is concerned'. [5]

45. Two restaurateurs offering exactly the same service, for an identical total price, but one of whom states on his invoice that a service charge is levied, and the other of whom does not state it but does include in his invoice a sum corresponding to the service charge, will on the basis of the administrative instruction of 1976 find that they have differing demands for VAT, because the taxable amount used as the basis for assessing the tax due will be different for each of them, even though the supply and the consideration for it will have been exactly the same.

46. From the difference at the level of the charge to tax there will flow a difference at the level of the profit made from the transaction, so that a nonsense will be made of the principle of fiscal neutrality and competition will be distorted.

5 — Paragraph 20.

47. We must now examine the relevance of the grounds of defence relied on by the French Government, which argues that an establishment fulfilling the four conditions laid down in the administrative instruction of 1976 cannot be said to be conducting its business in conditions identical to those governing the conduct of an establishment not satisfying them and which, on that account, is not permitted to exclude its service charges from its taxable amount.

48. That is why the French Government takes issue with the Commission's description in its application of these conditions as arbitrary. The word was such as to shock the French authorities, in fact, and there would have been some advantage, as the Commission concedes in its reply, in replacing it by 'without relevance'. But the Commission's criticism seems to me essentially right in emphasising that the final destination of the sums levied as service charges, and the way in which they are dealt with, has nothing to do with the question of whether these sums should or should not form part of the taxable amount.

49. What is important is to determine the amount of these sums, assets, goods or services received or to be received by the supplier by way of consideration for the service which he has furnished. The allocation of the sums is wholly irrelevant. What constitutes the taxable amount is not the profit of the supplier but, need I say it, his turnover. That is why the question of what actually becomes of the sums described on

the invoice as service charges is quite immaterial in determining the taxable amount, unless of course there is any provision to the contrary in the Sixth Directive to be taken into account, and no-one in this case has argued that there is any relevant provision in that respect.

50. The way in which the supplier provides for the remuneration of the staff whom he relies on to deliver the service which he supplies is quite immaterial in settling the taxable amount. That, as the Court has held, must correspond to the subjectively ascertained value of the consideration which the supplier has obtained from the customer. The cost of the service to the supplier plays no part in the determination of it, still less does the structure of that cost.

51. A very specific example, drawn once more from the restaurant sector, will assist in understanding how the principle of fiscal neutrality, around which the Community system of VAT is built, can in no way be reconciled with the French practice under consideration.

52. Let us suppose that a restaurateur conducts his business with a single employee. If the owner is the one who waits on the customers while the employee is the chef, the 1976 administrative instruction will offer no possibility of a deduction. Naturally, the restaurateur will be able to break down his bill and show a service charge on it. But he will still not be able to deduct it from his taxable amount since, if he puts together at the end of the day the amount invoiced as service charge, there will be no allocation of it to salaried staff. If, on the other hand, he does pay it to his employee, he will still not be able to deduct it because the beneficiary was not in direct contact with customers.

53. If, on the other hand, it is the owner who is the chef and the employee who waits on the customers, the amounts invoiced as service charges will be deductible from the taxable amount if, of course, the four conditions are satisfied.

54. If the point of view of the French Government were to be accepted, it would mean that the way in which an undertaking was organised could influence the amount of VAT it has to pay, which is precisely what the Community system of VAT, and the principle of fiscal neutrality which underpins it, aims to avoid.

55. Lastly, it should be observed, almost as a side-note and still in connection with those conditions, which the Government claims support its practice, that in Annex 1 to its defence under the heading 'VAT rules applicable to gratuities in relation to the different ways of charging for service' the French Government discloses that a special system operates where the invoice to the customer states 'service not included'. In

that case, gratuities are at the customer's discretion, and the customer may in fact leave nothing by way of gratuity. To the extent that the customer does leave something, the amount is received by the employees from hand to hand. The gratuities may then be shared among the employees by means of a 'kitty' in which they are pooled by a representative of the staff, who then distributes them among the various persons entitled, or they may be allocated on the basis that each employee keeps the gratuities that he receives. In every possible situation, the tax authority includes in the taxable amount — without exception, according to the French Government — a 'reconstituted receipt' corresponding to the amount received by the employees.

56. In my view that is fatal to the French position, which is based precisely on the fact that it is because a supplier does not retain service charges but repays them entirely to his staff that he is permitted in certain cases not to include them in the taxable amount by reference to which the amount of VAT due from him will be calculated. Moreover, this system appears paradoxical, since one would have expected that the French Government would rather have based its case on the uncertainty of the sums received by employees in order, relying on the *Tolsma* decision cited above, simply to exclude them from the taxable amount. Fortunately, it is not my task to explain the mystery of why this Annex was produced.

57. For the remainder, the French Government is content to rely on the point that when the practice made permanent by the 1976 administrative instruction was introduced it was perfectly justified. It maintains that the practice provided security for staff employed in certain sectors, who depended upon gratuities for at least the greater part of their remuneration, and who would have had it curtailed if the employer had redistributed the service charges only after deducting the turnover tax relating to them as a consequence of their being accounted for in the overall receipts of the undertaking.

58. Protection of staff was, and would now still be, essential in certain sectors and the Commission was seriously mistaken to claim, in its reply, that what was of real concern was the competitive position of establishments redistributing all the service charges received.

59. I am willing to accept that the French Government is better placed than the Commission for clarifying the objectives of the French legislature before the Second World War. But that is not the problem. In 1923, the French authorities were free to provide for all the exemptions from the turnover tax that they thought desirable in the context of the French taxation system, just as they remain free today to adopt protective measures for certain categories

of workers who do not enjoy a fixed remuneration.

60. The question today is whether the end justifies the means, namely whether a State is free not to comply with the Sixth Directive where it considers that it has good reasons for not doing so. And to that question the reply can only be in the negative, since otherwise neither the primacy nor the uniform application of Community law would continue to be ensured.

61. The French Republic is perfectly entitled to put the practice with regard to service charges on a permanent footing, and to guarantee certain workers a share in the turnover of their employers by requiring the complete payment over to staff of service charges collected, inasmuch as — and only inasmuch as — it does so without providing the establishments in question with a VAT relief prohibited by the Sixth Directive.

62. The directive is in no way opposed to a protective social policy: it requires only that such a policy should not be pursued by certain means. That involves, indeed, a constraint, but it is inherent in the Community system of VAT which, as the Commission very rightly pointed out in its letter of formal notice also underpins the mechanism of the European Union's own resources.

63. There is a further matter on which the analyses of the Commission and the French Government diverge. It concerns the possible significance for the practice criticised by the Commission of changes in the French legislation on price information for consumers.

64. The Commission believes that a circular in 1988 about prices being displayed on a 'service included' basis recognises that the service charge is an integral part of the price paid by the customer, while the French Government points out that the obligation to display prices 'service included' is far from being as generally applicable as the Commission maintains. But, there also, the dispute seems to me to have no relevance.

65. What the Commission criticises is that the administrative instruction of 1976 lays down a method for calculating the taxable amount which is incompatible with the rules of the Sixth Directive, and the French Government does not dispute that it is in practice applied by a certain number of suppliers of services.

66. Whether these suppliers are numerous or not is of little importance in establishing whether or not there is an infringement. Equally beside the point is the question whether the French authorities succeed, by

the strict enforcement of the four conditions laid down in the administrative instruction of 1976, in limiting the number of establishments which can pass through the breach which they themselves have made in the system of calculation and levying of VAT.

67. The fact is that the Community system of VAT, while it provides for a whole range of exemptions, has no *de minimis* rule which would permit still more to be created, which is what the French Republic has claimed. The infringement seems to me, as a result, to be clearly established.

Conclusion

68. In view of all the above considerations, I consider that the Court should declare that:

— by authorising, under certain conditions, the exclusion from the taxable amount for value added tax of the 'service charges' claimed by certain taxable persons, the French Republic has failed to fulfil its obligations under Articles 2(1) and 11A(1)(a) 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;

— the French Republic should pay the costs.