OPINION OF ADVOCATE GENERAL JACOBS

delivered on 6 March 2003 [1]

1. In the present proceedings, the Bundesfinanzhof (Federal Finance Court, Germany) asks the Court to clarify the status under the Sixth VAT Directive [2] of what it calls 'true factoring'. Factoring is a term used to refer to a variety of services supplied to creditors in connection with the management of their debts. A supplier of such services is known as a factor. True factoring, in the usage of the referring court, describes a transaction whereby the factor purchases debts owed to its client, and thereby assumes the risk of the debtor defaulting. It is thus differentiated from 'quasi factoring' arrangements, in which a factor assists in the administration and collection of debts without any corresponding assumption of the risk of loss.

2. The Bundesfinanzhof raises two questions concerning the analysis of true factoring. By its first question, it aims to establish whether true factoring is an economic activity which involves the supply of a taxable service so as to bring it within the field of application of the Sixth Directive. If so, it seeks by its second question to know whether such factoring falls within one of the categories of exemption from VAT laid down by Article 13B(d).

Legal framework

3. Under Article 2 of the Sixth Directive, a supply of goods or services effected for consideration by a taxable person acting as such is to be subject to VAT. According to Article 4(1), a taxable person is a person who carries out an economic activity, whatever the purpose or results of that activity. Economic activities include, under Article 4(2), 'all activities of producers, traders and persons supplying services' as well as 'the exploitation of tangible or intangible property for the purpose of obtaining income therefrom on a continuing basis'.

4. Title X of the Sixth Directive specifies various exemptions from the obligation to

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 (here after referred to as the 'Sixth Directive').

pay VAT. Article 13B(d) requires Member States to exempt a range of activities, including:

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

...

3. transactions, including negotiation, concerning deposit and current accounts, payments, transfers, debts, cheques and other negotiable instruments, but excluding debt collection and factoring;

...'

5. In the English and Swedish language versions of the Sixth Directive, the final clause of Article 13B(d)(3) contains an explicit reference to 'factoring' as a service which is excluded from the exemption. The other language versions make no such mention. The French text, for example, refers more generally to 'recouvrement de créances'.

6. By Article 13C(b), Member States may allow taxpayers a right of option for taxation in respect of, *inter alia*, the transactions covered in Article 13B(d).

7. Title XI of the Directive specifies the circumstances in which a taxable person may make deductions from the VAT which he is liable to pay. Article 17(2)(a) provides for the right of a taxable person to deduct the tax due or paid in respect of goods and services supplied or to be supplied to him by another taxable person insofar as they are used for the purposes of his own taxable transactions.

8. The relevant provisions of Community law are implemented in German law by the Umsatzsteuergesetz 1991 (German turnover tax law – 'the UStG'). By paragraph 9 thereof, Germany has chosen to exercise the option provided for by Article 13C(b) of the Sixth Directive.

9. It appears that, in its previous case-law applying the UStG, the Bundesfinanzhof has treated true and quasi factoring differently. Whereas it has regarded the activities comprising quasi factoring as subject to taxation unless falling within an exemption, it has held that true factoring does not constitute an economic activity or the supply of a service and is therefore not taxable.

The facts and questions referred

10. The facts as they appear from the order for reference are as follows.

11. The applicant and respondent on appeal is the successor in title to MKG-Kraftfahrzeuge-Factoring GmbH & Co. KG (MKG). MKG supplied factoring and financing services to MMC-Auto Deutschland GmbH (M-GmbH), a company which imported Mitsubishi vehicles and distributed them via its own dealer network on the German market.

12. In 1991, MKG entered into a contract with M-GmbH. As part of that contract, MKG agreed to purchase certain debts owed to M-GmbH by its dealers in connection with the delivery of vehicles if they were not paid within 150 days of their falling due. In relation to those debts, MKG assumed the risk of loss resulting from default, thereby performing true factoring services. In exchange, it received from M-GmbH factoring and *del credere* fees as well as interest payments on a loan equivalent to the nominal value of the debt less those fees during the 150 day period. In addition, MKG agreed to perform various quasi factoring services for M-GmbH.

13. MKG took the view that the true factoring services which it supplied to M-GmbH were taxable and on that basis sought in its tax declaration for 1991 to deduct tax in respect of goods and services supplied to it.

14. MKG made its tax declaration to the defendant and appellant, the Finanzamt Groß-Gerau (Groß-Gerau Tax Office), which was the competent tax authority. After examining MKG's business, the Finanzamt refused to allow the deduction sought. It took the view, on the basis of the Bundesfinanzhof's previous case-law, that true factoring does not amount to an economic activity or to the supply of a service, and is therefore not taxable.

15. MKG successfully challenged the Finanzamt's decision before the Hessisches Finanzgericht (Finance Court, Hesse). The Finanzgericht held that true factoring was an economic activity and therefore taxable. The Finanzamt appealed against that decision to the Bundesfinanzhof, which made the present order for reference.

16. The Bundesfinanzhof wonders whether it was correct in its previous case-law to hold that true factoring does not constitute a taxable service for the purposes of the Sixth Directive. However, it considers that

there are sufficient doubts as to the proper interpretation of the applicable Community law to merit a reference, and has accordingly referred to the Court the following two questions:

'1. Can a factoring company which buys debts and assumes liability for the risk of loss in relation to those debts be said to be using goods and services received by it for the purposes of its transactions?

2. Do such activities involve taxable transactions or transactions (they involve the latter in any event) for the purposes of Article 13B(d) of [the Sixth Directive] which may be taxed to the extent that the Member States have conferred on taxable persons a right to opt for taxation? Which of the transactions listed in Article 13B(d) of [the Sixth Directive] are involved?'

17. It is clear from the order for reference that by its first question the referring court is in essence seeking to ascertain whether (contrary to its previous case-law) a person who undertakes true factoring can be said to perform an economic activity and therefore to supply a taxable service within the field of application of the Sixth Directive. If so, the purpose of the second question is then to establish whether true factoring none the less falls within one of the exemptions specified by Article 13B(d).

Analysis

18. As regards the first question, the German Government argues that true factoring is not a taxable transaction under the Sixth Directive because it is not an economic activity for the purposes of Article 4 of the Directive, nor does it involve the supply of a service within the meaning of Article 2(1) of the Directive.

19. In support of its claim that true factoring is not an economic activity, the German Government makes reference to the Court's judgment in *Polysar Investments Netherlands*. [3] The Court held in that case that the mere acquisition and holding of shares in a company, in the absence of any direct or indirect involvement in the management of that company, does not amount to an economic activity within the meaning of Article 4 of the Sixth Directive. The holding of shares cannot in itself be said to constitute the exploitation of property for the purpose of obtaining income therefrom on a continuing basis because any dividend yielded is merely the result of ownership of the property. [4]

3 — Case C-60/90 [1991] ECR I-3111, paragraph 17.

4 — Paragraphs 13 and 14 of the judgment. For a discussion of the subsequent case-law of the Court applying the principle established in *Polysar Investment Netherlands*, see the Opinion of Advocate General Léger of 12 September 2002 in Case C-77/01 *EDM*, at footnote 19, and the Opinion of Advocate General Ruiz-Jarabo Colomer of 6 February 2003 in Case C-442/01 *KapHag Renditefonds*, paragraphs 25 to 31, judgment of 26 June 2003 ECR I-6851, I-6853.

20. According to the German Government, the acquisition of debts in a true factoring transaction is exactly equivalent to an acquisition of shares. Each type of transaction is a financial investment in which the investor assumes a risk of loss and in which any returns are merely the consequence of owning the property in question. Following *Polysar*, true factoring is therefore not an economic activity for the purposes of Sixth Directive.

21. The German Government also argues that true factoring is not taxable under the Sixth Directive because the factor does not supply any service within the meaning of Article 2 of the Directive. The only transaction involved is the sale of a debt, in relation to which the factor is the consumer. It refers in that regard to the *Mirror Group* judgment, [5] in which the Court was called upon to determine, *inter alia*, whether a lessee of commercial property supplied taxable services to the lessor by committing to the original lease and by exercising an option to lease additional property, in each case in exchange for consideration. In addressing that question, the Court underlined the general proposition that 'a taxable person who only pays the consideration in cash due in respect of a supply of services, or who undertakes to do so, does not himself make a supply of services for the purposes of Article 2(1) of the Sixth Directive'. [6]

22. I am not persuaded that true factoring falls outside the scope of the Sixth Directive.

23. The Court has on a number of occasions confirmed that Article 4 gives the Sixth Directive a very wide scope, so that it comprises all stages of production, distribution and the provision of services. [7]

24. Moreover, the English and Swedish language versions of Article 13B(d)(3) expressly state that factoring is excluded from the exemption laid down by that provision, and thereby constitutes a taxable transaction. 'Factoring' must surely be read as encompassing true factoring, given the general usage of that word, reflected in the Bundesfinanzhof's choice of terminology. Whilst the other language versions of

5 — Case C-409/98 [2001] ECR I-7175.

6 — At paragraph 26 of the judgment.

7 — Case C-186/89 *Van Tiem* [1990] ECR I-4363, paragraph 17 of the judgment.

Article 13B(d)(3) do not contain any explicit mention of factoring, it has not been suggested that any of them is inconsistent with the English and Swedish texts.

25. In any event, it would in my view ignore the economic reality of true factoring to place it outside the scope of the Sixth Directive. When a factor purchases debts, he provides a service by relieving his client of the risk of default. The client then provides consideration in exchange for the service supplied, normally in the form of a fee or commission. In the case of such a service, by contrast with either the acquisition and holding of shares or the lease of real estate, the vendor of the debt therefore obtains a benefit which is distinguishable from the proceeds of the sale of the property.

26. Support for the proposition that such an activity constitutes a taxable service under the Sixth Directive can be derived from the Court's judgment in *Bally*. [8] The Court held that the issuer of a credit card supplies a service to a trader who accepts the card from its customer in payment for goods or services. That service consists in part in providing a guarantee of payment to the trader for the purchases made. [9] Consideration for the service is supplied by the trader in the form of a commission calculated as a percentage of the purchase price of the goods or services purchased by the customer, which is deducted by the issuer of the card from the amount paid over to the trader. [10]

27. As the Commission and MKG submit, a true factoring transaction is very similar in nature to the service performed by the issuer of a credit card. A factor serves to guarantee payment of his client's debts by assuming the risk of default. In exchange, the client supplies consideration in the form of a fee which is usually deducted from the purchase price of the debt.

28. I am therefore of the opinion that true factoring constitutes a taxable service for the purposes of the Sixth VAT Directive.

29. As regards the second question referred, the German Government maintains that, if true factoring is a taxable service, it constitutes a 'transaction concerning debts' within the meaning of Article 13B(d)(3), and therefore falls within the exemption laid down by that provision. MKG submits that true factoring is

8 — Case C-18/92 *Bally* [1993] ECR I-2871.

9 — Paragraph 9 of the judgment.

10 — Paragraph 11 of the judgment.

excluded from the exemption by the final clause of Article 13B(d)(3).

30. The Commission questions whether an answer to the second question is in fact necessary to enable the referring court to resolve the dispute which is before it. Given that Germany has elected to allow taxpayers to opt to pay tax on transactions otherwise exempt by reason of Article 13B(d)(3), it would not appear to matter whether true factoring is understood to fall within the exemption set out in Article 13B(d)(3) or within the exclusion from that exemption.

31. Despite its reservations regarding the second question referred, the Commission none the less proceeds to offer submissions on the status under Article 13B(d) of both true and quasi factoring, both of which it regards as falling within the exclusion from the exemption.

32. In my view, since the Bundesfinanzhof considers that a response to the second question referred is necessary for it to give judgment in the proceedings before it, it is appropriate for the Court to address it. However, it appears to me that the second question relates only to true factoring transactions, such being the 'activities' which form the subject of the first question. Accordingly, I shall consider only the status of true factoring under Article 13B(d).

33. The explicit reference to factoring in the English and Swedish language versions of the final clause of Article 13B(d)(3) provides strong support for the conclusion that true factoring falls within the exclusion to the exemption laid down by that provision, especially given that the more general formulations of the exclusion adopted in the other language versions would not appear to be incompatible with an interpretation which encompassed true factoring.

34. Nor has the German Government advanced any argument as to why factoring should be deemed to fall within the exemption to Article 13B(d)(3). Its references to the legislative history of the Directive are to my mind inconclusive, suggesting merely that the appropriate classification of factoring was not an issue which gave rise to debate in the Council.

35. It therefore seems to me that true factoring is placed outside the exemption contained in Article 13B(d)(3) by reason of the exclusion contained in the final clause of that provision.

Conclusion

36. Accordingly, I am of the opinion that the Court should answer the questions submitted for preliminary ruling as follows:

(1) on a proper construction 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 — a factoring company acts as a taxable person when it buys debts and assumes liability for the risk of loss in relation to those debts and may accordingly deduct from the tax which it is liable to pay tax which it has paid in respect of goods and services supplied to it for the purposes of its taxable transactions;

(2) such an activity constitutes 'debt collection and factoring' within the meaning of Article 13B(d)(3) of the Directive and is therefore excluded from the exemption laid down by that provision.