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DIRECTORATE-GENERAL
TAXATION AND CUSTOMS UNION
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Value added tax

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VALUE ADDED TAX COMMITTEE
(ARTICLE 398 OF DIRECTIVE 2006/112/EC)
WORKING PAPER NO 786

QUESTION
CONCERNING THE APPLICATION OF EU VAT PROVISIONS

ORIGIN:	**Spain**
REFERENCES:	**Articles 9 and 10**
SUBJECT:	**Services provided to companies by their shareholders**

1. INTRODUCTION

The Spanish delegation has asked the opinion of the VAT Committee on whether professional services provided by a natural person to a company under an employment contract should be qualified as an economic activity, within the meaning of Articles 9 and 10 of the VAT Directive[1], when that natural person owns the majority of the capital of that company, which supplies the same type of services as those provided by the shareholder under the employment contract.

The question submitted by the Spanish delegation is attached in annex.

2. SUBJECT MATTER

Article 9(1) of the VAT Directive states that "'*taxable person' shall mean any person who, independently, carries out in any place any economic activity, whatever the purpose or results of that activity*", adding that "*any activity of producers, traders or persons supplying services, including mining and agricultural activities and activities of the professions, shall be regarded as 'economic activity'*".

On its part, Article 10 of the VAT Directive states that "*the condition in Article 9(1) that the economic activity be conducted 'independently' shall exclude employed and other persons from VAT 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*".

Therefore, activities of the professions are regarded as economic activity, according to Article 9(1) of the VAT Directive. However, to be considered a taxable person, the professional who carries out that economic activity, must do it independently.

In the case submitted by the Spanish authorities, the professional supplies his services under an employment contract to a company which provides the same type of services to its clients.

According to Article 10 of the VAT Directive, the existence of a contract of employment, in principle, would imply that the activity deployed is not carried out independently, so the person who performs that activity would not be considered a taxable person.

However, the Spanish authorities allege that problems arise when the professional providing services to the company directly or indirectly owns a majority, or all, of the capital of the company. In such cases there is a risk that the dependence and employee status could be undermined, given that this shareholder participates in the company decision-making. In addition, Spanish employment law excludes the possibility of the existence of an employment relationship when, in the case of trading companies, the

[1] Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ L 347, 11.12.2006, p. 1).

professionals providing services to a company have a direct shareholding in the company of 50% or more.

It is also alleged that in the case of professional services the main means of production lies in the shareholder himself, as those services are of a strictly personal nature and that the material means made available by the company for the provision of these services are of scant significance compared with the human factor. The shareholder arranges the economic activity himself, where necessary, even if this simply entails making himself available to provide the services.

Thus, we need to determine whether these professional services supplied to a company by a shareholder who controls the majority of the capital of that company, when those services are of the same type as those supplied by the company itself, can or cannot be considered to be an activity carried out "dependently".

3. THE COMMISSION'S OPINION

Although under Spanish law, the existence of an employment relationship is not possible when the professional who provides services to a company has a direct shareholding in the company of 50% or more, this is not relevant for the qualification of the activity for VAT purposes. Article 10 of the VAT Directive excludes the notion of independence when the person is 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***".

Therefore, we have to look at the conditions under which the services are provided by the professional to the company, to assess if the notion of dependency is present or not.

That the professional is the majority shareholder of the company does not in itself impede the existence of a relationship employer-employee. The Court of Justice of the European Union (CJEU) ruled in case C-355/06 *Van der Steen*[2] that "*a natural person carrying out all work in the name and on behalf of a company that is a taxable person pursuant to a contract of employment binding him to that company of which he is also the sole shareholder, the sole manager and the sole member of staff, is not himself a taxable person within the meaning of Article 4(1) of that Directive* (the Sixth Directive)".

The CJEU based its conclusions on the following four factors:

- contracts for the provision of services were entered into by the company,
- that the shareholder acted on behalf and under the responsibility of the company,
- that the shareholder did not bear any economic business risk in acting as manager and performing the work in the course of the company's dealings with third parties, and finally,

[2] CJEU, judgment of 18 October 2007 in case C-335/06, *J.A. van der Steen*.

- that the company paid the shareholder a fixed monthly salary and annual holiday payment, deducting income tax and social security contributions from his salary, so the shareholder depended on the company to determine his remuneration.

Therefore, in the view of the CJEU, the majority shareholder of a company can conclude an employment contract with that company.

Moreover, it is irrelevant to the relationship between them that the services supplied by the company are of the same nature as those supplied by the shareholder to the company. Otherwise, that would imply that none of the professionals, whether shareholders or not, working for a company which provides the same type of services could be considered employees but would have to be regarded as taxable persons.

Thus, we have to analyse the elements to which Article 10 of the VAT Directive refers, such as working conditions, remuneration and liability, to determine whether the services are supplied by the shareholder dependently or independently.

This is consistent with the ruling of the CJEU in case C-202/90 *Ayuntamiento de Sevilla*[3]. The case referred to whether the tax collectors working for the City Council carried out an economic activity. There was no contract of employment, so the CJEU considered whether their legal relationship with the Commune created the relationship of employer and employee as regards working conditions, remuneration and the employer's liability.

Regarding the working conditions, the tax collectors themselves procured and organised independently, within the limits laid down by the law, the staff, equipment and materials necessary for them to carry out their activities.

With regard to remuneration, tax collectors bore the economic risk entailed in their activity as their profit depended on the amounts collected and the expenses incurred for staff and equipment.

Regarding the employer's liability, that the City Council could be held liable for the activity of tax collectors was not considered sufficient to establish the existence of a relationship of employer and employee.

For those reasons, the CJEU concluded that the activity of the tax collectors was being carried out independently.

For the Commission services, the fact that the shareholder owns the majority of the capital of the company, and that he provides to the company the same services that the company supplies to its clients, are not by themselves decisive to determine whether the activity is being carried out independently. However, where a professional, who is already a taxable person for VAT proposes:

- supplies his services to the company under an employment contract, and

- undertakes this in the same fashion and means as applied in his economic activity as a taxable person,

[3] CJEU, judgment of 25 July 1991 in case C-202/90, *Ayuntamiento de Sevilla*.

then it could be considered that the services supplied to the company under such an employment contract are carried out independently, notwithstanding the employment contract.

Therefore, to determine whether in these situations there is a dependent or an independent relationship, it is necessary to perform a case-by-case analysis similar to the one of the CJEU in the *Ayuntamiento de Sevilla* case, examining all circumstances of the case.

Thus, elements such as

- whether the shareholder uses the means of the company to provide the services or different means, or
- whether he receives a fixed remuneration plus commission and bonuses or the remuneration is a percentage of the profits or the amounts invoiced to the clients, or
- whether he has personal responsibility for his work towards the clients,

all have to be weighed in order to qualify the relationship between the shareholder and the company as dependent or independent.

It should be mentioned at this point that the VAT Committee already in 2012 discussed the conditions to be met for an activity to be regarded as an economic activity within the meaning of the VAT Directive[4]. That however was before the most recent decision of the CJEU in case C-62/12 *Kostov*[5]. In its working paper, the Commission services had considered that when a member of the board who is a taxable person, was only on the board because he owned shares and not because he had been appointed to the board in his professional capacity, then that would be an activity carried out on an occasional basis and therefore outside the scope of VAT, unless the Member State had availed itself of the option provided for in Article 12(1) of the VAT Directive. With the recent CJEU decision in the *Kostov* case, it would appear that in that respect the conclusion reached in that working paper has been overruled.

In conclusion, a natural person who owns the majority of the shares of a company can be bound to that company by an employment contract. The qualification of the relationship of the shareholder with the company as dependent or independent has to be done on a case-by-case basis, analysing the elements to which Article 10 of the VAT Directive refers such as working conditions, remuneration and liability. Where that shareholder is already a taxable person for VAT purposes, the services supplied to his company under an employment contract could be considered carried out independently in cases where there is no difference in the means used by that shareholder when supplying services to third parties as a taxable person, and those used when supplying services under the employment contract to the company where he is the majority shareholder.

4 See Working paper No 731.
5 CJEU, judgment of 13 June 2013 in case C-62/12, *Galin Kostov*.

4. DELEGATIONS' OPINION

Delegations are invited to express their views on the matters raised by the Spanish authorities and the observations made by the Commission.

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ANNEX

Question from Spain

The Spanish Ministry of Finance and Public Administrations would like the VAT Committee's opinion on the interpretation and practical application of Articles 9 and 10 of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax, in particular as regards whether professionals who are shareholders of companies whose company objective is to provide professional services (legal, consultancy, architecture, engineering, etc.) are deemed to be taxable persons in respect of services provided by them to these firms that come under the company's objectives.

Articles 9(1) and 10 of Directive 2006/112/EC were transposed into Spanish law chiefly by Articles 4(1), 5, 7(5) and 11(2)(1) of VAT Law 37/1992 of 28 December 1992.

Article 11(2)(1) of Law 37/1992 states that, in particular, the provision of services is deemed for VAT purposes to be '*the independent pursuit of a profession, an artistic activity or a trade*'.

Under Spanish administrative law, services provided by a shareholder in the company are not subject to VAT if they are provided by an employee in the context of a dependent employment relationship. The Spanish Supreme Court's position concerning the existence of this employment relationship in judgments handed down on 9 December 2004 and 7 November 2007 can be summarised as follows:

– The classification of contracts depends not on how they have been designated by the contracting parties, but on the actual nature of the obligations undertaken in the contract and the services that are the subject of the contract.

– When, in addition to the general requirements of work and remuneration, the work performed meets the specific requirements of work by an employee carried out in a dependent relationship, the relationship must be formalised by an employment contract.

– Both dependence and work as an employee are fairly abstract concepts. Thus, in resolving legal disputes, in order to determine whether an employment contract exists, the existence of these two requirements is verified. In legal interpretations, the most habitual common evidence of dependence is the worker's presence at the employer's workplace or at the workplace designated by the employer and the application of specific working hours. Other factors are the personal performance of the work, the inclusion of the worker in the organisation of the work by the employer or entrepreneur who programmes his activity or, conversely, the absence of any entrepreneurial organisation by the worker himself.

Common circumstantial evidence that the worker is an employee rather than self-employed includes the following: the worker delivers or makes available to the entrepreneur the products manufactured or the services provided; the entrepreneur, rather than the worker, makes decisions on market relations or relations with the public, for example setting prices or rates, selecting customers, indicating the persons to be catered for; whether the remuneration for the work is fixed or periodic; calculation of the

remuneration or of the main components thereof that is proportional to the activity performed, without the risk or the profit element characterising the remuneration of entrepreneurs or of services provided by professionals.

Consequently, when there is sufficient evidence of dependence and of employee status in the shareholder's relationship with the company to which he provides services, we can conclude that the shareholder does not carry out an independent economic activity and is therefore not taxable for VAT purposes.

The problem arises when the professional shareholder providing services to the company directly or indirectly owns a majority, or all, of the share capital of the company. In these cases, dependence and employee status appear to be very diluted, since ultimately the shareholder participates in company decision-making.

Spanish employment law excludes the possibility of the existence of an employment relationship when, in the case of trading companies, the professionals providing services to the company have a direct shareholding in it of 50 % or more.

In addition, in the case of professional services, the main means of production lies in the shareholder himself (lawyer, consultant, architect, engineer, etc.), i.e. in the professional qualification of the individual providing the services. This is providing that the services are of a strictly personal nature and that the material means made available by the company for provision of these services are of scant significance compared with the human factor. This may mean that the shareholder arranges the means of production himself, where necessary, even if this simply entails making himself available to provide the services.

In view of the above, the question that arises is whether the professional services provided by a shareholder under an employment contract to his company, where the company objective is to provide this type of services, and where **the shareholder has a majority shareholding** in the company as indicated above, may be deemed to be provided in the course of carrying out an economic activity within the meaning of Directive 2006/112/EC or whether they should be deemed to be outside the scope of that Directive.