MALTA
INSTITUTE
OF TAXATION

Position Paper 02/2020

Decision of the CJEU in Case C-94/19 *San Domenico Vetraria SpA v Agenzia delle Entrate* and the VAT treatment of reimbursement of employee costs

October 2020

This Position Paper sets out the MIT's views on the CJEU Decision in Case C-94/19 and, in particular, on the implications, if any, on the local practice concerning the sharing of staff by companies forming part of a corporate group.

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1. Case C-94/19

*In its **judgement** in case C-94/19, the CJEU essentially confirmed that the lending or secondment of staff by a parent company to its subsidiary, carried out in return for the mere reimbursement of the related costs, generally constitutes a (taxable) supply for consideration falling within the scope of VAT.*

The case concerned the secondment of an employee by one company, Avir, to a subsidiary, San Domenico Vetraria. Avir invoiced San Domenico Vetraria for amounts corresponding to the costs incurred for the seconded employee. San Domenico Vetraria applied VAT to the amount reimbursed and then exercised its right to deduct that VAT. The tax authorities took the view that those reimbursements fell outside the scope of VAT since they did not concern supplies of services between the parent and its subsidiary, and denied San Domenico Vetraria's input tax claim. The Italian Court acknowledged that in terms of Italian VAT legislation (Article 8(35) of Law No 67/88), in the case of the secondment of staff by one company to another, where the sum reimbursed corresponds to the amount of costs incurred for the seconded staff, the secondment is not taxable, since it falls outside the scope of VAT. However, the Italian Court expressed doubt as to whether the secondment of staff should fall outside the scope of VAT and referred the matter to the CJEU, asking whether national legislation under which the lending or secondment of staff by a parent company in respect of which the subsidiary merely reimburses the related costs is regarded as irrelevant for VAT purposes is contrary to the VAT Directive and the principle of fiscal neutrality.

The CJEU found that the secondment was carried out on the basis of a legal relationship of a contractual nature between Avir and San Domenico Vetraria, in the context of which there was reciprocal performance, namely the secondment of an employee (a Director) from Avir to San Domenico Vetraria, on the one hand, and the payment by San Domenico Vetraria to Avir of the amounts invoiced to it, on the other. It furthermore maintained that if it were to be established (which it held was for the referring court to ascertain) that the payment by San Domenico Vetraria of the amounts invoiced to it by its parent company was a condition for the latter to second the director, and that the subsidiary paid those amounts only in return for the secondment, it would have to be held that there is a direct link between the two services. On this basis, the court held that the transaction should be regarded as having been carried out for consideration and subject to VAT, maintaining that the amount of the consideration, in particular the fact that it is equal to, greater or less than, the costs which the taxable person incurred in providing his service, is irrelevant.

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2. MIT comments

The Indirect Tax Committee of the MIT has considered the above decision in the context of the interpretation and practice which we understand applies locally, where companies forming part of the same corporate group effectively share staff and the employment costs relating thereto. On the basis of the below analysis, we are of the view that the CJEU's decision in the San Domenico Vetraria Case should not, of itself, impact the Malta VAT treatment of the reimbursement of employee costs in the circumstances as below-described.

At the outset it is acknowledged that Maltese VAT legislation does not contain a provision equivalent to Article 8(35) of Italian Law No 67/88 which was addressed in the San Domenico Vetraria case, in terms of which secondments were regarded as outside the scope of Italian VAT if made on a cost basis.

However, the decision of the CJEU in this case has been considered in the context of the practice which is understood is adopted in Maltese corporate group structures, where one entity within the corporate group acts as the formal employer of an employee (for employment law and payroll purposes) – typically for administrative simplification reasons – when the said employee exercises his/her employment duties in favour of not merely (if indeed at all) the formal employer but also other related entities forming part of the same corporate group.

In such a scenario, from a cost accounting perspective, the relevant group companies would typically bear their respective portion of the employee costs, which should generally be based on a fair allocation of those employee costs under some form of cost-sharing arrangement (based, for example, on records of actual time spent by the employee in exercising employee duties for the relevant related entities).

From a Malta VAT perspective, we understand that in such a scenario, *where staff are in effect jointly employed by two or more companies forming part of the same corporate group* (even though for employment law and income tax purposes, only one of the companies is identified as the formal employer, and is the person responsible for the withholding of taxes under the FSS), the said 'sharing' of staff is not regarded as giving rise to a supply of services for Malta VAT purposes, and the reimbursement of employee costs (to the extent that the employee costs are being shared on a pure cost basis i.e. with no form of mark-up or other additional charge whatsoever), would not give rise to a Malta VAT liability.

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The activities of an employee do not constitute an economic activity for VAT purposes in terms of Article 5(2) of the Value Added Tax Act, chapter 406 of the laws of Malta (the '**VAT Act**'). By virtue of Article 5(5) of the VAT Act, an "employee" is defined *an individual bound to an employer by a contract of employment or by other legal ties creating the relationship of employer and employee as regards working conditions, remuneration and the employee's liability* (and includes the holder of an office).

In our view, this categorisation of the activities of an employee would apply whether the employee is engaged to perform duties for one employer, or for more than one.

An arrangement such as the above-mentioned involving multiple employer companies would, in our view, fall within the parameters of a non-economic activity for Malta VAT purposes (and therefore outside the scope of VAT), in so far as the related entities which benefit from the employee's activities and which therefore bear their corresponding share of the pure employee costs **are in effect joint employers of the employee,** typically evidenced by their being party to the contract of employment (or equivalent legal ties). In other words, whilst the contract of employment would identify one formal / official employer as a Principal Employer (e.g. for employment law registration and payroll purposes), the other group companies for which the employee exercises employment duties in favour would also be party to the contract of employment; therefore, the legal ties creating the relationship of employer and employee shall subsist also vis-à-vis those entities for the purposes of article 5 of the VAT Act. Of course it is recognised that regard should be had to any relevant employment law considerations.[1] In such a scenario (i.e. where an individual is engaged to perform duties for more than one company within a corporate group, and the responsibility for the payment of wages is attributed to the primary employer for employment law purposes or the so-called 'Paymaster', the mere recovery of the relevant proportion of that cost from the other group companies which have also engaged the employee would not constitute consideration for a supply of services, but would in effect constitute a reimbursement of amounts disbursed by the primary employer on behalf of the other employer companies, which reimbursement would fall outside the scope of VAT.

On the other hand, any amount received by the primary employer/paymaster over and above the amounts being reimbursed could, in our view, constitute consideration for services being carried out by the primary employer/paymaster in fulfilling its role and administering the wages etc. Of course, each scenario would have to be considered on a case-by-case basis.

[1] We understand that local employment law does not preclude multiple employers on a single employment contract, subject to the assumption of the relevant obligations (including registration) by the identified 'primary' employer. However this is a matter to be confirmed by legal counsel competent to advise on Maltese employment law.

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The above views relate specifically to the scenario in which all the companies involved are in fact employers of the employee. On the other hand, and in line with the *San Domenico Vetraria* CJEU judgment, the lending or secondment of staff for consideration (whether on a pure cost reimbursement basis or otherwise) between related entities, where one of the entities is the contractual employer of the employee and makes the said employee available to one or more other entities within the same corporate group (which entities constitute separate taxable persons for VAT purposes) in principle is, and remains, a (taxable) supply falling within the scope of VAT.

Note: The above refers to arrangements between companies forming part of the same corporate group and not to companies forming part of a VAT Group for the purposes of the Value Added Tax (Registration as a Single Taxable Person) Regulations, 2018.

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