

Case C-288/07

Commissioners of Her Majesty's Revenue and Customs

v

Isle of Wight Council and Others

(Reference for a preliminary ruling from the High Court of Justice of England and Wales (Chancery Division))

(Sixth VAT Directive – Article 4(5) – Activities engaged in by bodies governed by public law – Provision of off-street car-parking facilities for which a charge is made – Distortions of competition – Meaning of 'would lead to' and 'significant')

Summary of the Judgment

1. *Tax provisions – Harmonisation of laws – Turnover taxes – Common system of value added tax – Taxable persons – Bodies governed by public law*

(Council Directive 77/388, Art. 4(5), second subpara.)

2. *Tax provisions – Harmonisation of laws – Turnover taxes – Common system of value added tax – Taxable persons – Bodies governed by public law*

(Council Directive 77/388, Art. 4(5), second subpara.)

3. *Tax provisions – Harmonisation of laws – Turnover taxes – Common system of value added tax – Taxable persons – Bodies governed by public law*

(Council Directive 77/388, Art. 4(5), second subpara.)

1. The second subparagraph of Article 4(5) of Sixth Directive 77/388 on the harmonisation of the laws of the Member States relating to turnover taxes is to be interpreted as meaning that the significant distortions of competition, to which the treatment as non-taxable persons of bodies governed by public law acting as public authorities would lead, must be evaluated by reference to the activity in question, as such, without such evaluation relating to any local market in particular.

A body governed by public law may be responsible, under national law, for carrying on certain activities of an essentially economic nature under the special legal regime applicable to them where those same activities can also be carried on in parallel by private operators, with the result that the treatment of that body as a non-taxable person in respect of value added tax may give rise to certain distortions of competition.

The third subparagraph of Article 4(5) of the Sixth Directive is intended to avoid that undesirable result by providing that the activities specifically listed in Annex D to that directive are, 'in any event', unless they are negligible, to be subject to value added tax, even when they are carried on by bodies governed by public law acting as public authorities. In other words, the treatment of bodies governed by public law as non-taxable persons in respect of value added tax and those activities is, unless such activities are negligible, presumed to lead to distortions of competition. It is thus clear from the third subparagraph of Article 4(5) of the Sixth Directive that the treatment of

those bodies as taxable persons in respect of that tax results from the carrying-on, as such, of the activities listed in Annex D to that directive, irrespective of the question whether or not a particular body governed by public law faces competition at the level of the local market on which it carries on those same activities.

Furthermore, there may exist, on the national level, other activities of an essentially economic nature, not listed in Annex D to the Sixth Directive, the list of which may vary from one Member State to another or from one economic sector to another, which are carried on in parallel both by bodies governed by public law in their capacity as public authorities and by private operators. It is precisely to those activities that the second subparagraph of Article 4(5) of the Sixth Directive applies, in providing that bodies governed by public law, even when they act as public authorities, are to be considered taxable persons where their treatment as non-taxable persons would lead to significant distortions of competition.

The second and the third subparagraphs of Article 4(5) of the Sixth Directive are, consequently, closely linked since they pursue the same objective, namely the treatment of bodies governed by public law as taxable persons in respect of value added tax, even when they are acting as public authorities. Those subparagraphs are thus subject to the same logic, by which the Community legislature intended to limit the scope of the treatment of bodies governed by public law as non-taxable persons, so that the general rule stated in Articles 2(1) and 4(1) and (2) of that directive, under which any activity of an economic nature is, in principle, to be subject to value added tax, is observed. Consequently, the second and third subparagraphs of Article 4(5) of the Sixth Directive are to be interpreted as a whole. It follows that the treatment of bodies governed by public law as taxable persons in respect of value added tax, either on the basis of the second subparagraph of Article 4(5) of the Sixth Directive, or on that of the third subparagraph of that provision, results from the carrying-on, as such, of a given activity, irrespective of whether or not those bodies face competition at the level of the local market on which they engage in that activity.

Compliance with the principle of fiscal neutrality is thus ensured, given that all bodies governed by public law are, for the purposes of value added tax, either taxable or non-taxable persons, the sole strain on that principle concerning only relations between those bodies and private operators, and that to the extent that the distortions of competition remain insignificant. The evaluation of the existence of distortions of competition having regard to each of the local markets on which the local authorities offer off-street parking assumes a systematic re-evaluation, on the basis of often complex economic analyses, of the conditions of competition on a multitude of local markets, the determination of which may prove particularly difficult since the markets' demarcation does not necessarily coincide with the areas over which the local authorities exercise their powers. In that case, neither the local authorities nor the private operators would be in a position to provide, with the required certainty, for the conduct of their affairs if, on a given local market, the activity carried on by the local authorities will or will not be subject to value added tax, which would be likely to jeopardise the principles of fiscal neutrality and legal certainty.

(see paras 33-41, 46, 49, 51-53, operative part 1)

2. The expression 'would lead to' is, for the purposes of the second subparagraph of Article 4(5) of Sixth Directive 77/388 on the harmonisation of the laws of the Member States relating to turnover taxes, to be interpreted as encompassing not only actual competition, but also potential competition, provided that the possibility of a private operator entering the relevant market is real, and not purely hypothetical.

Indeed, the treatment of bodies governed by public law as non-taxable persons in respect of value added tax under the first subparagraph of Article 4(5) of the Sixth Directive constitutes a derogation from the general rule that any activity of an economic nature be subjected to value

added tax. That provision must, therefore, be interpreted strictly. But the second subparagraph of Article 4(5) restores that general rule in order to avoid such treatment of those bodies leading to significant distortions of competition. The latter provision cannot therefore be construed narrowly.

However, the purely theoretical possibility of a private operator entering the relevant market, which is not borne out by any matter of fact, or by any objective evidence or by any analysis of the market, cannot be assimilated to the existence of potential competition. To make such an assimilation, that possibility must be real, and not purely hypothetical.

(see paras 60, 64-65, operative part 2)

3. The word 'significant' is, for the purposes of the second subparagraph of Article 4(5) of Sixth Directive 77/388 on the harmonisation of the laws of the Member States relating to turnover taxes, to be understood as meaning that the actual or potential distortions of competition must be more than negligible.

Indeed, that word is to be understood as intended to restrict the scope of the treatment, under the first subparagraph of Article 4(5) of the Sixth Directive, of bodies governed by public law as non-taxable persons for those activities. If that word had to be understood as meaning 'material', or even 'exceptional', the scope of the treatment of bodies governed by public law as non-taxable persons would be unduly enlarged. On the other hand, if their treatment as such were allowed only in cases where it would lead only to negligible competition, that scope would be circumscribed effectively.

Also, it is clear from the third subparagraph of Article 4(5) of the Sixth Directive that the treatment of bodies governed by public law as non-taxable persons in respect of value added tax for the activities listed in Annex D thereto is permitted provided that those activities are negligible, assuming thus that the distortions of competition which would result would also be negligible. Since the second and third subparagraphs of Article 4(5) of the Sixth Directive are closely linked, as they pursue the same objective and are subject to the same logic, the word 'significant' is to be understood as meaning that the treatment of public bodies as non-taxable persons can be permitted only in cases where it would lead only to negligible distortions of competition.

Finally, the treatment of those bodies as non-taxable persons in circumstances where it would not lead to any distortion of competition or lead only to negligible distortions would bring about the least possible damage to the principle of fiscal neutrality.

(see paras 72-76, 78-79, operative part 3)

JUDGMENT OF THE COURT (Grand Chamber)

16 September 2008 (*)

(Sixth VAT Directive – Article 4(5) – Activities engaged in by bodies governed by public law – Provision of off-street car-parking facilities for which a charge is made – Distortions of competition – Meaning of 'would lead to' and 'significant')

In Case C-288/07,

REFERENCE for a preliminary ruling under Article 234 EC from the Chancery Division of the High Court of Justice of England and Wales (United Kingdom), made by decision of 6 March 2007, received at the Court on 14 June 2007, in the proceedings

The Commissioners of Her Majesty's Revenue & Customs

v

Isle of Wight Council,

Mid-Suffolk District Council,

South Tyneside Metropolitan Borough Council,

West Berkshire District Council,

THE COURT (Grand Chamber),

composed of V. Skouris, President, P. Jann, C.W.A. Timmermans, A. Rosas and K. Lenaerts, Presidents of Chambers, G. Arestis, U. Lõhmus, A. Borg Barthet, M. Ilešič, J. Malenovský, E. Levits, A. Ó Caoimh and A. Arabadjiev (Rapporteur), Judges,

Advocate General: M. Poiares Maduro,

Registrar: C. Strömholm, Administrator,

having regard to the written procedure and further to the hearing on 1 April 2008,

after considering the observations submitted on behalf of:

- the Isle of Wight Council, Mid-Suffolk District Council, South Tyneside Metropolitan Borough Council and West Berkshire District Council, by J. Ghosh QC, J. Henderson, Barrister, R. Genn, Solicitor, and L. Leach, adviser,
- the Government of the United Kingdom of Great Britain and Northern Ireland by Z. Bryanston-Cross, acting as Agent, and by C. Vajda QC and B. Rayment, Barrister,
- Ireland, by D. O'Hagan, acting as Agent, assisted by A. Aston SC, and N. Travers, BL,
- the Italian Government, by I.M. Braguglia, acting as Agent, assisted by G. De Bellis, avvocato dello Stato,
- the Commission of the European Communities, by R. Lyal and M. Afonso, acting as Agents,

after hearing the Opinion of the Advocate General at the sitting on 12 June 2008,

gives the following

Judgment

1 This reference for a preliminary ruling concerns the interpretation of the second subparagraph of Article 4(5) of 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; 'the Sixth Directive').

2 The reference was made in the course of proceedings between the Commissioners of Her Majesty's Revenue & Customs ('the Commissioners') and four local authorities, namely the Isle of Wight Council, Mid-Suffolk District Council, South Tyneside Metropolitan Borough Council and West Berkshire District Council (hereinafter, together, 'the local authorities concerned'), regarding their treatment as taxable persons for the purposes of value added tax ('VAT') on the provision of off-street car-parking facilities ('off-street parking').

Legal context

3 Article 2 of the Sixth Directive, in Title II thereof, entitled 'Scope', 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;

...'

4 Article 4 of the Sixth Directive, in Title IV thereof, entitled 'Taxable Persons', states:

'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 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.

...

5. States, regional and local government authorities and other bodies governed by public law shall not be considered taxable persons in respect of the activities or transactions in which they engage as public authorities, even where they collect dues, fees, contributions or payments in connection with these activities or transactions.

However, when they engage in such activities or transactions, they shall be considered taxable persons in respect of these activities or transactions where treatment as non-taxable persons would lead to significant distortions of competition.

In any case, these bodies shall be considered taxable persons in relation to the activities listed in Annex D, provided they are not carried out on such a small scale as to be negligible.

Member States may consider activities of these bodies which are exempt under Article 13 or 28 as activities which they engage in as public authorities.'

5 Annex D to the Sixth Directive, to which the third subparagraph of Article 4(5) of the Sixth Directive refers, lists 13 types of activities. However, the provision of off-street parking is not among them.

6 Article 4(5) of the Sixth Directive, the direct effect of which was recognised by the Court in Joined Cases 231/87 and 129/88 *Comune di Carpaneto Piacentino and Others* [1989] ECR 3233, paragraph 33, has not been transposed into the law of the United Kingdom.

The dispute in the main proceedings and the questions referred for a preliminary ruling

7 The local authorities concerned provide off-street car-parking facilities. The private sector also provides like facilities.

8 Historically, the local authorities in the United Kingdom accepted that they were accountable for VAT on their revenue from the provision of off-street parking. However, following the decision in Case C-446/98 *Fazenda Pública* [2000] ECR I-11435, some 127 local authorities made claims for repayment of the VAT they had previously paid, taking the view by reason of the first subparagraph of Article 4(5) of the Sixth Directive that they should not have been accountable for that VAT. The total of the claims made for repayment amounts to GBP 129 million. As regards the total sum which could be reclaimed, it is stated in the order for reference that there are some 468 local authorities in the United Kingdom of Great Britain and Northern Ireland.

9 In the cases in the main proceedings, the claims amount to GBP 1.6 million. The referring court indicates that these cases are test cases as the local authorities concerned form a representative cross-section of all local authorities. The Isle of Wight Council, Mid-Suffolk District Council, South Tyneside Metropolitan Borough Council and West Berkshire District Council administer, respectively, an island, a rural area, an urban area and a provincial region.

10 Since the local authorities concerned concluded that under a correct interpretation of Community law they were not subject to VAT for the activities in question, they claimed repayment of the VAT previously paid. However, the Commissioners refused such repayment. Consequently, those local authorities appealed against the Commissioners' decision to the VAT and Duties Tribunal, London. Having held that the question of the exemption from VAT of bodies governed by public law on the basis of the second subparagraph of Article 4(5) of the Sixth Directive must be dealt with separately for each of the local authorities concerned, that is on a 'taxable person by taxable person' basis, the VAT and Duties Tribunal, London, concluded that the exemption of those authorities from VAT did not lead to significant distortions of competition. Each of those authorities was thus exempt from VAT in respect of its revenue from the provision of off-street parking.

11 The Commissioners appealed against the decision of the VAT and Duties Tribunal, London, to the Chancery Division of the High Court of Justice of England and Wales. Their principal argument is that Article 4(5) of the Sixth Directive is of national scope which requires that there should be an investigation of the nationwide impact on the private sector generally of the exemption of local authorities from VAT on the provision of off-street parking. Their appeal also concerns the meaning of the words 'would lead to' and 'significant' in the passage comprised of the words 'where treatment as non-taxable persons would lead to significant distortions of competition' in the second subparagraph of Article 4(5) of the Sixth Directive.

12 In those circumstances the Chancery Division of the High Court of Justice of England and Wales decided to stay the proceedings and to refer the following questions to the Court of Justice for a preliminary ruling:

'1. Is the expression "distortions of competition" to be ascertained on a public body by public body basis such that, in the context of the present case, it should be determined by reference to the area or areas where the particular body in question provides off-street parking or by reference

to the totality of the national territory of the Member State?

2. What is meant by the expression “would lead to”? In particular, what degree of probability or level of certainty is required for that condition to be satisfied?

3. What is meant by the word “significant”? In particular, does “significant” mean an effect on competition that is more than trivial or *de minimis*, a “material” effect or an “exceptional” effect?

The questions referred for a preliminary ruling

The first question

Observations submitted to the Court

13 The local authorities concerned submit that the expression ‘distortions of competition’ is properly to be ascertained on a public body by public body basis, such that, in the context of the present case, it should be interpreted by reference to the area or areas where the particular body in question provides off-street parking and not by reference to a hypothetical market which encompasses the totality of the national territory of any particular Member State. A contrary approach would be inconsistent with the very concept of ‘competition’. The VAT exemption conferred on each of those authorities does not lead in any way to distortions of competition in relation to private providers or local authorities in, for example, Glasgow, let alone to ‘significant’ distortions. Similarly, a person who wished to shop on the Isle of Wight would not park his vehicle in Manchester.

14 The United Kingdom Government, relying especially on the fundamental principles of fiscal neutrality and legal certainty, submits that as a matter of principle, ‘the activities’ approach, that is taking account of the entire national market and not of each local market, is the most sensible approach to the interpretation of the second subparagraph of Article 4(5). The local nature of demand means that even in an area within a given local authority, several local markets could exist in some of which there might be competition, while there might be no competition in others.

15 In Ireland’s submission, it is clear from the Court’s case-law that the Member States are free to choose the appropriate method for transposing the second and third subparagraphs of Article 4(5) of the Sixth Directive into national law. It is for each Member State to determine the activities engaged in by the State or public entities which, if not subjected to VAT, would lead to significant distortions of competition. The Member States may, thus, adopt local, regional or nationwide approaches.

16 The Italian Government suggests that principles specific to the field of competition be applied. In that regard, it refers to the Commission’s Notice on the definition of relevant market for the purposes of Community competition law (OJ 1997 C 372, p. 5) and concludes, on that basis, that the relevant geographic market cannot be the entire national market. In matters of off-street parking there cannot be any conceivable competition between the parking facilities offered by different towns.

17 The Commission of the European Communities takes the view that it is the nature of the activity, and not the local conditions of competition, that has to be taken into account to assess the likelihood of distortions of competition. That such an approach is correct may be inferred from the fact that the third subparagraph of Article 4(5) of the Sixth Directive provides that the activities listed in Annex D thereto are in any event to be subjected to VAT, unless they are negligible. In doing so, the Sixth Directive clearly proceeds on the basis that the relationship of competition and the consequent likelihood of distortions fall to be determined in the abstract, having regard to the

activity as such and without reference to local conditions.

The Court's reply

18 At the outset, it must be noted that, under the first subparagraph of Article 4(5) of the Sixth Directive, States, regional and local government authorities and other bodies governed by public law are not to be considered taxable persons in respect of the activities or transactions in which they engage as public authorities.

19 As the Court has held on numerous occasions, two conditions must be cumulatively fulfilled in order for that provision to apply: the activities must be carried out by a body governed by public law and they must be carried out by that body acting as a public authority (see to that effect, particularly, Case C-202/90 *Ayuntamiento de Sevilla* [1991] ECR I-4247, paragraph 18, and *Fazenda Pública*, cited above, paragraph 15).

20 As regards the first of those conditions, it is common ground that the local authorities concerned are bodies governed by public law within the meaning of Article 4(5) of the Sixth Directive.

21 As for the second condition, activities pursued as public authorities within the meaning of that provision are those engaged in by bodies governed by public law under the special legal regime applicable to them and do not include activities pursued by them under the same legal conditions as those that apply to private economic operators (see, particularly, *Fazenda Pública*, paragraph 17, and the case-law cited).

22 In view of the nature of the analysis to be carried out, it is for the national court to classify the activity at issue in the main proceedings in the light of the criterion adopted above (*Comune di Carpaneto Piacentino and Others*, cited above, paragraph 16; Case C-4/89 *Comune di Carpaneto Piacentino and Others* [1990] ECR I-1869, paragraph 11; and *Fazenda Pública*, paragraph 23).

23 Since the question whether, in the cases in the main proceedings, the local authorities concerned were acting as public authorities has not been referred to the Court, it is appropriate to start from the hypothesis, subject to verification by the referring court, that the activity in question in the main proceedings must be regarded, for the purposes of this reference for a preliminary ruling, as coming within Article 4(5) of the Sixth Directive.

24 It must also be noted that, even where local authorities carry on such an activity as public authorities, they are, under the second subparagraph of Article 4(5) of the Sixth Directive, to be considered taxable persons where their treatment as non-taxable persons would lead to significant distortions of competition. The referring court is asking, in that respect, whether those distortions are to be evaluated by reference to the local market on which each of the local authorities concerned operates or by reference to the activity, as it is carried on throughout the national territory.

25 To reply to that question, it is necessary, in the absence of any guidance in the text of the second subparagraph of Article 4(5) of the Sixth Directive, to take into account the scheme and purpose of the Sixth Directive, as well as the place of Article 4(5) in the common system of VAT established by it.

26 It is important to emphasise in that regard that, as a general rule and in accordance with Article 2(1) of the Sixth Directive, the supply of services effected for consideration is to be subject to VAT.

27 Indeed, 'taxable person' means, under Article 4(1) of the Sixth Directive, any person who independently carries out in any place any economic activity specified in paragraph 2 thereof, whatever the purpose or results of that activity. 'Economic activity' is defined in Article 4(2) as including all activities of producers, traders and persons supplying services (Case C-284/04 *T-Mobile Austria and Others* [2007] ECR I-5189, paragraph 33).

28 Article 4 of the Sixth Directive gives a very wide scope to VAT (see Case 235/85 *Commission v Netherlands* [1987] ECR 1471, paragraph 7, and Case C-186/89 *van Tiem* [1990] ECR I-4363, paragraph 17).

29 However, only activities of an economic nature are covered by that provision (see, to that effect, Case C-306/94 *Régie dauphinoise* [1996] ECR I-3695, paragraph 15; Case C-77/01 *EDM* [2004] ECR I-4295, paragraph 47; Case C-465/03 *Kretztechnik* [2005] ECR I-4357, paragraph 18; and *T-Mobile Austria and Others*, cited above, paragraph 34).

30 It is only by way of derogation from that general rule that certain activities of an economic nature are not to be subjected to VAT. Such derogation is laid down by the first subparagraph of Article 4(5) of the Sixth Directive, under which activities engaged in by a body governed by public law acting as a public authority are not to be subject to VAT.

31 That derogation covers principally activities engaged in by bodies governed by public law acting as public authorities, which, while fully economic in nature, are closely linked to the exercise of rights and powers of public authority. In those circumstances, the fact that such bodies are not subject to VAT on those activities does not potentially have an anticompetitive effect, inasmuch as they are generally engaged in exclusively, or almost exclusively, by the public sector.

32 However, even where those bodies carry on such activities in their capacity as public authorities, they are to be considered taxable persons, under the second and third subparagraphs of Article 4(5) of the Sixth Directive, where their treatment as non-taxable persons would lead to significant distortions of competition or again if those activities, provided they are not carried out on such a small scale as to be negligible, are listed in Annex D to that directive.

33 A body governed by public law may, thus, be responsible, under national law, for carrying on certain activities of an essentially economic nature under the special legal regime applicable to them where those same activities can also be carried on in parallel by private operators, with the result that the treatment of that body as a non-taxable person may give rise to certain distortions of competition.

34 It is that undesirable result that the Community legislature sought to avoid by providing, in the third subparagraph of Article 4(5) of the Sixth Directive, that the activities specifically listed in Annex D to that directive (telecommunications, the supply of water, gas, electricity and steam, the transport of goods, port and airport services and passenger transport, etc.) are, 'in any event', unless they are negligible, to be subject to VAT, even when they are carried on by bodies governed by public law acting as public authorities.

35 In other words, the treatment of bodies governed by public law as non-taxable persons in respect of those activities is, unless such activities are negligible, presumed to lead to distortions of competition. It is thus clear from the wording of the third subparagraph of Article 4(5) of the Sixth Directive that the treatment of those bodies as taxable persons results from the carrying-on, as such, of the activities listed in Annex D to that directive, irrespective of the question whether or not a particular body governed by public law faces competition at the level of the local market on which it carries on those same activities.

36 Furthermore, there may exist, on the national level, other activities of an essentially economic nature, not listed in Annex D to the Sixth Directive, the list of which may vary from one Member State to another or from one economic sector to another, which are carried on in parallel both by bodies governed by public law in their capacity as public authorities and by private operators.

37 It is precisely to those activities that the second subparagraph of Article 4(5) of the Sixth Directive applies, in providing that bodies governed by public law, even when they act as public authorities, are to be considered taxable persons where their treatment as non-taxable persons would lead to significant distortions of competition.

38 The second and the third subparagraphs of Article 4(5) of the Sixth Directive are, consequently, closely linked since they pursue the same objective, namely the treatment of bodies governed by public law as taxable persons, even when they are acting as public authorities. Those subparagraphs are thus subject to the same logic, by which the Community legislature intended to limit the scope of the treatment of bodies governed by public law as non-taxable persons, so that the general rule stated in Articles 2(1) and 4(1) and (2) of that directive, under which any activity of an economic nature is, in principle, to be subject to VAT, is observed.

39 Consequently, the second and third subparagraphs of Article 4(5) of the Sixth Directive are to be interpreted as a whole.

40 It follows that the treatment of bodies governed by public law as taxable persons, either on the basis of the second subparagraph of Article 4(5) of the Sixth Directive, or on that of the third subparagraph of that provision, results from the carrying-on, as such, of a given activity, irrespective of whether or not those bodies face competition at the level of the local market on which they engage in that activity.

41 That conclusion is supported by the general principles of Community law applicable to fiscal matters, such as the principles of fiscal neutrality and legal certainty.

42 Thus, the principle of fiscal neutrality, a fundamental principle of the common system of VAT (see, particularly, Case C-255/02 *Halifax and Others* [2006] ECR I-1609, paragraph 92), precludes economic operators carrying on the same activities from being treated differently as far as the levying of VAT is concerned (see, particularly, Case C-216/97 *Gregg* [1999] ECR I-4947, paragraph 20).

43 In that regard, it must be recalled that the second subparagraph of Article 4(5) of the Sixth Directive is intended to ensure compliance with the principle of fiscal neutrality (Case C-430/04 *Feuerbestattungsverein Halle* [2006] ECR I-4999, paragraph 24).

44 Whilst it is true that the Sixth Directive provides for certain derogations which may interfere to some extent with the application of the principle of fiscal neutrality, like the derogation under the second subparagraph of Article 4(5) of the Sixth Directive (see, to that effect, Case C-378/02 *Waterschap Zeeuws Vlaanderen*

[2005] ECR I-4685, paragraph 43), since that provision permits the treatment of bodies governed by public law as non-taxable persons provided that such treatment would only distort competition insignificantly, the fact remains that that derogation must be interpreted in such a way that the least possible damage is done to that principle.

45 The argument put forward by the local authorities concerned amounts to treating only certain local authorities as taxable persons to the exclusion of others, according to whether distortions of competition are or are not produced on each of the local markets on which those local authorities operate, although the supply of services in question, namely the provision of off-street parking is substantially the same. That argument thus entails not only that private operators are treated differently to bodies governed by public law in a situation where the latter's treatment as non-taxable persons would lead to only insignificant distortions of competition, but also that different treatment might be introduced even among bodies governed by public law.

46 On the other hand, if those distortions are analysed by reference to the activity as such, irrespective of the conditions of competition prevailing on a given local market, compliance with the principle of fiscal neutrality is ensured, given that all bodies governed by public law are either taxable or non-taxable persons, the sole strain on that principle concerning only relations between those bodies and private operators, and that to the extent that the distortions of competition remain insignificant.

47 Moreover, as the Court has repeatedly held, Community legislation must be certain and its application foreseeable by those subject to it (see, particularly, Case C-301/97 *Netherlands v Council* [2001] ECR I-8853, paragraph 43, and *Halifax and Others*, cited above, paragraph 72). That requirement of legal certainty must be observed all the more strictly in the case of rules liable to entail financial consequences, in order that those concerned may know precisely the extent of the obligations which they impose on them (see, particularly, Case 326/85 *Netherlands v Commission* [1987] ECR 5091, paragraph 24, and Case C-17/01 *Sudholz* [2004] ECR I-4243, point 34).

48 The principle of legal certainty, which forms part of the Community legal order, must be observed both by the Community institutions and by the Member States when they exercise the powers conferred on them by Community directives (see Case C-376/02 '*Goed Wonen*' [2005] ECR I-3445, paragraph 32).

49 The argument that distortions of competition, within the meaning of the second subparagraph of Article 4(5) of the Sixth Directive, must be evaluated having regard to each of the local markets on which the local authorities offer off-street parking assumes a systematic re-evaluation, on the basis of often complex economic analyses, of the conditions of competition on a multitude of local markets, the determination of which may prove particularly difficult since the markets' demarcation does not necessarily coincide with the areas over which the local authorities exercise their powers. In addition, several local markets may exist within the territory of the same local authority.

50 Such a situation is capable, consequently, of giving rise to numerous disputes following any change affecting the conditions of competition prevailing on a given local market.

51 Thus, neither the local authorities nor the private operators will be in a position to provide, with the required certainty, for the conduct of their affairs if, on a given local market, the provision by the local authorities of off-street parking will or will not be subject to VAT.

52 That situation is therefore likely to jeopardise the principles of fiscal neutrality and legal certainty.

53 Accordingly, the reply to the first question must be that the second subparagraph of Article 4(5) of the Sixth Directive is to be interpreted as meaning that the significant distortions of competition, to which the treatment as non-taxable persons of bodies governed by public law acting as public authorities would lead, must be evaluated by reference to the activity in question, as such, without such evaluation relating to any local market in particular.

The second question

54 By its second question, the referring court is asking, in essence, whether the expression 'would lead to' significant distortions of competition, within the meaning of the second subparagraph of Article 4(5) of the Sixth Directive, is to be interpreted as encompassing only actual competition or as extending also to potential competition. That court is also asking for clarification as to what degree of probability is required for that condition to be satisfied.

Observations submitted to the Court

55 Relying on Paragraph 139 of Advocate General Kokott's Opinion in Case C-369/04 *Hutchison 3G and Others* [2007] ECR I-5247, the local authorities concerned maintain that the expression 'would lead to' is to be interpreted as requiring a real risk of material distortions of competition.

56 The United Kingdom Government submits that the expression 'would lead to' is interchangeable with the expression 'could lead to', which the Court used in the above-cited judgments in the two *Carpaneto Piacentino and Others* cases and which is also consistent with Advocate General Kokott's analysis in paragraphs 127 and 131 of her Opinion in *Hutchison 3G and Others*, cited above. It adds that there is already, on the one hand, competition between private companies and local authorities in many areas of the United Kingdom as well as, on the other hand, potential competition in other areas where there are, as yet, no private operators.

57 In Ireland's submission, the expression 'would lead to' requires the relevant national authorities charged with applying Article 4(5) of the Sixth Directive to be satisfied that an apprehended distortion of competition must be likely as a matter of probability rather than something that merely could or might result.

58 The Italian Government submits that, while absolute certainty is not necessary, the expression 'would lead to' must be understood as meaning that the risks of distortions of competition arising from the carrying-on of an activity which is not subject to VAT represent a strong probability and not a mere possibility.

59 The Commission contends that, in order to ensure that public bodies and private operators are placed on an equal footing in relation to the conditions of competition, there should be no barrier to the entry of private traders on to the market in question in the main proceedings. The Commission therefore submits that the expression 'would lead to' includes potential competition. It is sufficient, in that regard, that there be a real possibility for private traders to enter that market in competition with the relevant bodies governed by public law.

The Court's reply

60 It is important to record, as is clear from paragraph 30 of the present judgment, that the treatment of bodies governed by public law as non-taxable persons under the first subparagraph of

Article 4(5) of the Sixth Directive constitutes a derogation from the general rule that any activity of an economic nature be subjected to VAT, and that this provision must, therefore, be interpreted strictly. But the second subparagraph of Article 4(5) restores that general rule in order to avoid such treatment of those bodies leading to significant distortions of competition. The latter provision cannot therefore be construed narrowly.

61 The scope of the first subparagraph of Article 4(5) of the Sixth Directive would be enlarged unduly if the treatment, under the second subparagraph of Article 4(5), of those bodies as taxable persons had to be confined to cases of distortion of actual competition, which would, were they confronted only with potential competition, permit their treatment as non-taxable persons.

62 In addition, the treatment of those same bodies as non-taxable persons is liable, by itself, to discourage potential competitors from entering the market for the provision of off-street car-parking facilities.

63 It follows that the expression 'would lead to', for the purposes of the second subparagraph of Article 4(5) of the Sixth Directive, encompasses not only actual competition, but also potential competition.

64 However, the purely theoretical possibility of a private operator entering the relevant market, which is not borne out by any matter of fact, or by any objective evidence or by any analysis of the market, cannot be assimilated to the existence of potential competition. To make such an assimilation, that possibility must be real, and not purely hypothetical.

65 Consequently, the reply to the second question must be that the expression 'would lead to' is, for the purposes of the second subparagraph of Article 4(5) of the Sixth Directive, to be interpreted as encompassing not only actual competition, but also potential competition, provided that the possibility of a private operator entering the relevant market is real, and not purely hypothetical.

The third question

66 The third question concerns the interpretation to be given to the word 'significant', for the purposes of the second subparagraph of Article 4(5) of the Sixth Directive, and, in particular, whether it is to be interpreted as meaning 'more than trivial or *de minimis*', or 'material' or even 'exceptional'.

Observations submitted to the Court

67 The local authorities concerned submit that the word 'significant' means 'a materially adverse effect' or 'exceptional effect' on the public sector body's competitors, or an effect other than the simple fact that the public body does not charge VAT while its private sector competitors do charge it. They rely, in that regard, on Paragraph 41 of Advocate General Jacobs' Opinion in Case C-378/02 *Waterschap Zeeuws Vlaanderen*, cited above, according to which the word 'significant' is a synonym for 'exceptional'.

68 The United Kingdom Government contends that the word 'significant' means any distortion of competition that is not insignificant or *de minimis*. It adds, in relation to the use of the word 'exceptional' by Advocate General Jacobs in Paragraph 41 of his Opinion in *Waterschap*, that the Court did not endorse his analysis and did not repeat that word.

69 In Ireland's submission, the word 'significant' means that the distortions of competition must be important and appreciable, in the sense of likely to create a considerable alteration of the

conditions of competition otherwise applicable on the market in question to the clear detriment of the affected taxable private operators.

70 The Italian Government submits that the word 'significant' is to be interpreted as meaning 'at least material and not merely negligible'.

71 The Commission takes the view that the word 'significant' refers to a distortion that is not insignificant or negligible. It relies, in that regard, on the third subparagraph of Article 4(5) of the Sixth Directive, read in conjunction with Annex D thereto, according to which the activities listed in that annex are to be subject to VAT 'provided they are not carried out on such a small scale as to be negligible'. The function of the third subparagraph is, in any event, to make subject to VAT certain categories of activities which would otherwise have to be assessed under the second subparagraph of Article 4(5). Those two subparagraphs follow the same logic and it may be inferred that in using the word 'negligible' the legislature intended to describe activities which do not lead to 'significant' distortions of competition.

The Court's reply

72 It must be emphasised, first of all, as is clear from paragraph 60 of the present judgment, that the treatment of bodies governed by public law as taxable persons for the activities of an economic nature which they carry on as public authorities, required by the second subparagraph of Article 4(5) of the Sixth Directive, restores the general rule that any activity of an economic nature be subject to VAT, in order to avoid the treatment of those bodies as non-taxable persons leading to significant distortions of competition, and that that provision cannot therefore be construed narrowly.

73 Accordingly, the word 'significant' is to be understood as intended to restrict the scope of the treatment, under the first subparagraph of Article 4(5) of the Sixth Directive, of bodies governed by public law as non-taxable persons for those activities.

74 If that word had to be understood as meaning 'material', or even 'exceptional', the scope of the treatment of bodies governed by public law as non-taxable persons would be unduly enlarged. On the other hand, if their treatment as such were allowed only in cases where it would lead only to negligible competition, that scope would be circumscribed effectively.

75 Moreover, under the third subparagraph of Article 4(5) of the Sixth Directive, bodies governed by public law are taxable persons for the activities listed in Annex D thereto, provided they are not carried out on such a small scale as to be 'negligible'. In other words, the treatment of those bodies as non-taxable persons is permitted provided that those activities are negligible, assuming thus that the distortions of competition which would result would also be negligible.

76 Since, as is clear from paragraph 38 of the present judgment, the second and third subparagraphs of Article 4(5) of the Sixth Directive are closely linked since they pursue the same objective and since they are subject to the same logic, the word 'significant' is to be interpreted as meaning that the treatment of public bodies as non-taxable persons can be permitted only in cases where it would lead only to negligible distortions of competition.

77 Finally, compliance with the principle of fiscal neutrality supports that interpretation. The argument put forward by the local authorities concerned that bodies governed by public law should be subjected to VAT only in cases where the distortions of competition resulting from their treatment as non-taxable persons are material, or even exceptional, would create a fiscal situation in which a significant number of private operators effecting the same transactions as those carried out by those bodies would be treated differently from them in respect of the levying of VAT, which

would constitute a significant impairment of the principle of fiscal neutrality.

78 By contrast, the treatment of those bodies as non-taxable persons, in circumstances where it would not lead to any distortion of competition or lead only to negligible distortions, would bring about the least possible damage to the principle of fiscal neutrality.

79 Therefore the reply to the third question must be that the word 'significant' is, for the purposes of the second subparagraph of Article 4(5) of the Sixth Directive, to be understood as meaning that the actual or potential distortions of competition must be more than negligible.

Costs

80 Since these proceedings are, for the parties to the main proceedings, a step in the action pending before the national court, the decision on costs is a matter for that court. Costs incurred in submitting observations to the Court, other than the costs of those parties, are not recoverable.

On those grounds, the Court (Grand Chamber) hereby rules:

1. **The second subparagraph of Article 4(5) of 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 is to be interpreted as meaning that the significant distortions of competition, to which the treatment as non-taxable persons of bodies governed by public law acting as public authorities would lead, must be evaluated by reference to the activity in question, as such, without such evaluation relating to any local market in particular.**
2. **The expression 'would lead to' is, for the purposes of the second subparagraph of Article 4(5) of Sixth Council Directive 77/388, to be interpreted as encompassing not only actual competition, but also potential competition, provided that the possibility of a private operator entering the relevant market is real, and not purely hypothetical.**
3. **The word 'significant' is, for the purposes of the second subparagraph of Article 4(5) of Sixth Council Directive 77/388, to be understood as meaning that the actual or potential distortions of competition must be more than negligible.**

[Signatures]

* Language of the case: English.