Arrêt de la Cour
Case C-77/01

Empresa de Desenvolvimento Mineiro SGPS SA (EDM), formerly Empresa de Desenvolvimento Mineiro SA (EDM)

v

Fazenda Pública

(Reference for a preliminary ruling from the Tribunal Central Administrativo)

(Sixth VAT Directive – Articles 2, 4(2), 13B(d) and 19(2) – Meaning of 'economic activities' – Meaning of 'incidental financial transactions' – Services effected for consideration)

Summary of the Judgment

1. *Tax provisions – Harmonisation of laws – Turnover taxes – Common system of value added tax – Deduction of input tax – Goods and services used both for transactions in respect of which VAT is deductible and for transactions in respect of which it is not deductible – Proportionate deduction – Calculation – Sale of shares and other securities such as holdings in investment funds – Excluded if they do not constitute an economic activity – Placements in investment funds – Excluded if they do not constitute supplies of services for consideration – Loans by a holding company to its subsidiaries or placements in bank deposits or securities – Included – Limit – Exempt activities constituting incidental transactions – Assessment criteria – Jurisdiction of the national court*

(Council Directive 77/388, Arts 2(1), 4(2), 13B(d)(1) and (5), 17(5) and 19)

2. *Tax provisions – Harmonisation of laws – Turnover taxes – Common system of value added tax – Taxable transactions – Supplies of goods or services effected for consideration – Meaning – Operations carried out under a consortium contract by a member of the consortium – Excluded – Limits*

(Council Directive 77/388, Art. 2(1))

1. Under Article 17(5) of Sixth Directive 77/388 on the harmonisation of the laws of the Member States relating to turnover taxes, if the taxable person uses goods and/or services, on which he has paid input tax, both for transactions in respect of which VAT is deductible and for transactions in respect of which it is not deductible, it is necessary to calculate, in accordance with Article 19 of that directive, the deductible proportion to be applied to the amount of the input tax paid, transactions outside the scope of the Sixth Directive which do not give rise to a right to deduct having to be excluded from the calculation of that proportion.

In that regard, activities which consist in the simple sale of shares and other securities, such as holdings in investment funds, do not constitute economic activities within the meaning of Article 4(2) of the Sixth Directive and therefore do not come within the scope of that directive.

Moreover, placements in investment funds do not constitute supplies of services ‘effected for consideration’ within the meaning of Article 2(1) of the Sixth Directive and therefore likewise do not come within the scope thereof.

The amount of turnover relating to those transactions must consequently be excluded from the calculation of the deductible proportion referred to in Articles 17 and 19 of that directive.

By contrast the annual granting by a holding company of interest-bearing loans to companies in which it has a shareholding and placements by that holding company in bank deposits or in securities, such as Treasury notes or certificates of deposit, constitute economic activities carried out by a taxable person acting as such within the meaning of Articles 2(1) and 4(2) of the Sixth Directive.

However, since the said transactions are exempted from value added tax under points 1 and 5 of Article 13B(d) of the Sixth Directive, turnover attributable to them must be excluded from the calculation of the deductible proportion if they are incidental transactions within the meaning of the second sentence of Article 19(2) of the directive. They must in that respect be regarded as such in so far as they involve only very limited use of assets or services subject to value added tax; although the scale of the income generated by financial transactions within the scope of the Sixth Directive may be an indication that those transactions should not be regarded as incidental within the meaning of that provision, the fact that income greater than that produced by the activity stated by the undertaking concerned to be its main activity is generated by such transactions does not suffice to preclude their classification as ‘incidental transactions’.

It is for the national court to establish whether transactions involve only very limited use of assets or services subject to value added tax and, if so, to exclude those transactions from the calculation of the deductible proportion.

(see paras 53-55, 80, operative part 1)

2. Operations carried out by the members of a consortium in accordance with the provisions of a consortium contract and corresponding to the share assigned to each of them in that contract do not constitute supplies of goods or services ‘effected for consideration’ within the meaning of Article 2(1) of Sixth Directive 77/388 on the harmonisation of the laws of the Member States relating to turnover taxes, nor, consequently, a taxable transaction under that directive. The fact that such operations are carried out by the member of the consortium which manages it is irrelevant in that respect.

On the other hand, where the performance of more of the operations than the share thereof fixed by the said contract for a consortium member involves payment by the other members against the operations exceeding that share, those operations constitute a supply of goods or services ‘effected for consideration’ within the meaning of that provision

(see para. 91, operative part 2)

JUDGMENT OF THE COURT (Fifth Chamber)
29 April 2004(1)

(Sixth VAT Directive – Articles 2, 4(2), 13B(d) and 19(2) – Meaning of ‘economic activities’ – Meaning of ‘incidental financial transactions’ – Services effected for consideration)

In Case C-77/01,
REFERENCE to the Court under Article 234 EC by the Tribunal Central Administrativo (Portugal) for a preliminary ruling in the proceedings pending before that court between
Empresa de Desenvolvimento Mineiro SGPS SA (EDM), formerly Empresa de Desenvolvimento Mineiro SA (EDM),

and

Fazenda Pública, intervener:**Ministério Público,**
on the interpretation of Articles 2, 4(2), 13B(d) and 19(2) 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 COURT (Fifth Chamber),,

composed of: P. Jann, acting for the President of the Fifth Chamber, C.W.A. Timmermans and S. von Bahr (Rapporteur), Judges,
Advocate General: P. Léger,
Registrar: H.A. Rühl, Principal Administrator,
after considering the written observations submitted on behalf of:

– Empresa de Desenvolvimento Mineiro SGPS SA (EDM), by D. Duarte, advogado,
– the Portuguese Government, by M. Pretes, A. Seiça Neves and L. Fernandes, acting as Agents,
– the Commission of the European Communities, by T. Figueira and C. Giolito, acting as Agents,
after hearing the oral observations of Empresa de Desenvolvimento Mineiro SGPS SA (EDM), represented by D. Duarte, of the Portuguese Government, represented by V. Guimarães, acting as Agent, and of the Commission, represented by C. Giolito and M. França, acting as Agent, at the hearing on 29 May 2002,

having regard to the Report for the Hearing,

after hearing the Opinion of the Advocate General at the sitting on 12 September 2002,

gives the following

Judgment

1 By order of 19 December 2000, received at the Court on 15 February 2001, the Tribunal Central Administrativo (Central Administrative Court) referred to the Court for a preliminary ruling under Article 234 EC three questions on the interpretation of Articles 2, 4(2), 13B(d) and 19(2) 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, hereinafter ‘the Sixth Directive’).
2 Those questions were raised in the course of a dispute between Empresa de Desenvolvimento

Mineiro SGPS SA (hereinafter 'EDM') and the Fazenda Pública (Treasury) on the right to deduct value added tax (hereinafter 'VAT') paid as an input by EDM as a taxable person carrying out not only transactions in respect of which VAT is deductible under Article 17(2)(a) of the Sixth Directive, but also transactions which that undertaking does not regard as constituting an economic activity, within the meaning of Article 4(2) of that directive, or as incidental financial transactions, within the meaning of the second sentence of Article 19(2) thereof.

Legal background

Community legislation

3 Under Article 2(1) of the Sixth Directive, VAT is chargeable on the supply of goods and services effected for consideration within the territory of the country by a taxable person acting as such.

4 Under Article 4(1) of the Sixth Directive, 'taxable person' means any person who independently carries out any economic activity specified in Article 4(2). The term 'economic activities' is defined in Article 4(2) as comprising all activities of producers, traders and persons supplying services, including the exploitation of tangible or intangible property for the purpose of obtaining income therefrom on a continuing basis.

5 Under Article 11A(1)(a) of the Sixth Directive, the taxable amount is everything which constitutes the consideration which has been or is to be obtained by the supplier of goods or services from the purchaser, the customer or a third party for such supplies including subsidies directly linked to the price of such supplies.

6 Article 13B(d) of the Sixth Directive provides:

'Without prejudice to other Community provisions, Member States shall exempt …:

…

(d)the following transactions:

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

2.the negotiation of or any dealings in credit guarantees or any other security for money and the management of credit guarantees by the person who is granting the credit;

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

...

5.transactions, including negotiation, excluding management and safekeeping, in shares, interests in companies or associations, debentures and other securities excluding:

–documents establishing title to goods

–the rights or securities referred to in Article 5(3).'

7 Article 17(2)(a) of the Sixth Directive provides that 'in so far as the goods and services are used for the purposes of his taxable transactions, the taxable person shall be entitled to deduct from the tax which he is liable to pay … value added tax due or paid in respect of goods or services supplied or to be supplied to him by another taxable person'.

8 As regards goods and services used by a taxable person both for transactions in respect of which VAT is deductible and for transactions in respect of which it is not deductible, the first subparagraph of Article 17(5) of the Sixth Directive provides 'only such proportion of the value added tax shall be deductible as is attributable to the former transactions'. The second subparagraph of Article 17(5) states that 'this proportion shall be determined, in accordance with Article 19, for all the transactions carried out by the taxable person'.

9 Paragraphs (1) and (2) of Article 19 of the Sixth Directive read as follows:

'1. The proportion deductible under the first subparagraph of Article 17(5) shall be made up of a fraction having:

– as numerator, the total amount, exclusive of value added tax, of turnover per year attributable to transactions in respect of which value added tax is deductible under Article 17(2) and (3),

– as denominator, the total amount, exclusive of value added tax, of turnover per year attributable to transactions included in the numerator and to transactions in respect of which value added tax is not deductible. The Member States may also include in the denominator the amount of subsidies, other than those specified in Article 11A(1)(a).
The proportion shall be determined on an annual basis, fixed as a percentage and rounded up to a figure not exceeding the next unit.
2. By way of derogation from the provisions of paragraph 1, there shall be excluded from the calculation of the deductible proportion, amounts of turnover attributable to the supplies of capital goods used by the taxable person for the purposes of his business. Amounts of turnover attributable to transactions specified in Article 13B(d), in so far as these are incidental transactions, and to incidental real estate and financial transactions shall also be excluded. …'
National legislation
10 Article 23 of the Código do imposto sobre o valor acrescentado (VAT Code, hereinafter 'the CIVA') provides:
'1.Where the taxable person, in the course of his business, makes supplies of goods or services, some of which do not give rise to the right to deduct, input tax shall be deductible only in direct proportion to the annual turnover of the transactions which give rise to the right to deduct.
...
4.The specific proportion of deduction referred to in paragraph 1 is derived from a fraction whose numerator is the annual amount, exclusive of VAT, of the supplies of goods and services which give rise to the right to deduct under Articles 19 and Article 20(1) and whose denominator is the annual amount, exclusive of VAT, of all the transactions carried out by the taxable person, including exempt transactions and transactions outside the scope of VAT, particularly grants not subject to VAT other than grants for plant or equipment.
5.However, the calculation referred to in the preceding paragraph does not include supplies of fixed assets which have been used in the undertaking's business or real estate or financial transactions that are incidental to the business carried on by the taxable person.'
11 Under Article 9(28) of the CIVA exempt activities are:
'(a)The granting and the negotiation of credit, in any form, including discount and rediscount transactions, and the administration and management of credit by the person who granted it.
(b)The negotiation and issuing of securities, bonds, sureties and other guarantees, and the administration and management of credit guarantees by the person who issued them.
...
(f)Transactions and services, including negotiation, but excluding mere safekeeping, administration or management, relating to shares, other interests in companies or associations, debentures and other securities, excluding documents establishing title to goods.
(g)Services and transactions relating to the placing, subscription for and firm purchase of issues of public or private securities.
(h)The administration or management of investment funds.'
12 In Portuguese law, 'consortium' means a 'contract by which two or more natural or legal persons, who carry on an economic activity, agree with each other to carry on, in a concerted manner, a certain activity or to make a certain contribution' with a view to attaining one of the objectives set out, among which is prospecting or exploring for natural resources (Articles 1 and 2 of Decreto-lei (Decree-law) No 231/81 of 28 July 1981, *Diário da República* I, Series A, No 171, of 28 July 1981).

The main proceedings and the questions referred for a preliminary ruling
13 It is apparent from the order for reference that EDM is a holding company in the mining sector which, after being a public undertaking, was converted into a legal entity governed by private law, in the form of a limited company, with effect from September 1989.

14 Under Article 3(1) of its statutes, which derive from Decreto-lei No 313/89 of 21 September 1989 (*Diário da República* I, Series A, No 218, of 21 September 1989), EDM's main purpose is:

'(a)Prospecting and exploring for, extracting, developing and exploiting metallic and non-metallic minerals, and the marketing thereof and of the products and by-products resulting from their processing;

(b)Applied research and technological development aimed directly at productive investment, by means of joint ventures;

(c)Managing company shareholdings which it owns or whose management powers have been contractually entrusted to it, for companies whose purposes include the activities referred to in paragraph (a);

(d)Promoting investment projects and the formation of companies whose purpose is connected to the mining industry by encouraging, especially, the association of public and private interests'.

15 Until its conversion into a limited company, one of EDM's main purposes was also, under its statutes then in force, to assist companies in which it had a shareholding to obtain loans from credit institutions, by being able to guarantee such loans.

16 The referring court observes that the management of its shareholdings and scientific and technological research in the mining sector with a view to investment therein, particularly through the creation of new undertakings, were always EDM's principal activity and it has only occasionally sold its shareholdings in companies, even if the proceeds of those sales attained a considerable sum.

17 EDM participates in three consortia the sole purpose of each of which is to discover mineral deposits in three different regions of Portugal and to examine the profitability of their exploitation. Under the contracts creating those consortia (hereinafter 'the consortium contracts'), if a mineral deposit whose exploitation would be profitable is discovered, a company is created to exploit it.

18 EDM's activities in the context of each of those consortia consist in technical activity and coordination of operations as manager of the consortium, as well as participation in advisory councils and technical committees established for that purpose. Invoices describing the operations to be carried out and stating their costs are issued by each of the undertakings which are members of the consortium and sent to its manager, namely EDM. Those invoices are used solely for subsequent settlement of the accounts between the undertakings making up the consortium, in accordance with the percentages for sharing of the expenses agreed in each consortium contract.

19 The order for reference shows that EDM was the subject of an inspection by the Portuguese tax authorities (hereinafter 'the tax authorities') in connection with the consideration of an application for repayment it had made. During that inspection, it was established that between 1988 and 1992, EDM deducted VAT as if it carried out only transactions conferring the right to deduct, although, according to those authorities, because of the type of transactions carried out, it should have been treated as a mixed taxable person, subject to the regime of Article 23 of the CIVA, that is to say to the use of the method of calculating the deductible proportion laid down by that provision.

20 Goods were acquired and services received which were common to the different activities carried on by the taxable person, such as those carried out for its administration or for its headquarters, for which VAT was deducted globally without any apportionment being made between taxable and exempt transactions.

21 During that inspection, it was established that EDM incorrectly deducted PTE 137 933 862 (around EUR 688 000).

22 The referring court states that, according to the tax authorities, the following constitute revenue arising from the supply of goods and/or services which does not give rise to the right to deduct:

– dividends arising from shareholdings in the capital of companies;
– interest on loans to undertakings in which EDM has a shareholding;
– the proceeds of sale of shares and other negotiable securities;
– revenue from other treasury operations;
– the value of operations performed in connection with the consortia, of which EDM is a member and manager.

23 The tax authorities consider that dividends, loan interest, revenue from short-term treasury operations, including shareholdings and the proceeds of sale of shares and other negotiable securities, are income from activities covered by the exemption in Article 9(28)(a) and (f) of the CIVA and do not therefore confer any right to deduct input tax. As regards operations performed by EDM in connection with the consortia, since it is responsible for the consortia and therefore the manager of their investments, those operations come under subparagraph (h) of the same provision of the CIVA and are therefore also exempt from VAT. Since it carries on simultaneously exempted and taxed activities, EDM is subject to the provision of Article 23 of the CIVA. All the abovementioned revenue should, therefore, be included in the denominator of the fraction used in calculating the deductible proportion, in accordance with Article 23(4), because all the activities in question form part of the principal activity of EDM, including the sale of securities and the other treasury operations, given that the volume of those transactions is greater than that of the taxable transactions.

24 In those circumstances, the tax authorities calculated the amount of the deductible proportion and assessed the VAT and compensatory interest for the financial years 1988 to 1992.

25 EDM contested the tax authorities' decisions as regards that assessment before the Tribunal Tributário de Primeira Instância de Lisboa (Tax Court of First Instance, Lisbon, Portugal) which dismissed its action save as regards the said dividends.

26 EDM appealed to the Tribunal Central Administrativo in so far only as that judgment dismissed its claims at first instance.

27 The national court states that, in the dispute before it, it is necessary to decide, first, whether the provision of interest-bearing loans granted annually by EDM to the undertakings in which it has a shareholding and the operations performed by it in connection with the three consortia of which it is a member and which it manages, in particular in respect of that part which exceeds its own share of those operations as fixed in the consortium contracts, against payment by the other members, comes within the meaning of 'economic activity'. According to that court, it is necessary to decide, secondly, whether the sale of shares and other negotiable instruments as well as the other treasury operations and the loans granted by EDM, if they are to be treated as taxable transactions for the purposes of VAT, are 'incidental transactions' within the meaning of Article 19(2) of the Sixth Directive.

28 On the basis of those considerations, the Tribunal Central Administrativo decided to stay the proceedings and to refer the following questions to the Court for a preliminary ruling:

'1.Does the annual granting of interest-bearing loans by a holding company to companies in which it has a shareholding, where its principal activity is their management and, to a certain extent also, the guaranteeing of loans contracted by them, constitute an "economic activity" within the meaning of [Article 4(2) of] the Sixth Directive …?

2.Does the performance of operations, in connection with a consortium, as in this case, by a company which both is a member thereof and manages it, particularly where they exceed its share as stipulated in the contract, against payment by the other members of the consortium constitute an "economic activity" within the meaning of the Sixth Directive?

3.Is an undertaking's financial activity which generates annual income which is clearly higher than that from the activity described in its statutes as its principal activity to be regarded as "incidental" for the purposes of Article 19(2) of the Sixth Directive?'

The first and third questions

29 By its first and third questions, which it is convenient to consider together, the national court is asking, in essence, whether the financial transactions of a holding company, consisting in the annual granting of interest-bearing loans to companies in which it has a shareholding, in the sale of shares and other negotiable securities and in other treasury operations, constitute 'economic activities' within the meaning of Article 4(2) of the Sixth Directive and, if so, since those financial transactions are exempted under Article 13B(d) of that directive, whether they are to be regarded as 'incidental' for the purposes of Article 19(2) of that directive and whether, therefore, the amount of turnover relating to those transactions is to be excluded from the denominator of the fraction used in calculating the deductible proportion.

Observations submitted to the Court

30 EDM claims that the financial transactions to which the tax authorities refer, which include interest from securities, bank deposits and other short-term placements, like the interest on the loans granted by EDM to companies in which it has a shareholding and the proceeds of sale of securities and shares, do not correspond to its main corporate purpose as set out in Article 3 of its statutes but come within the scope of activities which it could carry on only incidentally.

31 In that regard, it relies on the judgment in Case C-142/99 *Floridienne and Berginvest* [2000] ECR I-9567, pointing out particularly that the Court held that interest paid to a holding company by its subsidiaries on loans it has made to them, where the loan transactions do not constitute, for the purposes of Article 4(2) of the Sixth Directive, an economic activity of that holding company, must be excluded from the denominator of the fraction used to calculate the deductible proportion.

32 As regards interest from short-term placements, EDM submits that, given that for legal purposes short-term placements are regarded as loans, they are excluded from the field of EDM's main activities, like its loans to its subsidiaries. In addition, those loans are comparable to loans on debenture or share their nature and should therefore be classified as 'incidental financial transactions' (see Case C-80/95 *Harnas & Helm* [1997] ECR I-745).

33 The result is the same for sales of shares and other negotiable securities, since their financial character is obvious as is also their incidental nature. So far as concerns the taking into account of the scale of the sales of shares and other securities by a non-financial entity, EDM refers to Case C-155/94 *Wellcome Trust* [1996] ECR I-3013.

34 EDM concludes that the second sentence of Article 19(2) of the Sixth Directive is to be interpreted as meaning that the financial transactions by an undertaking whose economic activity, for the purposes of Article 4(1) and (2) of the Sixth Directive, includes only the management of its shareholdings in mining sector companies and scientific and technical research in the same sector, by supplying services to other mining undertakings in that domain, are to be excluded from the fraction used as the basis for calculating the deductible proportion.

35 As a preliminary point, the Portuguese Government submits that EDM is not purely a holding company, but that it carries on directly a commercial and industrial business which is, in most cases, the same as that of the companies in which it has a shareholding.

36 As regards loan interest, the Portuguese Government maintains that the interest rate is laid down in the loan contracts and that it is adapted to the amount of the principal lent, which distinguishes it from dividends, for which it is impossible to establish a direct connection between the payment of their amount and the value of the service provided (see *Floridienne and Berginvest*, cited above, paragraph 14). Likewise, as regards sales of shares and other negotiable securities, the price depends on and is quantitatively a function of the value of the interest sold.

37 In view of the nature of EDM's activities and having regard, in particular, to the fact that it is only exceptionally that the commercial nature of the activities coming within Article 13B(d) of the Sixth Directive is recognised (see *Wellcome Trust*, paragraph 35, and *Harnas & Helm*, cited above, paragraph 16), it cannot be concluded that the loans and the sales of

shares take place always and only in the domain of a holding company's non-commercial activity. Although those loans and sales of shares concern only EDM's subsidiaries, nothing prevents them being carried in such a way as also to constitute a source of revenue for EDM, which it uses for the purposes of its commercial activities.

38 Consequently, the Portuguese Government takes the view that the annual grant of interest-bearing loans by a holding company to companies in which it has a shareholding and the sale of shares and other negotiable securities constitute an 'economic activity' within the meaning of Article 4(2) of the Sixth Directive.

39 According to that Government, those loans and sales of shares and other negotiable securities are exempt financial transactions under point 5 of Article 13B(d) of the Sixth Directive, which constitute an extension of the activity of the taxable person. Those transactions cannot therefore be regarded as 'incidental' for the purposes of Article 19(2) of that directive (see Case C-306/94 *Régie dauphinoise* [1996] ECR I-3695, paragraph 22). The considerable amount of those transactions and their frequency confirm that conclusion.

40 The Commission, basing itself on paragraphs 26 to 31 of the judgment in *Floridienne and Berginvest,* submits that the granting of loans by a holding company to its subsidiaries should be regarded, for the purposes of Article 4(2) of the Sixth Directive, as an economic activity, consisting in the exploitation of capital with a view to obtaining therefrom continuing income by way of interest, since such activity is not carried on an occasional basis, but in accordance with a business or commercial purpose, characterised by, in particular, a concern to maximise returns on the capital invested.

41 If such is the case, the interest paid to the holding company by its subsidiaries constitutes consideration for the transactions exempted from VAT under Article 13B(d) of the Sixth Directive and they should be included in the denominator of the fraction used for calculating the deductible proportion, in accordance with Article 19 of that directive.

42 So far as concerns the financial transactions other than EDM's loans to its subsidiaries, the Commission observes that three possible situations must be distinguished among them.

43 As regards the first possible situation, the Commission maintains that, while the national court considers that EDM's financial activities are carried out in connection with a business objective or commercial purpose, they come within VAT's field of application (see *Floridienne and Berginvest*, paragraph 28), but are exempt from VAT. Since they cannot be regarded as 'incidental' transactions, whatever their scale, those transactions must be included in the denominator of the fraction used to calculate the deductible proportion, in accordance with Article 19 of the Sixth Directive.

44 So far as concerns the second possible situation, if it is considered that the said financial activities do not correspond to a taxable activity, but that it is simply a question of the management of a private investment consequent on the mere holding of an asset, it is in that case an activity which remains outside the scope of VAT.

45 As regards the third possible situation, the Commission makes clear that, although the transactions concerned come within the scope of VAT, they must be regarded as 'incidental', that is to say, they cannot be regarded as forming part of the usual business activity of the taxable person.

46 In that regard, the Commission maintains, relying on paragraph 21 of the judgment in *Régie dauphinoise*, cited above, that the fact that the yield from the financial transactions carried out by EDM may exceed that from its principal activity does not mean that the concept of an incidental transaction cannot apply. On the contrary, in the case of an undertaking such as EDM, whose prospecting and exploration activity is profitable only in the medium term and may even turn out to be unprofitable in the long term, the inclusion of its financial transactions in the denominator of the fraction used to calculate the deductible proportion would have precisely the effect of distorting the calculation of the deduction and, therefore, of putting the neutrality of VAT in question. Therefore, activities which do not come within the compass of the usual business activities of that undertaking must be regarded as 'incidental transactions' within the meaning of Article 19(2) of the Sixth

Directive, irrespective of the profits they generate.

Findings of the Court

47 As a preliminary point, it is appropriate to note that, although Article 4 of the Sixth Directive gives a very wide scope to VAT (see Case C-186/89 *Van Tiem* [1990] ECR I-4363, paragraph 17), only activities of an economic nature are covered by that provision (see *Régie dauphinoise*, paragraph 15).

48 Under Article 4(1) of the Sixth Directive, a taxable person means any person who independently carries on such economic activities. Economic activities are defined in Article 4(2) as encompassing all activities of producers, traders and persons supplying services, in particular the exploitation of tangible or intangible property for the purpose of obtaining income therefrom on a continuing basis. That concept of 'exploitation' refers, in accordance with the requirements of the principle that the common system of VAT should be neutral, to all those transactions, whatever their legal form (see *Van Tiem*, cited above, paragraph 18, and *Régie dauphinoise*, paragraph 15).

49 In that regard, it follows from the Court's consistent case-law that only payments which are the consideration for a transaction or an economic activity come within the scope of VAT and that such is not the case of those which arise simply from ownership of the asset (see Case C-333/91 *Sofitam* [1993] ECR I-3513, paragraph 13, *Régie dauphinoise*, paragraph 17, and *Floridienne and Berginvest*, paragraph 26).

50 Furthermore, it follows from Article 2(1) of the Sixth Directive that a taxable person must act 'as such' in order for a transaction to be subject to VAT (see *Régie dauphinoise* , paragraph 15).

51 It follows from the foregoing that, in a case such as the main proceedings, it is appropriate, first, to establish whether the various financial transactions in question are activities which are among those referred to in Articles 2(1) and 4(1) and (2) of the Sixth Directive or whether they are outside its scope.

52 As regards financial transactions which come within the Sixth Directive, it is necessary, secondly, to determine whether they are exempted under Article 13B(d) of that directive.

53 Thirdly, under Article 17(5) of the Sixth Directive, if the taxable person uses goods and/or services, on which he has paid input tax, both for transactions in respect of which VAT is deductible and for transactions in respect of which it is not deductible, it is necessary to calculate, in accordance with Article 19, the deductible proportion to be applied to the amount of the input tax paid.

54 It is appropriate to point out in that regard that it follows from the Court's case-law that, in order not to compromise the objective of neutrality which the common system of VAT guarantees, transactions outside the scope of the Sixth Directive which do not therefore give rise to a right to deduct must be excluded from the calculation of the deductible proportion referred to in Articles 17 and 19 of the Sixth Directive (see to that effect, among others, *Sofitam*, cited above, paragraphs 13 et 14, and Case C-16/00 *Cibo Participations* [2001] ECR I-6663, paragraph 44).

55 Fourthly, in calculating the deductible proportion, it is appropriate to examine whether the financial transactions in question which come within the Sixth Directive, but which are exempted under Article 13B(d) thereof, are to be regarded as incidental transactions, since in that case, under the second sentence of Article 19(2) and by way of derogation from Article 19(1), amounts of turnover attributable to such transactions must be excluded from the calculation of the deductible proportion.

The scope of the Sixth Directive

56 Apart from interest received by EDM in consideration of the loans granted to companies in which it has a shareholding, the national court refers to the sale of negotiable securities and to other treasury operations. It seems to be clear from the observations submitted to the Court and from the replies to its written questions to EDM that it is, in fact, a matter of sales of shares and of holdings in investment funds, of payment of interest produced by bank deposits and by securities such as Treasury notes and certificates of deposit, and of the yield from placements in investment funds.

57 In that regard, it must be noted at the outset that under consistent case-law the mere acquisition and holding of shares in a company is not to be regarded as an economic activity within the meaning of the Sixth Directive, conferring on the holder the status of a taxable person. The mere acquisition of financial holdings in other undertakings does not amount to the exploitation of property for the purpose of obtaining income therefrom on a continuing basis because any dividend yielded by those holdings is merely the result of ownership of the property and is not the consideration for any economic activity within the meaning of that directive (see *Harnas & Helm*, paragraph 15, and *Floridienne and Berginvest*, paragraph 21). If such activities do not therefore in themselves constitute an economic activity within the meaning of that directive, the same must be true of activities consisting in the sale of such holdings (see *Wellcome Trust*, cited above, paragraph 33, and Case C-442/01 *KapHag* [2003] ECR I-6851, paragraphs 38 and 40).

58 Likewise, the simple acquisition and the mere sale of other negotiable securities cannot amount to exploitation of an asset intended to produce revenue on a continuing basis, the only consideration for those transactions consisting of a possible profit on the sale of those securities.

59 Such transactions cannot as a rule constitute, by themselves, economic activities within the meaning of the Sixth Directive. Admittedly, it follows from point 5 of Article 13B(d) thereof that transactions affecting securities may come within the scope of VAT. However, the transactions covered by that provision are those which consist in drawing revenue on a continuing basis from activities which go beyond the compass of the simple acquisition and sale of securities, such as transactions carried out in the course of a business trading in securities.

60 It follows that an undertaking which pursues activities consisting in the simple sale of shares and other negotiable securities, such as holdings in investment funds, is to be regarded, so far as those activities are concerned, as confining itself to managing an investment portfolio in the same way as a private investor (see *Wellcome Trust*, cited above, paragraph 36).

61 It is important to observe in that regard that neither the scale of a share sale, nor the employment in connection with such a sale of consultancy undertakings, can constitute criteria for distinguishing between the activities of a private investor, which fall outside the scope of the Sixth Directive, and those of an investor whose transactions constitute an economic activity (see *Wellcome Trust*, paragraph 37).

62 Therefore, it must be held that activities which consist in the simple sale of shares and other negotiable securities, such as holdings in investment funds, do not constitute economic activities within the meaning of Article 4(2) of the Sixth Directive and, therefore, they do not come within the scope of that directive.

63 As regards the yield from placements in investment funds, it must be held that it does not constitute direct consideration for supplies of services consisting in making capital available for the benefit of a third party (see *Régie dauphinoise*, paragraphs 16 and 17). Like dividends, such yield cannot be regarded as the effective exchange for services rendered. Consequently, those placements do not constitute supplies of services 'effected for consideration', within the meaning of Article 2(1) of the Sixth Directive, and therefore do not come within the scope of VAT (see, to that effect, Case C-305/01 *MKG-Kraftfahrzeuge-Factoring* [2003] ECR I-6729, paragraph 47).

64 It follows from the case-law noted in paragraph 54 of this judgment that since the simple sale of shares and other negotiable securities, such as holdings in investment funds, and the yield from placements in investment funds do not come within the scope of the Sixth Directive, the amount of turnover relating to those transactions is to be excluded from the calculation of the deductible proportion referred to in Articles 17 and 19 of that directive.

65 On the other hand, in accordance with the Court's case-law, interest received by a holding company in consideration of loans granted to companies in which it has shareholdings cannot be excluded from the scope of VAT, since that interest does not arise

from the simple ownership of the asset, but is the consideration for making capital available for the benefit of a third party (see, to that effect, *Régie dauphinoise*, paragraph 17).

66 As regards the question whether, in such a situation, a holding company supplies that service in the capacity of a taxable person, the Court has held, at paragraph 18 of the judgment in *Régie dauphinoise*, that a person carrying out transactions which constitute the direct, continuous, and necessary extension of the person's taxable activity, such as the receipt by a managing agent of interest resulting from the placements of monies received from clients in the course of managing those clients' properties, acts in that capacity.

67 That is with stronger reason the case when the transactions concerned are carried out with a business or commercial purpose characterised by, in particular, the wish to maximise returns from capital invested.

68 It is clear that an undertaking acts thus if it uses funds forming part of its assets to supply services constituting an economic activity within the meaning of the Sixth Directive, such as the granting of interest-bearing loans by a holding company to companies in which it has shareholdings, whether those loans are granted as economic support to those companies or as placements of treasury surpluses or for other reasons.

69 Interest paid to an undertaking in consideration of bank deposits or placements in securities such as Treasury notes or certificates of deposit likewise cannot be excluded from the scope of VAT, since the interest paid does not arise from the simple ownership of the asset but constitutes the consideration for making capital available for the benefit of a third party (see, to that effect, *Régie dauphinoise*, paragraph 17). It follows from the preceding paragraph that an undertaking acts as a taxable person if it thus uses funds forming part of its assets.

70 Therefore, it must be held that the annual granting by a holding company of interest-bearing loans to companies in which it has a shareholding and placements by that holding company in bank deposits or in securities, such as Treasury notes or certificates of deposit, constitute economic activities carried out by a taxable person acting as such within the meaning of Articles 2(1) and 4(2) of the Sixth Directive.

The concept of transactions exempted from VAT

71 Since the granting by a holding company of loans to companies in which it has a shareholding and placements by that holding company in bank deposits or in securities, such as Treasury notes or certificates of deposit, are to be regarded as supplies of services within the scope of the Sixth Directive, it must be held that such activities are exempted from VAT under points 1 and 5 of Article 13B(d) of the Sixth Directive.

The calculation of the deductible proportion

72 Where the undertaking concerned carries out both transactions in respect of which VAT is deductible and transactions in respect of which it is not, it follows from the second subparagraph of Article 17(5) of the Sixth Directive that the deductible proportion to be applied to the amount of input tax paid is to be calculated in accordance with Article 19 of that directive.

73 In that regard, it is clear from Article 19(1) of the Sixth Directive that the deductible proportion is the product of a fraction whose numerator is the total amount, exclusive of VAT, of turnover attributable to transactions in respect of which VAT is deductible and whose denominator is the total amount, exclusive of VAT, of the turnover attributable to transactions included in the numerator and to transactions in respect of which VAT is not deductible, such as those exempted under Article 13B(d). As follows from paragraph 54 of this judgment, transactions which are outside the scope of the Sixth Directive must be excluded from the calculation of that proportion.

The derogation for incidental transactions

74 It is appropriate therefore to consider whether the granting by a holding company of loans to companies in which it has a shareholding and placements by that holding company in bank deposits or in securities, such as Treasury notes or certificates of

deposit, which are exempt under points 1 and 5 of Article 13B(d) of the Sixth Directive, constitute incidental transactions within the meaning of the second sentence of Article 19(2) thereof, in which case the latter provision requires those transactions to be left out of the calculation of the deductible proportion.

75 In that regard, it is appropriate to observe that, for the purposes of applying Article 19(1) of the Sixth Directive, an increase of the amount of the turnover relating to transactions in respect of which VAT is not deductible leads to a decrease in the amount of VAT which the taxable person may deduct. The purpose of excluding certain incidental transactions from the denominator of the fraction used to calculate the deductible proportion, in accordance with the second sentence of Article 19(2), is to neutralise the negative effects for the taxable person of that consequence inherent in the said calculation in order to avoid such transactions distorting that calculation and to thus meet the objective of neutrality guaranteed by the common system of VAT.

76 As the Court held at paragraph 21 of the judgment in *Régie dauphinoise,* if all receipts from a taxable person's financial transactions linked to a taxable activity were to be included in that denominator, even where the creation of such receipts did not entail the use of goods or services subject to VAT, or at least entailed only their very limited use, calculation of the deduction would be distorted.

77 In that regard, it is appropriate to observe that the scale of the income generated by financial transactions within the scope of the Sixth Directive may be an indication that those transactions should not be regarded as incidental within the meaning of the second sentence of Article 19(2). However, the fact that income greater than that produced by the activity stated to be its main activity by the undertaking concerned is generated by such transactions does not suffice to preclude their classification as 'incidental transactions' within the meaning of that provision. As the Commission correctly observed, in a situation such as that in the main proceedings, in which the activity of prospecting is profitable in the medium term only or may even prove to be unprofitable and the turnover from transactions in respect of which VAT is deductible may, as a result, be very small, the inclusion of those transactions solely because of the extent of the income they produce would clearly result in distortion of the calculation of the deduction.

78 It follows from the foregoing that the annual granting of loans by a holding company to companies in which it has a shareholding and placements in bank deposits or in securities such as Treasury notes or certificates of deposit, in so far as those transactions involve only very limited use of assets or services subject to VAT, are to be regarded as incidental transactions within the meaning of the second sentence of Article 19(2) of the Sixth Directive. In that regard, although the scale of the income generated by financial transactions within the scope of the Sixth Directive may be an indication that those transactions should not be regarded as incidental within the meaning of that provision, the fact that income greater than that produced by the activity stated by the undertaking concerned to be its main activity is generated by such transactions does not suffice to preclude their classification as 'incidental transactions'.

79 It is for the national court to establish whether the transactions concerned in the main proceedings involve only very limited use of assets or services subject to VAT and, if so, to exclude interest generated by those transactions from the denominator of the fraction used to calculate the deductible proportion.

80 Therefore the answer to the first and third questions must be that, in a situation such as that in the main proceedings,

– activities which consist in the simple sale of shares and other securities, such as holdings in investment funds, do not constitute economic activities within the meaning of Article 4(2) of the Sixth Directive and therefore do not come within the scope of that directive;

placements in investment funds do not constitute supplies of services 'effected for consideration' within the meaning of Article 2(1) of the Sixth Directive and therefore likewise do not come within the scope thereof;

the amount of turnover relating to those transactions must consequently be excluded from the calculation of the deductible proportion referred to in Articles 17 and 19 of that directive;

– by contrast the annual granting by a holding company of interest-bearing loans to companies in which it has a shareholding and placements by that holding company in bank deposits or in securities, such as Treasury notes or certificates of deposit, constitute economic activities carried out by a taxable person acting as such within the meaning of Articles 2(1) and 4(2) of the Sixth Directive;

however, such transactions are exempted from VAT under points 1 and 5 of Article 13B(d) of that directive;

in calculating the deductible proportion referred to in Articles 17 and 19 of the Sixth Directive, those transactions are to be regarded as incidental transactions within the meaning of the second sentence of Article 19(2) thereof in so far as they involve only very limited use of assets or services subject to VAT; although the scale of the income generated by financial transactions within the scope of the Sixth Directive may be an indication that those transactions should not be regarded as incidental within the meaning of that provision, the fact that income greater than that produced by the activity stated by the undertaking concerned to be its main activity is generated by such transactions does not suffice to preclude their classification as 'incidental transactions';

it is for the national court to establish whether the transactions concerned in the main proceedings involve only very limited use of assets or services subject to VAT and, if so, to exclude interest generated by those transactions from the denominator of the fraction used to calculate the deductible proportion.

The second question

81 By its second question the national court is asking, in essence, whether operations such as those at issue in the main proceedings, performed under the terms of a consortium contract made by a company which is a member of that consortium and manages it, constitute taxable transactions under the Sixth Directive, in particular where the performance by that company of more of the operations than the share for which it is responsible under the said contract entails payment by the other members of that consortium against the operations exceeding the said share.

Observations submitted to the Court

82 EDM submits that it follows from Article 2(1) of the Sixth Directive that in order to ascertain whether there is a supply of services for VAT purposes it is sufficient to determine whether it can be described as a transaction effected 'for consideration'.

83 In that regard, EDM points out that the obligation assumed by each undertaking which is a member of the consortium to perform certain operations, to which a given value is attributed, is not such as to constitute consideration for the similar obligations assumed by the other undertakings which are members of the consortium. The services supplied are not consideration for each other, but are intended rather to achieve a common result. The values which the parties attribute to them are not determined in order to be paid. On the contrary, the purpose of the contract concluded between the members of the consortium is precisely that there should be no such payment, by stipulating that each undertaking is to perform the operations for which it is responsible. The said values serve therefore only as an economic measure of each undertaking's share. The result is that those operations cannot be described as transactions 'effected for consideration', either for a part equal to or lower than the share attributed to the undertaking concerned, or for the part exceeding that share.

84 The Commission observes that one of the limits of the scope of VAT, which encompasses all stages of the production, distribution and supply of services, is the determination that they are supplied for consideration, within the meaning of Article 2(1) of the Sixth Directive.

85 The operations performed by EDM in connection with the consortia of which it is a member should be regarded as an economic activity for the purposes of the Sixth Directive if the ultimate aim of those operations is the effecting of taxable transactions for consideration.

Findings of the Court

86 For VAT purposes, operations performed in connection with a consortium, for its account, by each of its members are not generally different from those carried out by an undertaking for its own account and should therefore be treated in the same way. As is clear from Article 2(1) of the Sixth Directive, VAT is chargeable only on the supply of goods and services effected for consideration. Therefore, in so far as supplies of goods and services are not effected for consideration for a third party, they cannot, as a rule, constitute taxable transactions, except, in particular, in the cases laid down in Article 6(2)(b) of the Sixth Directive.

87 In the main proceedings, it is clear from the order for reference and from the observations submitted to the Court that the operations carried out by the members of the consortia in question which correspond to the share contractually assigned to each of them are not paid for. In respect of those operations, no taxable transaction has therefore been effected.

88 Consequently, operations such as those at issue in the main proceedings, carried out by the members of a consortium in accordance with the provisions of a consortium contract and corresponding to the share assigned to each of them in that contract, do not constitute supplies of goods or services 'effected for consideration' within the meaning of Article 2(1) of the Sixth Directive, nor, consequently, a taxable transaction thereunder. The fact that such operations are carried out by the member of the consortium which manages it is irrelevant in that respect.

89 On the other hand, where the performance of more of the operations than the share thereof fixed by the said contract for a consortium member involves payment by the other members against the operations exceeding that share, those operations constitute a supply of goods or services 'effected for consideration' within the meaning of Article 2(1) of the Sixth Directive.

90 In that case, under Article 11A(1)(a) of the Sixth Directive, the taxable amount is the sum received by the consortium member concerned as payment for the part of the operations which exceeds its share as laid down in the consortium contract.

91 Therefore, the reply to the second question must be that operations such as those at issue in the main proceedings, carried out by the members of a consortium in accordance with the provisions of a consortium contract and corresponding to the share assigned to each of them in that contract, do not constitute supplies of goods or services 'effected for consideration' within the meaning of Article 2(1) of the Sixth Directive, nor, consequently, a taxable transaction under that directive. The fact that such operations are carried out by the member of the consortium which manages it is irrelevant in that respect. On the other hand, where the performance of more of the operations than the share thereof fixed by the said contract for a consortium member involves payment by the other members against the operations exceeding that share, those operations constitute a supply of goods or services 'effected for consideration' within the meaning of that provision.

Costs

92 The costs incurred by the Portuguese Government and by the Commission, which have submitted observations to the Court, are not recoverable. 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.

On those grounds,

THE COURT (Fifth Chamber),

in answer to the questions referred to it by the Tribunal Central Administrativo by order of 19 December 2000, hereby rules:

1.In a situation such as that in the main proceedings:

–activities which consist in the simple sale of shares and other securities, such as holdings in investment funds, do not constitute economic activities within the meaning of Article 4(2) 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, and therefore do not come within the scope of that directive;

placements in investment funds do not constitute supplies of services 'effected for consideration' within the meaning of Article 2(1) of Sixth Directive 77/388 and therefore likewise do not come within the scope thereof;

the amount of turnover relating to those transactions must consequently be excluded from the calculation of the deductible proportion referred to in Articles 17 and 19 of that directive;

–by contrast the annual granting by a holding company of interest-bearing loans to companies in which it has a shareholding and placements by that holding company in bank deposits or in securities, such as Treasury notes or certificates of deposit, constitute economic activities carried out by a taxable person acting as such within the meaning of Articles 2(1) and 4(2) of Sixth Directive 77/388;

however, the said transactions are exempted from value added tax under points 1 and 5 of Article 13B(d) of that directive;

in calculating the deductible proportion referred to in Articles 17 and 19 of Sixth Directive 77/388, those transactions are to be regarded as incidental transactions within the meaning of the second sentence of Article 19(2) thereof in so far as they involve only very limited use of assets or services subject to value added tax; although the scale of the income generated by financial transactions within the scope of Sixth Directive 77/388 may be an indication that those transactions should not be regarded as incidental within the meaning of that provision, the fact that income greater than that produced by the activity stated by the undertaking concerned to be its main activity is generated by such transactions does not suffice to preclude their classification as 'incidental transactions';

it is for the national court to establish whether the transactions concerned in the main proceedings involve only very limited use of assets or services subject to value added tax and, if so, to exclude interest generated by those transactions from the denominator of the fraction used to calculate the deductible proportion.

2.Operations such as those at issue in the main proceedings, carried out by the members of a consortium in accordance with the provisions of a consortium contract and corresponding to the share assigned to each of them in that contract, do not constitute supplies of goods or services 'effected for consideration' within the meaning of Article 2(1) of Sixth Directive 77/388, nor, consequently, a taxable transaction under that directive. The fact that such operations are carried out by the member of the consortium which manages it is irrelevant in that respect. On the other hand, where the performance of more of the operations than the share thereof fixed by the said contract for a consortium member involves payment by the other members against the operations exceeding that share, those operations constitute a supply of goods or services 'effected for consideration' within the meaning of that provision.

Jann

Timmermans

von Bahr

Delivered in open court in Luxembourg on 29 April 2004.
R. Grass

V. Skouris

Registrar

President

1 – Language of the case: Portuguese.