OPINION OF ADVOCATE GENERAL

MAZÁK

delivered on 26 October 2010 (1)

Case C?103/09

The Commissioners for Her Majesty's Revenue & Customs

v

Weald Leasing Limited

(Reference for a preliminary ruling from the Court of Appeal (England and Wales))

(Value added tax (VAT) – Sixth Council Directive 77/388/EEC – Concept of 'abusive practice' and 'normal commercial operations' – Transaction designed solely to obtain a tax advantage – Leasing and sub-leasing transactions intended to defer the payment of VAT – Redefinition of abusive practice)

I – **Introduction**

1. This reference for a preliminary ruling concerns, inter alia, the interpretation of the concept of 'abusive practice', as referred to in the judgment in Case C?255/02 *Halifax and Others*, (2) and its application in Case C?425/06 *Part Service* (3) and Case C?162/07 *Ampliscientifica and Amplifin* . (4) The reference was made in the course of proceedings between the Commissioners for Her Majesty's Revenue and Customs ('the Commissioners') and Weald Leasing Limited ('Weald Leasing') concerning the taxation of leasing transactions effected by the latter.

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

2. The Churchill Group of Companies ('the Churchill Group') predominantly supplies insurance services exempt from value added tax (VAT). (5) Churchill Management Limited ('CML') and its subsidiaries, Churchill Accident Repair Centre ('CARC') and Weald Leasing, (6) are members of the Churchill Group. CML and CARC have an input VAT recovery rate of about 1%, so that, when they purchase assets/equipment, they may deduct only 1% of the VAT on the purchase of those assets/equipment. (7) Weald Leasing's sole trading activity consists in purchasing the assets/equipment in question and then leasing them to Suas Limited ('Suas'). Weald Leasing is independently registered for VAT.

3. Suas is a company owned by a VAT consultant to the Churchill Group and his wife, but Suas is not part of that group and is separately registered for VAT. Suas' only significant trading activity is leasing assets from Weald Leasing and then subleasing them to CML and CARC.

4. When CML or CARC needed new equipment, it was purchased by Weald Leasing, which

leased it to Suas, which, in its turn, subleased it to CML or CARC. By resorting to that series of transactions CML and CARC avoided having to purchase directly the equipment they needed or pay in a single sum the total amount of non-deductible VAT on those purchases. The aim of those transactions was to divide and spread the payment of that amount in order to defer the Churchill Group's VAT liability. CML and CARC were not immediately liable for the non-deductible VAT on the total cost of the equipment purchased, but on the amount of rent relating to that equipment, spread over the term of the leasing agreements.

5. The Commissioners raised VAT assessments disallowing the deduction by Weald Leasing of the input VAT paid on the assets leased between October 2000 and October 2004, on the ground that the transactions in question were not economic activities and constituted an abuse of rights. Weald Leasing appealed against the assessments, arguing that those transactions had not been entered into solely to obtain tax advantages and that making taxable supplies of equipment by leasing was not contrary to the purpose of the Sixth Directive. After the judgment in *Halifax* (8) was delivered, the Commissioners abandoned their argument that the leasing transactions in question were not economic activities and argued only that those transactions constituted an abusive practice.

6. By decision of 7 February 2007, the VAT and Duties Tribunal held that the essential aim of those transactions was to obtain a tax advantage. Accordingly, those transactions satisfied the second condition for applying the doctrine of abuse, as set out in paragraph 75 of the Court's judgment in *Halifax*. In particular, the Tribunal stated that it did not find 'any of the explanations for the transactions other than the attainment of tax advantages by the Churchill VAT Group to be remotely convincing'. The VAT and Duties Tribunal found that the grant of the tax advantage was not contrary to the purpose of the relevant provisions in the Sixth Directive and that accordingly, the first condition set out in paragraph 74 of the Court's judgment in *Halifax* was not satisfied. The Tribunal could find nothing in the Sixth Directive to show that an exempt trader could not defer or spread the burden of input tax by leasing, even in situations such as this case where Weald Leasing was a company connected to CML and CARC. The VAT and Duties Tribunal held also that any abuse could only arise, not from the leases themselves, but from the level of rentals under the leases and from the arrangements to avoid a Direction from the Commissioners under Schedule 6 to the Value Added Tax Act 1994 ('the VAT Act 1994'). (9)

7. The Commissioners appealed against that decision to the Chancery Division of the High Court of Justice of England and Wales. The only issue on appeal was whether the tax advantage obtained by the Churchill Group was contrary to the purpose of the Sixth Directive. By judgment of 16 January 2008, the Chancery Division of the High Court of Justice of England and Wales dismissed the Commissioners' appeal against that decision, on the ground that the fact that the transactions in question were not carried out in the context of normal commercial operations was not sufficient to conclude that they were an abusive practice, since the tax advantage obtained by the Churchill Group by resorting to those transactions was not contrary to the principle of fiscal neutrality or to any other provision of the Sixth Directive. (10)

8. It was in those circumstances that the Court of Appeal of England and Wales (Civil Division) decided to stay the proceedings and to refer the following questions to the Court for a preliminary ruling:

‘(1) In circumstances such as those that exist in the present case, where a largely exempt trader adopts an asset leasing structure involving an intermediate third party, instead of purchasing assets outright, does the asset leasing structure or any part of it give rise to a tax advantage which is contrary to the purpose of the Sixth Directive within the meaning of paragraph 74 of the judgment in … *Halifax*?

(2) Having regard to the fact that the Sixth VAT Directive contemplates the leasing of assets by exempt or partly exempt traders, and having regard to the Court’s reference to “normal commercial operations” in paragraphs 69 and 80 of the judgment in *Halifax* and 27 of [the judgment in] … *Ampliscientifica* [*and Amplifin*] and also to the absence of any such reference in the judgment in … *Part Service*, is it an abusive practice for an exempt, or partly exempt, trader to do so even though in the context of its normal commercial operations it does not engage in leasing transactions?

(3) If the answer to Question 2 is yes:

(a) what is the relevance of “normal commercial operations” in the context of paragraphs 74 and 75 of the judgment in *Halifax*: is it relevant to paragraph 74 or to paragraph 75 or to both;

(b) is the reference to “normal commercial operations” a reference to:

(1) operations in which the taxpayer in question typically engages;

(2) operations in which two or more parties engage at arm’s length;

(3) operations which are commercially viable;

(4) operations which create the commercial burdens and risks typically associated with related commercial benefits;

(5) operations that are not artificial in that they have commercial substance;

(6) any other type or category of operations?

(4) If the asset leasing structure or any part of it is found to constitute an abusive practice, what is the appropriate redefinition? In particular, should the national court or the tax collecting authority:

(a) ignore the existence of the intermediate third party and direct that VAT be paid on an open market value of the rentals;

(b) redefine the leasing structure as an outright purchase; or

(c) redefine the transactions in any other way which either the court or the tax collecting authority considers to be an appropriate means by which to re-establish the situation that would have prevailed in the absence of the transactions constituting the abusive practice?’

III – **Proceedings before the Court**

9. Written observations were submitted by Weald Leasing, the Greek Government, Ireland, the Italian Government, the United Kingdom Government and the Commission. All, except the Italian Government, presented oral submissions at the hearing held on 3 June 2010.

IV – **Preliminary remarks**

10. Following the judgment of the Court in *Halifax*, it is clear that the abuse of law principle, as established by the case-law of the Court and which prevents European Union (EU) law being relied on for abusive or fraudulent purposes, also applies in VAT cases. However, the extension of the abuse of law principle to the sphere of VAT law may not impinge on the principle of legal certainty or on a trader's freedom to structure its business or opt for transactions in order to incur less VAT. (11)

11. Given that a finding of abuse of law in the field of VAT arises notwithstanding the fact that a trader has formally complied with the letter of the VAT legislation, I consider that the principle in question must be applied only in exceptional cases where the abuse is evident and any remedies must be applied in a parsimonious manner solely to the extent of the abuse in question. The Court stated in *Halifax* that in the absence of a clear and unambiguous legal basis, a penalty may not be imposed for a finding of abusive practice. (12) Rather, transactions involved in an abusive practice must be redefined so as to re-establish the situation that would have prevailed in the absence of the transactions constituting that abusive practice. (13)

12. In the judgment in *Halifax*, the Court laid down a two-part test which must be satisfied in order to find an abusive practice. First, the transactions concerned, notwithstanding the formal application of the conditions laid down by the relevant provisions of the Sixth Directive and the national legislation transposing it, result in the accrual of a tax advantage the grant of which would be contrary to the purpose of those provisions. Second, it must also be apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain a tax advantage. (14)

13. The two part test in question is, as submitted by the Greek Government, cumulative in nature. In order to establish the existence of an abusive practice for VAT purposes it is thus not sufficient to prove that a particular transaction results in the accrual of a tax advantage or even that the transaction is essentially aimed at, or has no rational or explanation other than, obtaining such an advantage. To find otherwise would impinge notably on a trader's recognised freedom to limit its tax liability. (15) It is therefore necessary to go further and establish that the transaction results in a tax advantage which would be contrary to the purpose of the Sixth Directive and the national legislation transposing it.

14. It would appear from the order of reference that the second part of the Halifax test has been satisfied in the main proceedings as the VAT and Duties Tribunal held that the essential aim of the relevant leasing and sub-leasing arrangements in the main proceedings was to obtain a tax advantage. According to the order for reference, the arrangements resulted, inter alia, in a cash flow advantage to CARC and CML.

15. The order for reference also states that in that context the rents under the leases were kept low because the higher the rent, the higher the irrecoverable VAT suffered by CML and CARC. Moreover, it would appear from the order for reference that under the leasing agreement between Weald Leasing and Suas, the rent payable on the assets was calculated so as to pay back 100 per cent of the cost to Weald Leasing in 10 years, irrespective of the expected life of the specific assets/equipment in question.

V – **The first and fourth questions**

16. The referring court by its first question asks in essence if the arrangements as set out above or any part thereof result in the accrual of a tax advantage the grant of which would be contrary to the purpose of the Sixth Directive and the national legislation transposing it.

17. Weald Leasing claims that in the context of VAT, one of the tax advantages of leasing for exempt or partly exempt traders is the ability to spread irrecoverable input tax over the duration of the lease. However, this tax advantage is not, of itself, sufficient to render the transactions abusive as it is simply the fiscal effect of their choice which is specifically contemplated by the Sixth Directive. It is not abusive as it has not been obtained wrongfully. In particular, there was no attempt by CML and CARC to recover any more input tax than that to which they are entitled. Whilst Weald Leasing obtained a cash flow advantage there was no outright saving of tax and nor was such a saving intended. According to Weald Leasing this is a key distinguishing feature between the present case and *University of Huddersfield* (16) as the only element of the leasing arrangements which might be regarded as potentially abusive is the level of the rentals. Weald Leasing notes that the only legislative provision that might potentially have been contravened is paragraph 1, Schedule 6, to the VAT Act 1994 which is a domestic law provision which does not transpose a provision of the Sixth Directive. Rather, it is an exception to the basic rule of valuation in Article 11A(1) of the Sixth Directive, made pursuant to a derogation granted to the United Kingdom in accordance with Article 27(2) of that directive. Such derogations do not give rise to Community (and now EU) law rights or obligations. (17) Consequently, the EU law doctrine of abuse does not apply to any contravention of paragraph 1, Schedule 6, which is a matter solely for domestic law.

18. The United Kingdom Government considers that despite the formal appearance of leasing, the arrangements in question were not at arm’s length and were a contrived and artificial attempt to disguise the true underlying commercial and economic reality which was that the Churchill Group of companies, through CML and CARC, selected and bought assets for use in its exempt insurance business. Weald Leasing sought in effect to secure the VAT advantages of leasing without carrying the associated economic and commercial burdens. The Greek Government considers that the leasing scheme in question had as its purpose and effect that acquisitions of assets by CARC and CML were taxed differently from similar acquisitions by their competitors providing similar services. The application of this scheme infringes the principle of fiscal equality and, by extension, the principle of fiscal neutrality. Ireland considers that the Churchill Group supplies 99% exempt services and to the extent that its input tax is not deductible the Sixth Directive must be seen as providing that the burden of paying this tax be assumed immediately upon its becoming chargeable, in order that it be passed on to the ultimate consumer. Weald Leasing and Suas are principally, if not solely, mechanisms for avoiding this and, being manifestly artificial, constitute an abuse. Ireland claims that all or most of the leasing arrangements are artificial and thus abusive and not simply the level of rental payments. The Italian Government considers that a leasing structure intended to enable a predominantly exempt taxable person to deduct the full amount of input VAT paid on goods or services purchased for its business is contrary to the principle of the fiscal neutrality of VAT enshrined in the Sixth Directive.

19. The Commission considers that the leasing of assets does not give rise to a tax advantage contrary to the purpose of the VAT legislation. There is no difference in economic terms for the State whether the assets are purchased or leased. While the deferral of the tax burden may be considered by the taxpayer to provide a cash flow advantage, he pays for that advantage in the long run. The Commission also considers that the use of a captive leasing company does not in itself constitute an abuse of law. The real risk of abuse in such circumstances lies in the opportunity for the taxpayer to manipulate the amount of the lease payments in order to reduce the amount of VAT paid. The Commission notes that the intervention of Suas appears to have had the sole purpose of preventing the tax authorities from verifying and reviewing the calculation of the taxable amount. That transaction would thus appear to fulfil the first part of the Halifax test. A transaction aimed at preventing the effective enforcement of the VAT rules must be regarded as equivalent to one aimed at obtaining an advantage contrary to the purpose of those rules.

20. In my view, and as submitted by the Commission in its observations, a trader is free, in principle, to choose whether to purchase or lease assets/equipment (18) for use in the course of its business. Moreover, the fact that an exempt trader chooses to enter into a leasing arrangement in respect of assets/equipment rather than purchase them outright in order to benefit from a more favourable treatment under VAT legislation, by deferring (19) its VAT burden is not, in itself, sufficient to support the finding that an abuse of that legislation has occurred. Where a trader chooses to lease equipment it pays VAT on the periodic rental payments made over the duration of the lease rather than a once-off payment of VAT on the purchase of that equipment. I consider that such a transaction is not in itself contrary to the purpose of the Sixth Directive and the national legislation transposing it. In my view, the transaction does not necessarily infringe the principle of fiscal neutrality. As Weald Leasing and the Commission indicated, the lease rather than the purchase of equipment does not in itself result in the trader paying less VAT or deducting more VAT than that to which a trader is entitled. Thus while there may be cash flow advantages for the trader, there is no inherent VAT saving in leasing rather than purchasing equipment.

21. I consider that the setting-up and use of a wholly owned or ‘captive’ subsidiary, in this case Weald Leasing, which for VAT purposes is a separate or independent taxpayer, (20) with the sole purpose of obtaining a VAT advantage in the form of a deferral of VAT is not per se abusive, as such an advantage could be obtained by entering into an arm’s length leasing arrangement with an unrelated third party. (21) Thus, the adoption of an asset leasing structure involving an unrelated third party or a wholly owned subsidiary which is independently registered for VAT by a largely exempt trader instead of purchasing assets outright in order to defer the payment of irrecoverable tax does not in itself give rise to a tax advantage which is contrary to the purpose of the Sixth Directive. Where, however, the rental payments under the leasing arrangements are set at artificially low levels, which do not reflect open market conditions, thereby in turn artificially reducing the amount of VAT payable, that part of the transaction relating to the level of payments rather than the lease itself would, in my view, be contrary to the purpose of the Sixth Directive and the national legislation transposing it.

22. As regards the arrangements concerning Suas, the order for reference states that the interposition of that company between Weald Leasing and CARC and CML meant that the Commissioners were unable to make a Schedule 6 direction (VAT Act 1994). It would appear, subject to verification by the referring court, that in order for the Commissioners to make a Schedule 6 direction, thereby entailing that the value of a supply is calculated at its open market value, the Commissioners must demonstrate, inter alia, that the person making the supply and the person to whom it is made are connected (22) and that the supply was at less than its open market value.

23. It appears from the order for reference that Weald Leasing itself argued before the referring court that '[t]he real tax advantage obtained by the participants arose from the interposition of Suas, thereby preventing a Schedule 6 Direction'. In its submissions to the Court, Weald Leasing considers that the abuse principle only applies to tax advantages which are contrary to Community law provisions and not to attempts to circumvent domestic law.

24. I consider that Weald Leasing's submission cannot be accepted. It would appear from the file before the Court, and subject to verification by the referring court, that paragraph 1, Schedule 6, of the VAT Act 1994 was enacted pursuant to a derogation under Article 27 of the Sixth Directive. (23) In my view, provisions of national legislation which were adopted in accordance with the derogations laid down in Article 27 of the Sixth Directive form an integral part of the national VAT system, are binding on a taxable person under national law (24) and may be relied upon by the tax authorities of a Member State before the national courts against that person. (25) For the purposes of the application by the national courts of the abuse principle as laid down in *Halifax*, any distinction between national provisions which implement the provisions of the Sixth Directive and those which were adopted in full compliance with a derogation permitted under that directive is, in my view, contrived and tends to undermine the integrity of the national VAT system and indirectly the EU VAT system.

25. I therefore consider that the doctrine of abuse as laid down in *Halifax* (26) applies to abuses of national provisions which were adopted in full compliance with the terms of Article 27 of the Sixth Directive. As regards the application of that principle in the main proceedings which is a matter for the national court, I consider that the use of a purely artificial structure essentially designed in order to gain a tax advantage by preventing tax authorities from directing in accordance with the provisions of national law adopted in full compliance with the Sixth Directive that the value of leasing arrangements between connected persons be taken to be their open market value is an abusive practice.

26. By its fourth question, the referring court seeks guidance on how to redefine the arrangements in the event that the asset leasing structure or any part of it is found to constitute an abusive practice.

27. The Court at paragraph 94 of the judgment in *Halifax* stated that transactions involved in an abusive practice must be redefined so as to re-establish the situation that would have prevailed in the absence of the transactions constituting that abusive practice. It follows from my assessment of the first question as regards the existence and extent of the abuse in the main proceedings that if the national court finds that the interposition of Suas in the relevant arrangements was artificially orchestrated essentially for the purpose of preventing a Paragraph 1, Schedule 6, direction (VAT Act 1994) in order to gain a tax advantage, the United Kingdom tax authorities should be entitled, as indicated by the Commission in its submissions, to treat the series of transactions in the main proceedings as leases by Weald Leasing to CML and CARC thereby ensuring that VAT is paid on an open market valuation (27) of those leases.

28. Thus, where a purely artificial structure is adopted in leasing arrangements in order to prevent tax authorities from directing, in accordance with the provisions of national law adopted in full compliance with a derogation permitted under the Sixth Directive, that the value of those arrangements between connected persons be taken to be their open market value, those arrangements should be redefined by ignoring the presence of that structure.

VI – **The second and third questions**

29. By its second question the referring court asks whether it is an abusive practice for an

exempt, or partly exempt, trader to engage in the leasing of assets even though in the context of its ‘normal commercial operations’ it does not do so. By its third question the referring court asks a number of questions concerning the interpretation and application of the terms ‘normal commercial operations’.

30. The expression ‘normal commercial operations’ is used in two paragraphs of the *Halifax* judgment. At paragraph 69 of the judgment in *Halifax*, the Court enunciated a broad principle that transactions which are not carried out in the context of normal commercial operations will be considered abusive where their purpose is to wrongfully obtain an advantage provided for by EU law. At paragraph 80 of that judgment, the Court stated that ‘[t]o allow taxable persons to deduct all input VAT even though, in the context of their normal commercial operations, no transactions conforming with the deduction rules of the Sixth Directive or of the national legislation transposing it would have enabled them to deduct such VAT, or would have allowed them to deduct only a part, would be contrary to the principle of fiscal neutrality and, therefore, contrary to the purpose of those rules’. The Court then stated at paragraph 81 of *Halifax* that ‘[a]s regards the second element [of the two part test], whereby the transactions concerned must essentially seek to obtain a tax advantage, it must be borne in mind that it is the responsibility of the national court to determine the real substance and significance of the transactions concerned. In so doing, it may take account of the purely artificial nature of those transactions and the links of a legal, economic and/or personal nature between the operators involved in the scheme for reduction of the tax burden’.

31. The reference to ‘normal commercial operations’ is however absent in the *Part Service* judgment (28) despite the Court’s reliance on the two part test laid down in paragraphs 74 and 75 of *Halifax*. (29) In the judgment in *Ampliscientifica and Amplifin* (30) the Court stated at paragraphs 27 and 28 that ‘the principle prohibiting the abuse of rights is intended to ensure, particularly in the field of VAT, that [EU] legislation is not extended to cover abusive practices by economic operators, that is to say transactions carried out not in the context of normal commercial operations, but solely for the purpose of wrongfully obtaining advantages provided for by [EU] law. The effect of that principle is therefore to prohibit wholly artificial arrangements which do not reflect economic reality and are set up with the sole aim of obtaining a tax advantage.’

32. I consider that the terms ‘normal commercial operations’ do not require an examination of the ‘typical’ business activity of a particular trader. (31) Thus the concept of ‘normal commercial operations’ in the context of VAT abuse is unrelated to the operations a taxpayer habitually engages in. An attempt to distil the typical or habitual commercial operations of a given trader is, in my view, an inherently unpredictable exercise (32) and thus unworkable in a tax law context where legal certainty is required.

33. An assessment of whether a transaction is carried out in the context of ‘normal commercial operations’ refers, in my view, to the second part (33) of the two part test laid down in *Halifax* and thus the nature of the transaction or scheme in question and whether it is a purely artificial construct established essentially in order to obtain a tax advantage rather than for other commercial reasons. (34) In that regard, the links of a legal, economic and/or personal nature between the operators involved in the scheme for reduction of the tax burden (35) are relevant and thus whether the parties to the transaction operate at arm’s length. (36) Moreover, the question whether a transaction gives rise to commercial burdens and risks typically associated with such transactions is relevant to the assessment of the artificial nature of the transaction and thus whether its essential aim is to obtain a tax advantage. I would note in addition that it is the objective nature of the transaction (37) which is relevant in such an assessment rather than the subjective motivation of the taxpayer.

VII – **Conclusion**

34. In the light of the foregoing observations, I propose that the Court should answer as follows the questions referred by the Court of Appeal (England and Wales):

(1) The adoption of an asset leasing structure involving an unrelated third party or a wholly owned subsidiary which is independently registered for value added tax by a largely exempt trader instead of purchasing assets outright in order to defer the payment of irrecoverable tax does not in itself give rise to a tax advantage which is contrary to the purpose 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.

(2) The use of a purely artificial structure essentially designed in order to gain a tax advantage by preventing tax authorities from directing in accordance with the provisions of national law adopted in full compliance with Sixth Directive 77/388 that the value of leasing arrangements between connected persons be taken to be their open market value is an abusive practice.

(3) Where an abusive practice has been found to exist, the transactions involved must be redefined so as to re-establish the situation that would have prevailed in the absence of the transactions constituting that abusive practice. Where a purely artificial structure is adopted in leasing arrangements essentially in order to prevent tax authorities from directing that the value of those arrangements between connected persons be taken to be their open market value, those arrangements should be redefined by ignoring the presence of that structure.

(4) The concept of 'normal commercial operations' in the context of value added tax abuse is unrelated to the operations a taxpayer typically or habitually engages in. An assessment of whether a transaction is carried out in the context of 'normal commercial operations' refers to the nature of the transaction or scheme in question and whether it is a purely artificial construct established essentially in order to obtain a tax advantage rather than for other commercial reasons. The links of a legal, economic and/or personal nature between the operators involved in the scheme for reduction of the tax burden and thus whether the parties to the transaction operate at arm's length, the question whether a transaction gives rise to commercial burdens and risks typically associated with such transactions are relevant for the purpose of assessing the nature of the transaction.

1 – Original language: English.

2 – [2006] ECR I?1609 ('*Halifax*').

3 – [2008] ECR I?897.

4 – [2008] ECR I?4019.

5 – See Article 13.B 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') which provides, inter alia, that Member States shall exempt insurance transactions. See now Article 135(1) of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ 2006 L 347, p. 1) ('the VAT Directive').

6 – Weald Leasing is a wholly owned subsidiary of CML and is independently registered for VAT.

7 – See Article 17(2) and (5) of the Sixth Directive, see now Articles 168 and 173 of the VAT

Directive.

8 – Cited in footnote 2.

9 – Paragraph 1(1) in Schedule 6 to the VAT Act 1994 provides:

‘Where –

(a) the value of a supply made by a taxable person for a consideration in money is (apart from this paragraph) less than its open market value, and

(b) the person making the supply and the person to whom it is made are connected, and

(c) if the supply is a taxable supply, the person to whom the supply is made is not entitled under sections 25 and 26 to credit for all the VAT on the supply,

the Commissioners may direct that the value of the supply shall be taken to be its open market value.’

10 – The High Court accepted the Commissioners’ submission that CML, CARC, Weald Leasing and Suas did not bear the ordinary economic and commercial risks typically associated with the leasing of assets. It accepted that the leasing arrangements were ‘commercially hollow’ because they were so different from what might be expected of parties dealing at arm’s length and concerned to behave as if in the course of normal commercial operations. It also accepted that although the leasing arrangements were not shams and despite attempts to confer the outer appearances of familiar commercial arrangements, the transactions were artificial in the sense that but for having the essential aim of obtaining a tax advantage, they would never have been made in any commercial context. Accordingly, the High Court accepted that the transactions fell outside the parties’ normal commercial operations. However, after referring to paragraphs 69 to 80 of the Court’s judgment in *Halifax* (cited in footnote 2), the Judge concluded that just because a scheme fell outside normal commercial operations, that did not mean that it amounted to an abusive practice. In that context, the Judge observed that the Court did not refer to ‘normal commercial operations’ either in paragraph 74 or in paragraph 86 of its judgment when setting out the first condition for application of the principle of abuse. He concluded that if the Court had intended the references to ‘normal commercial operations’ in paragraphs 69 and 80 of its judgment in *Halifax* to be important, the Court would have explained further what it meant by this term.

11 – See the judgment in *Halifax* (cited in footnote 2), paragraphs 69 to 73.

12 – See *Halifax*, cited in footnote 2, paragraph 93.

13 – See *Halifax*, cited in footnote 2, paragraph 94.

14 – See *Halifax*, cited in footnote 2, paragraphs 74 and 75.

15 – See *Halifax*, cited in footnote 2, paragraph 73.

16 – Case C?223/03 [2006] ECR I?1751.

17 – Case C?309/06 *Marks & Spencer* [2008] ECR I?2283, paragraph 28.

18 – The lease of equipment constitutes, in principle, a supply of services pursuant to Article 6(1) of the Sixth Directive and Article 24(1) of the VAT Directive.

19 – I would note by contrast that Ireland states in its written pleadings that the principle of fiscal

neutrality requires that a person who is not entitled to deduct tax when it becomes chargeable should be liable to bear the burden of its non-deductibility by paying it at that point in time.

20 – Pursuant to Article 4 of the Sixth Directive a taxable person means any person who independently carries out in any place any economic activity whatever the purpose or result of that activity.

21 – See by analogy, Case C?23/98 *Heerma* [2000] ECR I?419. In that case the Court held that a member of a partnership which let immovable property to the partnership of which he is a member and which is itself a taxable person acts independently within the meaning of Article 4(1) of the Sixth Directive. The Court noted that there was no relationship of employer and employee similar to that mentioned in the first subparagraph of Article 4(4) of the Sixth Directive between the partnership and the partner which would preclude the independence of the partner. The partner, in letting tangible property to the partnership, acted in his own name, on his own behalf and under his own responsibility, even if he was at the same time manager of the lessee partnership. It follows therefore in my view that the mere existence of a close relationship between two separate taxpayers is not sufficient for the tax authorities to treat those taxpayers as one. See by contrast, Case C?355/06 *van der Steen* [2007] ECR I?8863. The Court found in that case that there was a relationship of employer/employee between a company and a director of that company. The Court found firstly that the company paid the director a fixed monthly salary and annual holiday payment. The company deducted income tax and social security contributions from his salary. Secondly, at the time of providing services in his capacity as employee, the director did not act in his own name, on his own behalf and under his own responsibility, but on behalf and under the responsibility of the company. Thirdly the director did not bear any economic business risk in acting as manager and performing the work in the course of the company's dealings with third parties.

22 – It would appear from the file that if the leasing arrangements in question had not involved Suas, which is not part of the Churchill Group and is not formally connected to Weald Leasing or CARC or CML, the national tax authorities would have been able to direct that the value of the supplies in question be taken at their open market value.

23 – Article 27(1) of the Sixth Directive provides that '[t]he Council, acting unanimously on a proposal from the Commission, may authorise any Member State to introduce special measures for derogation from the provisions of this Directive, in order to simplify the procedure for charging the tax or to prevent certain types of tax evasion or avoidance …'. The procedure for such an authorisation is laid down in Article 27(2) to (4) of the Sixth Directive. Pursuant to Article 27(5) '[t]hose Member States which apply on 1 January 1977 special measures of the type referred to in paragraph 1 above may retain them providing they notify the Commission of them before 1 January 1978 and providing that where such derogations are designed to simplify the procedure for charging tax they conform with the requirement laid down in paragraph 1 above'.

24 – See by analogy, *Marks & Spencer*, cited in footnote 17, paragraphs 20 to 28. In my view, that judgment provides that a taxpayer does not derive a directly enforceable EU law right in respect of exemptions or derogations adopted by a Member State in compliance with the Sixth Directive. See, however, Advocate General Kokott's Opinion in that case where she effectively states that a taxpayer derives both a national law and an EU law right (point 43 of the Opinion).

25 – See, by analogy, Case 5/84 *Direct Cosmetics* [1985] ECR 617, paragraph 37.

26 – Cited in footnote 2.

27 – *Halifax*, cited in footnote 2. An assessment of the open market value of a leasing

arrangement necessarily implies taking into consideration the duration of those arrangements in the light of the nature of the assets/equipment in question.

28 – Cited in footnote 3.

29 – Cited in footnote 2.

30 – Cited in footnote 4.

31 – Despite the inclusion of the terms ‘*their* normal commercial operations’ (emphasis added) at paragraph 80 of the *Halifax* judgment (cited in footnote 2).

32 – Not least because a trader’s business operations may change and evolve over time.

33 – See therefore paragraph 75 of *Halifax* (cited in footnote 2).

34 – The referring court used the terms ‘commercially viable’ in its question 3(2)(3). As that term could be interpreted as meaning a transaction which is profitable in nature, I shall avoid using that term.

35 – See *Halifax* (cited in footnote 2), paragraph 81.

36 – In my view, the referring court must examine and weigh all the applicable contractual terms and relevant circumstances.

37 – See paragraph 75 of *Halifax* (cited in footnote 2).