European Union / Italy

VAT Grouping in Italy and the *Skandia* Judgment

Marco Abramo Lanza
Marco Zanetti[*]

Issue: International VAT Monitor, 2018 (Volume 29), No. 3
Published online: 19 April 2018

From 1 January 2019, taxable persons established in Italy can be part of an Italian VAT group. In this article, the authors analyse how the ECJ decision in the *Skandia* case and the Guidelines of the VAT Committee published by the European Commission in relation to that decision have had an impact on the Italian VAT legislation. The authors also discuss possible scenarios in which Italian branches or main establishments can be involved in the future and to which the *Skandia* case and the Guidelines will be applicable.

1. Introduction

Based on article 11 of the VAT Directive,[1] the Italian legislator adopted new VAT-grouping provisions at the end of 2016,[2] together with the Budget Law for 2017.[3] They entered into effect on 1 January 2018. Nevertheless, it will only be possible to create a VAT group in Italy with effect from 2019.[4]

Importantly, the Budget Law for 2018[5] (definitively approved by the Italian Parliament at the end of December 2017) has, inter alia, already modified the new VAT-grouping provisions in order to directly transpose the outcome of the Court of Justice of the European Union's (ECJ) decision in *Skandia* [6] in the upcoming domestic legislation.[7]

In this article, the authors analyse how the ECJ decision in *Skandia* and the Guidelines of the VAT Committee (the Guidelines), published by the European Commission in relation to that decision,[8] have had an impact on the Italian VAT legislation. The authors further discuss possible scenarios in which Italian branches or main establishments can be involved in the future, to which the *Skandia* case and the Guidelines (as implemented by the Italian VAT rules) will be applicable.

2. VAT Grouping in Italy

2.1. VAT group

Pursuant to the Italian VAT-grouping provisions and in accordance with article 11 of the VAT Directive, taxable persons that are closely bound to one another on account of specific financial, economic and organizational links (e.g. connected to the activities carried out or to the company exercising the control),[9] are established in Italy and belong to a group (of companies) will be able to constitute a VAT group according to the "all-in, all-out" principle.[10]

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* **Marco Lanza is Partner in Studio Biscozzi Nobili, legal and tax firm in Milan. Marco Zanetti is Senior Associate in Studio Biscozzi Nobili, legal and tax firm in Milan.**
The authors point out that, during the publication of the current article in International VAT Monitor 3 (2018), the Ministerial Decree containing the detailed implementing provisions for the Italian VAT grouping was issued on 6 April 2018, as communicated on 10 April 2018 on the website of the Italian Ministry of Economy and Finance. As at 12 April 2018, the Decree had not been published on the Official Gazette yet. The authors will comment on significant changes of their conclusions (if any) deriving from such provisions in a future contribution.

1. Council Directive 2006/112/EC of 28 November 2006 on the Common System of Value Added Tax, art. 11, OJ L347 (2006), EU Law IBFD [hereinafter VAT Directive].
2. The Italian VAT-grouping provisions are contained in the new Title V-bis (entitled *Gruppo IVA*, i.e. VAT group) of the Italian VAT Law (IT: Presidential Decree 633 of 26 Oct. 1972, National Legislation IBFD, introduced by art. 1, item 24 of IT: Law No. 232/2016 (Budget Law for 2017) and modified by the Budget Law for 2018.
3. In any case, a specific Ministerial Decree will have to be issued, containing the detailed implementing provisions for the regime under discussion.
4. In fact – as pointed out in sec. 2.1. – the related rules enter into force starting from 1 Jan. 2018, but a VAT group will be able to operate at the earliest in 2019, provided that the related option is exercised no later than 30 Sept. 2018.
5. IT: Law No. 205 of 27 December 2017 (Official Gazette No. 302 of 29 December 2017).
6. 6 SE: ECJ, 17 Sept. 2014, Case C-7/13, *Skandia America Corporation USA, filial Sverige v. Skatteverket*, ECJ Case Law IBFD.
7. Under art. 1, item 984 of the Budget Law for 2018, items 4-bis-4-sexies have been added to art. 70-quinquies of Presidential Decree 633.
8. The Guidelines of the VAT Committee (the Guidelines) can be found at the following link: https://ec.europa.eu/food/sites/food/files/safety/docs/fw_lib_guidelines-vat-committee_en.pdf.
9. The links required in order to constitute an Italian VAT group are provided for in art. 70-ter of Presidential Decree 633.
10. Due to the "all-in, all-out" principle, the new rules have provided that some negative effects will be produced for VAT groups in the case that one of the taxable persons for which the required links were in place did not exercise the option for the VAT group itself. First of all, the fiscal advantage already obtained by the VAT group will be recaptured. In addition, the VAT group will end starting from the year following the one when the said missed option is assessed, unless those taxable persons actually opt to join the VAT group (in this respect, *see* art. 70-quater of Presidential Decree 633).

As further detailed in the Italian Civil Code,[11] a "financial link" exists when two or more taxable persons established in Italy, pursuant to the relevant provisions of the Italian Civil Code and at least from 1 July of the calendar year preceding the setting up of the VAT group (i) are directly or indirectly linked by controlling interests; or (ii) are directly or indirectly controlled by the same entity, provided that it is established in the Italian territory or in a state that has signed an agreement that ensures an effective exchange of information with Italy.

An "economic link" exists when two or more taxable persons carry out at least *one* of the following types of "economic cooperation":

- the same main business activity;
- complementary or interdependent activities; or
- activities that positively affect, fully or partially, one or more of the taxable persons.

An "organizational link" exists in cases of "coordination" (i.e. when an entity can exercise a stable influence on the management of other companies in order to have a single direction within a group) between two or more taxable persons, resulting (i) "by law";[12] or (ii) "as a matter of fact" between the decision-making bodies of the same entities, even though such coordination is performed by another entity.

As a general rule, if the financial link exists, it is assumed that the economic and organizational links also exist.

From a subjective point of view, the following are not allowed by law to join a VAT group:[13]

- seats and branches established abroad;
- persons whose company is under seizure;
- persons subject to insolvency proceedings; and
- persons under winding-up procedure.

In practice, in order to exercise the option to become a VAT group, the representative[14] of the group needs to submit a statement with the main data of the VAT group and of the participants by electronic means. With regard to the validity of the option,[15] if it is submitted between 1 January and 30 September, it will be effective starting from the following year, while if submitted between 1 October and 31 December, it will be effective starting from the year after the following year. The option is binding for a 3-year period and is automatically renewed for each subsequent year, unless it is revoked.

Once set up, the Italian VAT group is treated as a single taxable person with a sole VAT identification number. As such, it is liable for all the VAT obligations and is able to exercise all the rights deriving from the members of the VAT group.[16]

In addition, the VAT group (and not its participants) will determine its periodical output and input VAT, will submit the VAT return and, if due, remit the VAT amount to the tax authorities.[17]

One of the main consequences of forming a VAT group is that the supplies of goods and services among the participants of the VAT group are outside the scope of VAT, while the same supplies carried out by or towards any of the participants will be respectively deemed carried out by or towards the VAT group.

A significant clarification regarding the application of this no-supply principle was brought by the ECJ in *Skandia*. As clarified by the Court (and these are the clarifications recently introduced by the Budget Law for 2018[18] on the provisions related to the VAT grouping in Italy):

- the supplies of goods and services carried out by an Italian main establishment or an Italian branch *belonging to an Italian VAT group* to one of the main establishment's branches or the branch's main establishment established abroad are deemed carried out by the Italian VAT group to a subject not part of it;
- the supplies of goods and services carried out to an Italian main establishment or an Italian branch *belonging to an Italian VAT group* by one of the main establishment's branches or the branch's main establishment established abroad are deemed carried out to the Italian VAT group by a subject not part of it;

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11. Reference is made in particular to art. 2359, para. 1, no. 1 of the Italian Civil Code, according to which, "the following are considered to be controlled companies: companies in which another company has the majority of votes that may be cast in General Meeting of Shareholders […]".
12. As provided for by the fifth book, title V, head IX, of the Italian Civil Code. Art. 2497-sexies of the Italian Civil Code provides that "it is assumed, unless otherwise proven, that the management and coordination activity of companies is performed by the company or entity required to consolidate their financial statements or that controls them, in accordance with article 2359".
13. Art. 70-bis of Presidential Decree 633.
14. In principle, the "representative", i.e. the taxable person executing the VAT obligations and exercising the VAT rights for the VAT group, is the subject exercising the control on the basis of the financial link (mentioned in this section (sec. 2.1.) (art. 70-septies of Presidential Decree 633).
15. Art. 70-quater of Presidential Decree 633.
16. Art. 70-quinquies of Presidential Decree 633.
17. Specific rules are provided for with reference to the VAT credits of the participants resulting from their VAT returns relating to the year previous to their joining the VAT group (art. 70-sexies of Presidential Decree 633).
18. *See* the new items 4-bis to 4-sexies inserted into art. 70-*q*uinquies of Presidential Decree 633 by art. 1, item 984 of Law No. 205 of 27 December 2017.

- the supplies of goods and services carried out to a main establishment or a branch *belonging to a VAT group established in another Member State* by one of the main establishment's branches or the branch's main establishment established in Italy are deemed carried out to the VAT group established in the other Member State by a subject not part of it; and
- the supplies of goods and services carried out by a main establishment or a branch *belonging to a VAT group established in another Member State* to one of the main establishment's branches or the branch's main establishment established in Italy are deemed carried out by the VAT group established in the other Member State to a subject not part of it.

For these four categories of transactions, the taxable basis for VAT purposes is determined, in the presence of a consideration, not only according to the general rules (and so, in principle, on the basis of the contractual conditions), but also considering the rules specifically foreseen for transactions carried out between related entities, i.e. belonging to the same group (the notion of "group" relevant here is the legal/civil law group; no reference is made to the notion of "VAT group" as defined in section 1.).[19]

More precisely:

- for *taxable* transactions carried out to a subject having a reduced right to the deduction of VAT, the taxable basis is represented by the fair value of the goods and services supplied in the case that the parties negotiated a lower consideration *and* the transactions are carried out by companies that directly or indirectly control the buyer/recipient, are controlled by the buyer/recipient or are controlled by the same company controlling the said subject;
- for *exempt* (*with no right* to deduction) transactions carried out by a subject having a reduced right to the deduction of VAT, the taxable basis is represented by the fair value of the goods and services supplied in the case that the parties negotiated a lower consideration *and* the transactions are carried out to companies that directly or indirectly control the supplier, are controlled by the supplier or are controlled by the same company controlling the said subject; and
- for *taxable* (and for the exempt *with a right* to deduction) transactions carried out by a subject having a reduced right to the deduction of VAT, the taxable basis is represented by the fair value of the goods and services supplied in the case that the parties negotiated a higher consideration *and* the transactions are carried out to companies that directly or indirectly control the supplier, are controlled by the supplier or are controlled by the same company controlling the said subject.

The application of these rules in transactions involving VAT groups are meant to avoid that the very strict link existing between a branch and its main establishment could influence the amount of the consideration when either the branch or its main establishment are participating (in Italy or in another Member State) in a VAT group and the other entity involved in the transaction (either the main establishment or the branch) is established in a different country.[20]

Moreover, even if it is not specifically provided for by the law, the same provisions regarding the taxable basis could be applicable (but a confirmation by the tax authorities would be necessary in this respect) also in the cases that the branch and its main establishment are part of two VAT groups, namely one in Italy and the other in another Member State.

As noted in this section, the new rules related to the Italian VAT grouping introduced by the Budget Law for 2018 (those transposing *Skandia*'s principles and those related to the taxable basis) entered into force on 1 January 2018, but an Italian VAT group can be created at the earliest in 2019. One may then wonder why the new rules entered into force in 2018 already. The answer is that these rules should already apply from 1 January 2018, only limited to the transactions between a branch or a main establishment established in Italy and its main establishment or its branch established in another Member State belonging to a VAT group in its state of establishment.

2.2. VAT group calculation (*IVA di gruppo*)

While VAT-grouping provisions in the sense of article 11 of the VAT Directive were only adopted in 2018, it is important to underline that the Italian VAT legislation has also been providing for a long time for specific rules regulating the so-called "*IVA di gruppo*".[21] According to the *IVA di gruppo* rules, provided that the relevant conditions are met,[22] the companies belonging to a group can choose to opt for the (simple) offsetting of their VAT positions (credit or debt).

A major difference between businesses joining a VAT group and those forming an *IVA di gruppo* is that the latter maintain their independence, not only from a legal point of view but also from a VAT point of view. In fact, each of them continues operating with its own VAT identification number, each has the obligation to determine its periodical output and input VAT and submit a VAT return, and so on. In other words, the only objective of the *IVA di gruppo* is that its members can offset their periodical VAT positions, which can point out, depending on the case, a VAT debt or a VAT credit. In practice, the controlling company carries out the offset of all of the periodical VAT positions of the participating companies (including its own) and determines the periodical VAT due (to be paid) or the periodical excess input VAT (to be carried forward) of the "group" of companies.

19. Art. 13, items 1 and 3 of Presidential Decree 633.
20. And provided, of course, that one of the parties of the transaction is subject to a limited deduction of VAT (as required by the law).
21. Reference is to IT: Ministerial Decree of 13 December 1979.
22. In principle, in order for the companies of a group to exercise the option under discussion (together with their controlling company), it is necessary that they are all controlled at least 50% by the controlling company as of 1 July of the previous calendar year (art. 2 of the Ministerial Decree of 13 December 1979).

The *IVA di gruppo* regime described is therefore clearly very different from the Italian "VAT group" that will be possible to implement starting from 2019, since the former provides for different "VAT entities" (the companies controlled by the controlling company and the controlling company itself) and not for a sole "VAT taxable person" represented by the VAT group, with the consequence that the transactions between companies participating in the same *IVA di gruppo* regime are within the scope of Italian VAT (since they are, in any case, considered to be carried out between two different taxable persons), while – as already pointed out in section 2.1. – the transactions among the participants in a VAT group will be outside the scope of VAT (as they occur within the same taxable person, i.e. the VAT group itself).

Even if the *IVA di gruppo* provisions will survive after the entering into force of those relating to the Italian VAT group, they will not be affected by the *Skandia* judgment and the Guidelines, considering that the latter specifically refer to VAT groups considered as single VAT taxable persons.

3. The *Skandia* Judgment

For the sake of clarity, the authors deem that it is useful at this stage to shortly summarize the *Skandia* principles.

The main conclusion of the *Skandia* judgment was that supplies of services from a main establishment in a third country to its branch in a Member State constitute taxable transactions when the branch belongs to a VAT group. As clarified by the ECJ, the fact that the branch itself is part of a VAT group (i.e. of another specific VAT taxable person) results in the non-applicability of the principle stated in the *FCE Bank* judgment[23] that the supply of services between a main establishment and its branch are outside the scope of VAT because they are being "rendered" within the same legal entity.

A second main finding of the ECJ was that the recipient of the services supplied by the main establishment was the VAT group as a single taxable person (and not the branch, which had actually received the services from its main establishment from an economic point of view, but was a member of the VAT group, i.e. the "taxable person" from a VAT point of view), and therefore that the group was the taxable person liable for the payment of the VAT (under reverse charge).

To summarize:

- when a transaction is incurred between the head office and its branch, the transaction is outside of the scope of VAT (*see FCE Bank*); and
- when a transaction is incurred between the head office and its branch – which is, however, part of a VAT group in the country of establishment – then the transaction becomes subject to VAT (*see Skandia*).

An issue that was not answered by the *Skandia* decision is the position of a head office dealing with its branch, regardless of whether it is an EU or non-EU resident. In other words, the question remains as to whether *FCE Bank* applies irrespective of the residence of the head office, since the ECJ expressly stated that the question was of no use to the referring court.[24] [25]

4. The Guidelines Issued by the VAT Committee Relating to the *Skandia* Judgment

4.1. The Guidelines

The VAT Committee issued guidelines following the *Skandia* decision, which were the outcome of a meeting held on 26 October 2015.[26] The VAT Committee, set up to promote the uniform application of the provisions of the VAT Directive, is an advisory committee only, which cannot take legally binding decisions for the European Commission or the Member States of the European Union, which are free not to follow them.[27] Nevertheless, the opinions rendered by the VAT Committee can surely represent an important reference when interpreting EU legislation or, as is the case in this article, when considering the possible implications of an ECJ judgment on the application of the VAT legislation by a Member State.

In the Guidelines, the VAT Committee reached very interesting conclusions relating to some open issues arising from the *Skandia* judgment, as follows:

23. IT: ECJ, 23 Mar. 2006, Case C-210/04, *Ministero dell'Economia e delle Finanze (Ministry of Economic Affairs and Finance) and Agenzia delle Entrate (Revenue Agency) v. FCE Bank plc*, ECJ Case Law IBFD.
24. In this respect, *see* point 22 of the *FCE Bank* case (id.), where the ECJ stated that "[i]t should be noted in this connection that the referring court asks to what extent do supplies of services made by *a company established in the United Kingdom* to its branch in Italy fall within the scope of the Sixth Directive. *It follows that it is of no use to the referring court to make a ruling on the situation in which the company is established in a non-Member State*" (emphasis added).
25. In addition, still subject to valuation is the position of a VAT group regulation whereby a branch is included only if the related head office can also be included.
26. The Guidelines have been defined as the result of the discussions in the meeting about the VAT Expert Group Working Paper No. 879 (2015), taking into consideration also the outcome of the discussions about the VAT Expert Group Working Paper No. 845 (2015), during the previous 103rd Meeting held on 20 April 2015. To be noted is that the European Commission has published all of the "Guidelines resulting from meetings of the VAT Committee", related to the meetings of the VAT Committee held until 8 March 2017.
27. The guidelines issued by the VAT Committee do not constitute an official interpretation of EU law and do not necessarily have the agreement of the European Commission.

- in the case of a legal person comprising a main establishment and a branch established in different territories, "only the entity" (i.e. the main establishment or branch) "physically present" in the "Member State that has introduced the VAT grouping scheme may be considered to be "established in the territory of that Member State" for the purposes of Article 11 of the VAT Directive, and thus able to join a VAT group there" (independently of its branch or main establishment not established in that Member State);
- "[b]y joining a VAT group pursuant to article 11 of the VAT Directive, an entity" (main establishment or branch) "becomes part of a new taxable person for VAT purposes – namely the VAT group – irrespective of the legal person to which it belongs". Being part of a VAT group, which is a single taxable person, "precludes the members of the VAT group from continuing to operate, within and outside their group, as individual taxable persons for VAT purposes";
- "[a] supply of goods or services by one entity to another entity of the same legal person" (main establishment to branch, branch to main establishment or branch to branch), "where only one of the entities involved in the transaction is a member of a VAT group or where the entities are members of separate VAT groups, shall constitute a taxable transaction for VAT purposes, provided that the conditions laid down in Article 2(1) of the VAT Directive [to identify the taxable transactions] are met". In this respect, "it is irrelevant whether the goods or services are supplied from a third country to a Member State or vice versa, or between two Member States"; and
- "[a] supply of goods or services between an entity of a legal person" (main establishment or branch) "established in a Member State, *irrespective of whether that Member State has introduced a VAT grouping scheme*, and a VAT group in another Member State which includes another entity of the same legal person" (branch or main establishment) "shall constitute a taxable transaction for VAT purposes, provided [again] that the conditions laid down in Article 2(1) of the VAT Directive [for the taxable transactions] are met". (Emphasis added)

These conclusions were reached "by large majority", which means that a number of Member States varying from 19 to 23 (of 28 in total) agreed with the defined solution.

4.2. Implications of the Guidelines

With reference to the concept of being "established in the territory of a Member State" within the meaning of article 11 of the VAT Directive, the VAT Committee could choose between two approaches (examined both in the VAT Expert Group Working Papers No. 845 and 879). According to a "broad" interpretation,[28] a VAT group can also include entities (the main establishment or branches) not established in the Member State where the VAT group was constituted, provided that they are legally bound to a member of the VAT group (branch or main establishment) physically present in that Member State, by which they would be so "attracted" in the same VAT group. According to such a hypothesis, the cross-border transactions between a main establishment and its branch would go on being outside the scope of VAT, regardless of the fact that a VAT group is actually in place.

According to a "narrow" interpretation,[29] only the entity (main establishment or branch) physically present in the territory of a Member State can take part in a VAT group in that Member State, regardless of its legal ties with other entities (branches or the main establishment) of the same legal person, which may be physically present in another Member State or in a third country. According to such a hypothesis, the cross-border transactions between these entities would be within the scope of VAT (and subject to tax, where applicable), since the entity belonging to the VAT group would lose its qualification as a single taxable person with the respective main establishment/branch and would become part of a new taxable person represented by the VAT group itself (which would be the counterpart of the transaction, from a VAT point of view).

As pointed out at no. 1 of the Guidelines,[30] the VAT Committee decided to adopt the "narrow" interpretation, which appears to be more in line with article 11 of the VAT Directive and allows the avoidance of potential conflicts between the jurisdictions of two Member States. In fact, according to the "broad" approach, a single entity of a legal person (the main establishment or branch) could belong to two VAT groups in two different Member States, generating issues not provided for or regulated by the VAT Directive.[31]

Moreover, as pointed out in no. 4 of the Guidelines, a taxable transaction for VAT purposes can be identified any time a supply of goods or services is carried out between a main establishment or branch established in a Member State — irrespective of whether that Member State has introduced a VAT grouping scheme — and a VAT group in another Member State that includes the other entity (namely the branch or main establishment) of the same legal person.

Considering these interpretations rendered by the VAT Committee in the Guidelines, the principles expressed in the *Skandia* judgment may actually also apply to transactions carried out in the past between a main establishment or a branch established in a Member State (or in a third country) and another entity (a branch or main establishment) of the same legal person established in another Member State (or in a third country) where one of the two entities involved was a member of a VAT group in its Member State of establishment. In this case, the circumstance that the VAT grouping was not (at the time of the transactions) or has not (even later) been introduced in the Member State of one of the involved entities would have no relevance.

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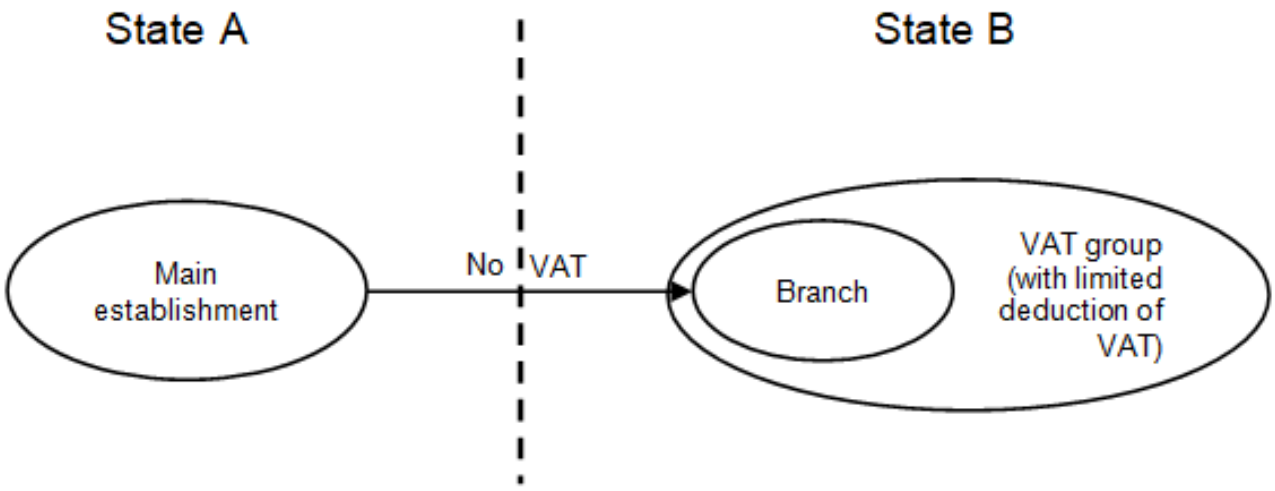
28. This approach is applied, e.g. in the United Kingdom and the Netherlands.
29. Applied, e.g. in Belgium, Germany, Italy and Sweden.
30. See *supra* n. 8.
31. This would be the situation, for example, of a branch established and a member of a VAT group in a Member State (State 1) adopting the "narrow" interpretation, with the main establishment of such branch established and a member of a VAT group in another Member State (State 2) adopting the "broad" interpretation. In such a case, the branch would be, at the same time, part of two VAT groups, one in State 1 and the other in State 2. Moreover, in the described scenario, the same transaction between the main establishment and the branch would be outside the scope of VAT in State 2, while it would be relevant for VAT purposes in State 1.

From a practical point of view, the application of the *Skandia* judgment to past transactions could have negative (and sometimes dramatic) consequences, of course mainly within the multinational financial (e.g. bank or insurance) groups, where taxable transactions between a main establishment and a branch (one of which was a member of a VAT group in the territory of establishment), initially considered outside the scope of VAT, had to be reconsidered as taxable in the state of the recipient. In fact, the input VAT to be accounted for through the reverse charge mechanism in such state on the cross-border transaction could be partially (according to the pro rata calculation) or totally not deductible (*see* Scheme 1).

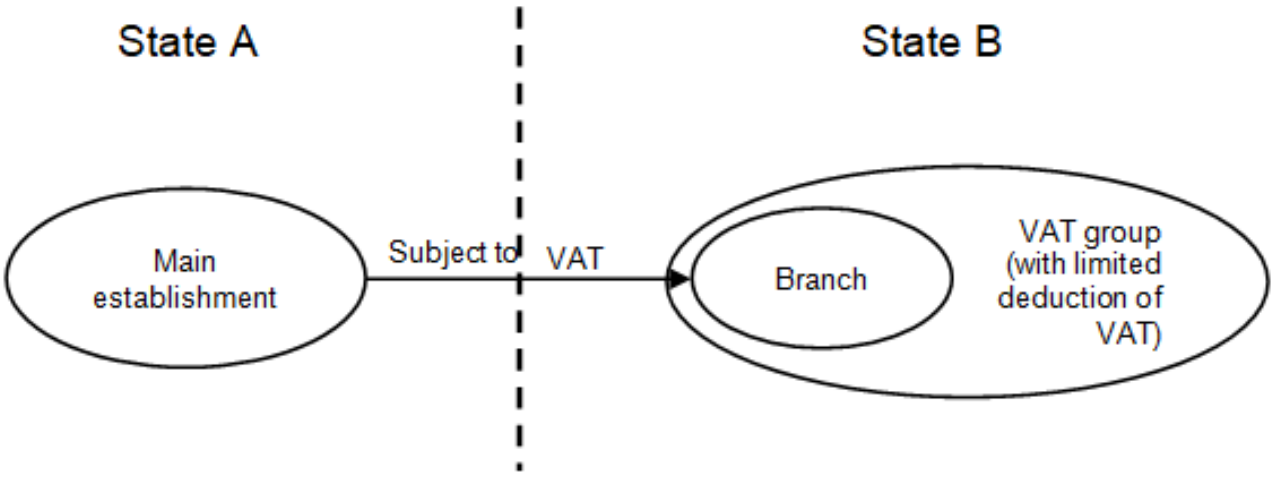
Scheme 1: Possible negative effects on the deduction of VAT due to the *Skandia* judgment

***Before* the *Skandia* judgment**



The transaction is outside the scope of VAT due to the fact that the main establishment and its branch belong to the same legal ty (

***After* the *Skandia* judgment**



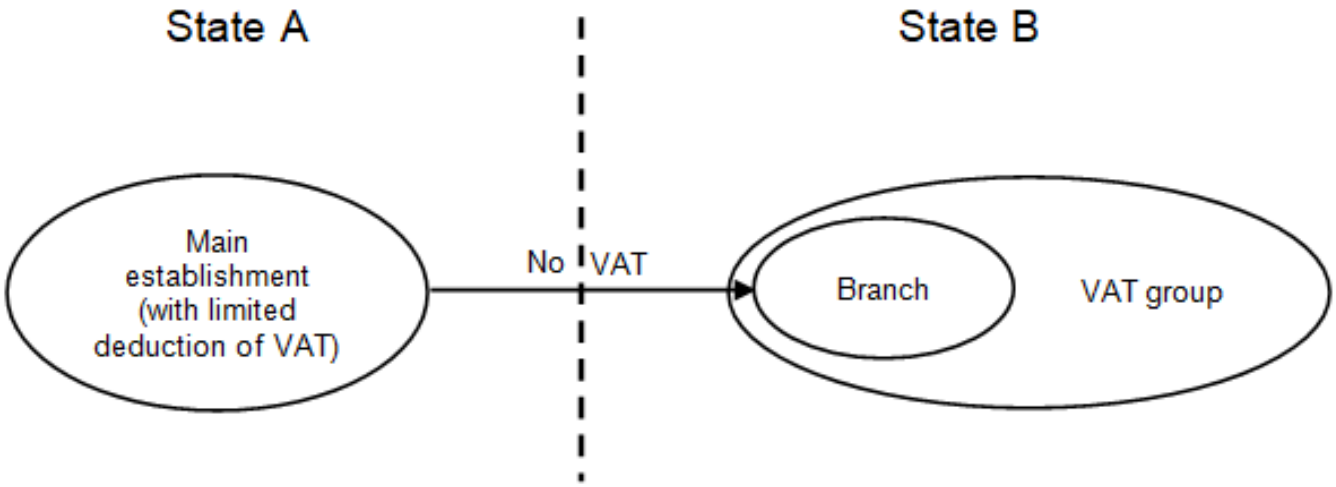
The transaction is subject to VAT (through the reverse charge mechanism) in State B (by the VAT group that the branch belongs

Since the VAT group is subject to a limited deduction of VAT, the input VAT accounted for will be partially or totally lost (mainly for financial groups).

On the contrary, in other situations, the "new" (on the basis of the *Skandia* judgment) VAT treatment (relevant for VAT purposes rather than exclusion) of taxable transactions carried out between a main establishment and a branch (one of which is a member of a VAT group in its state of establishment) could have a positive impact for the entity that supplied the services to the other upon the redetermination of the pro rata calculation for the deduction of input VAT. In fact, such transactions would then be relevant for the pro rata calculation(increasing it) as taxable services (even if subject to VAT in the state of the recipient through the reverse charge mechanism). Consequently, the supplying entity (the main establishment or branch) could evaluate the possibility to recover a higher input VAT not previously deducted through the submission of a new tax return (amending the one already filed) where possible, or through the submission of a claim for a refund of the excess of VAT paid (*see* Scheme 2).

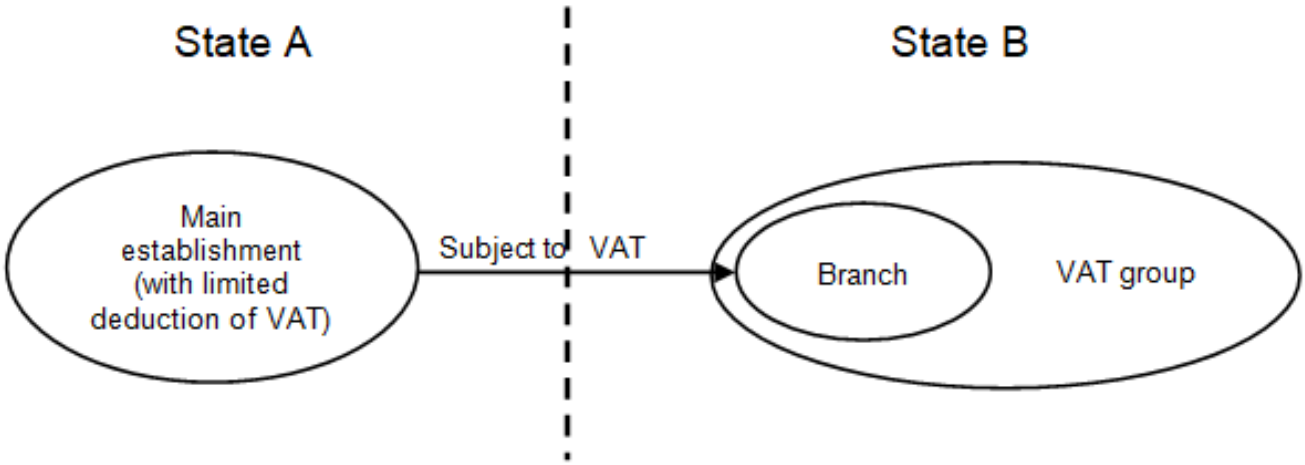
Scheme 2: Possible positive effects on the deduction of VAT due to the *Skandia* judgment

***Before* the *Skandia* judgment**



The transaction is outside the scope of VAT due to the fact that the main establishment and its branch belong to the same legal ty (

***After* the *Skandia* judgment**



With the transaction being taxable, the pro rata calculation for the deduction of VAT will improve for the main establishment (sup ing

5. The Italian Perspective

As noted in sections 2., 3. and 4., for what concerns past and current situations, the *Skandia* judgment principles (and the Guidelines) could only have an impact on transactions carried out between an Italian main establishment (or a branch established in Italy) and a branch (or main establishment) established in another Member State and belonging to a VAT group there.

For the future, the new provisions regulating an Italian VAT group are actually in line with the *Skandia* principles and the Guidelines. In fact, as seen in section 2., they provide for the possible inclusion in an Italian VAT group of taxable persons established in Italy (the main establishments and the branches established abroad are expressly excluded), and, moreover, the supplies of goods and services provided to a member of a VAT group by a taxable person that is not part of the VAT group are deemed to be provided to the VAT group.[32] In addition, a clear alignment of the Italian VAT-grouping provisions with the *Skandia* principles and with the Guidelines has been obtained through the new rules very recently introduced by the Budget Law for 2018, described in section 2. This means that, unless these provisions are changed in the future, the previously mentioned[33] (not only negative but also positive, in some cases) effects are expected to be produced.

For example, when the recipient of services subject to VAT in Italy is a financial entity (branch or main establishment) belonging to an Italian VAT group and the supplier is its main establishment or its branch established abroad, the services will be considered rendered to the Italian VAT group. Consequently, they will not be outside the scope of Italian VAT (according to the ECJ's judgment in *FCE Bank*),[34] but they will be subject to Italian VAT, and the related input VAT accounted for under the reverse charge mechanism will be recovered depending on the pro rata calculation of the VAT group. In some cases, it could be even totally lost if the VAT group's right to deduct is very limited or nil.

In the case of financial groups, the negative effects on the group's right to deduct VAT could be quite considerable and could even imply the total loss of the incurred input VAT.

Currently, the authors are not aware of any official public interpretations rendered by the Italian tax authorities after the issuing of the Guidelines by the VAT Committee or relating to the application of the *Skandia* judgment principles. Moreover, the new VAT-grouping rules introduced by the Budget Law for 2018 are very recent and have not yet been commented on by the tax authorities.

Nevertheless, on the basis of the available information,[35] the Italian tax authorities have provided answers to the questions submitted by a taxable person through a ruling (issued before the rules introduced by the Budget Law for 2018), which, as far as the authors know, have not been officially published (and therefore are not available in public document databases). These questions were related to the correct VAT treatment, among a group operating in the financial sector, of the transactions between the UK main establishment, belonging to a VAT group in the United Kingdom, and its Italian branch.

Sharing the approach of the *Skandia* judgment (and the Guidelines), in their reply, the Italian tax authorities first stated that the services between the UK main establishment and its Italian branch were to be considered relevant for VAT purposes, considering that the fact that the first entity belonged to a UK VAT group implied that two taxable persons (and not only one) were involved in the transaction, i.e. the UK VAT group, on one side, and the Italian branch, on the other side. In this respect, it is important to point out that the *Skandia* judgment principles were recognized as applicable even when, in the case at hand, the main establishment (and not the branch) was part of a VAT group.

Moreover, it has been stated that when the main establishment carries out services in Italy for taxable persons also established in Italy, the subjective "separation" between the main establishment (in this case, due to its membership in the UK VAT group) and the branch implies that no "force of attraction" (to the branch) applies (under the former article 192-bis of the VAT Directive), even for the transactions that directly involve the participation of the same branch.

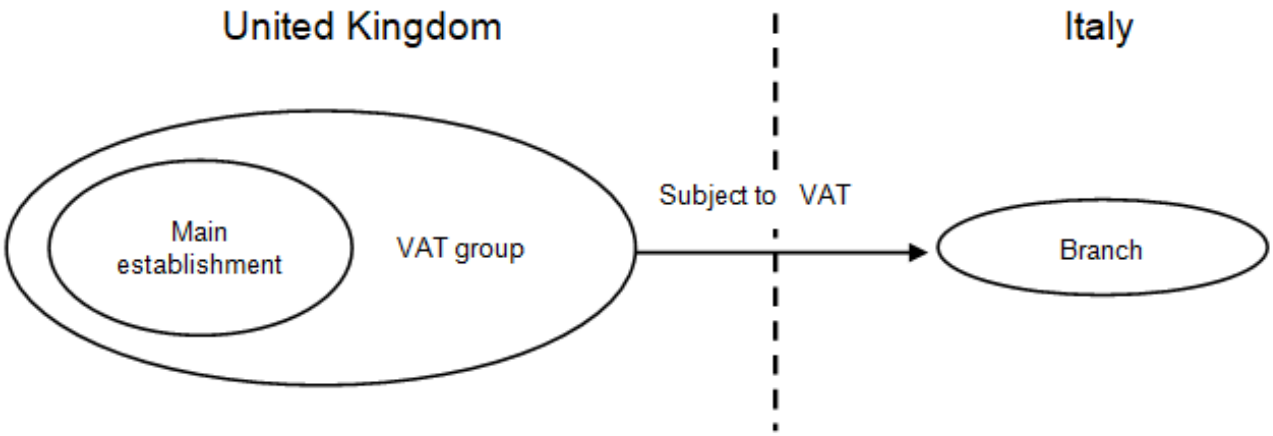
Consequently, according to such hypothesis, the Italian recipients (taxable persons) of the transactions carried out by the main establishment will apply Italian VAT through the reverse charge mechanism, and therefore, the branch will not take part as such in the transactions.

Again, in the case of services supplied in Italy by the UK main establishment for private individuals (or, more in general, non-taxable persons) or non-established taxable persons, the VAT group as a taxable person (and not the UK main establishment) will have to ask for an Italian VAT identification number in order to apply Italian VAT to the recipients.

32. As provided for by the new arts. 70-bis and 70-quinquies of Presidential Decree 633.
33. *See* sec. 4.2.
34. *FCE Bank* (C-210/04).
35. As mentioned in P.G.E. Altamura & V. Biraghi, *La disciplina IVA delle operazioni intercorrenti tra Casa Madre e Stabile Organizzazione alla luce della sentenza Skandia*, Strumenti finanziari e fiscalità (SFEF) 25, p. 125 (2016).

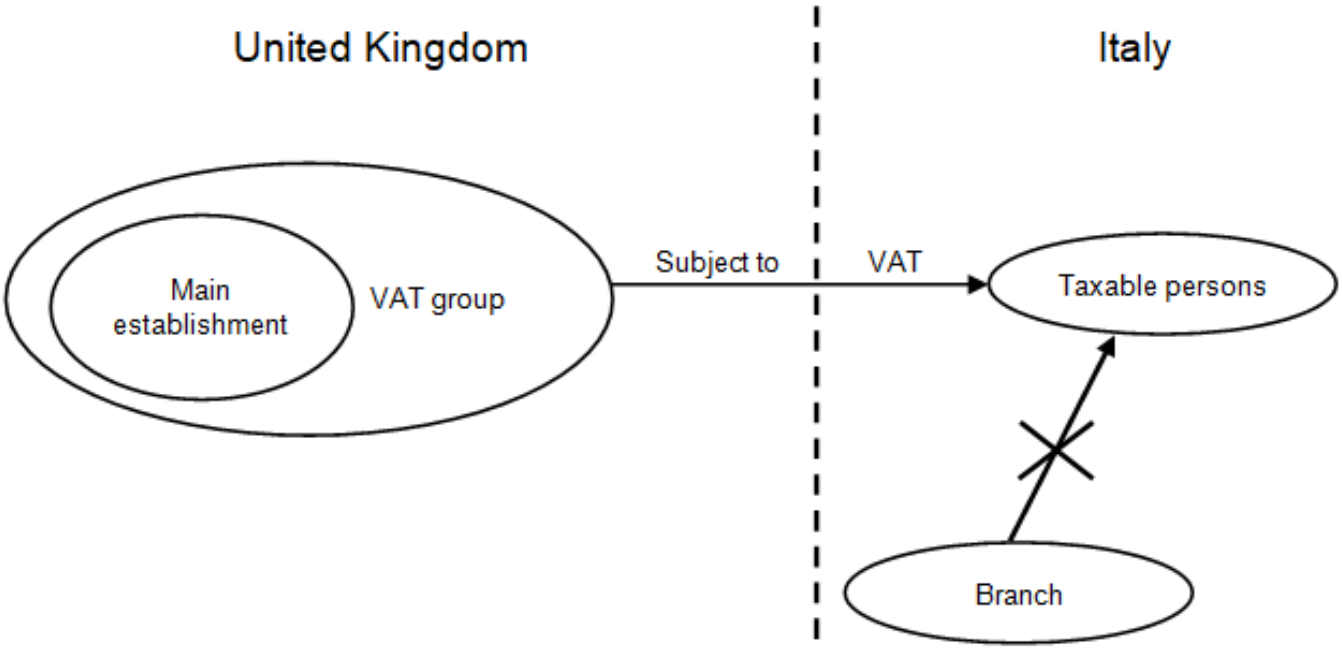
The authors summarize the principles expressed in the *Skandia* ruling in the case of transactions subject to VAT in Italy in the following examples of Cases 1, 2 and 3.

Case 1: Services between the UK main establishment and its Italian branch



Due to the participation of the main establishment in a UK VAT group, two taxable persons (the VAT group and the Italian branch) are involved in the transaction, which is subject to VAT in Italy (through the reverse charge mechanism by the Italian branch).

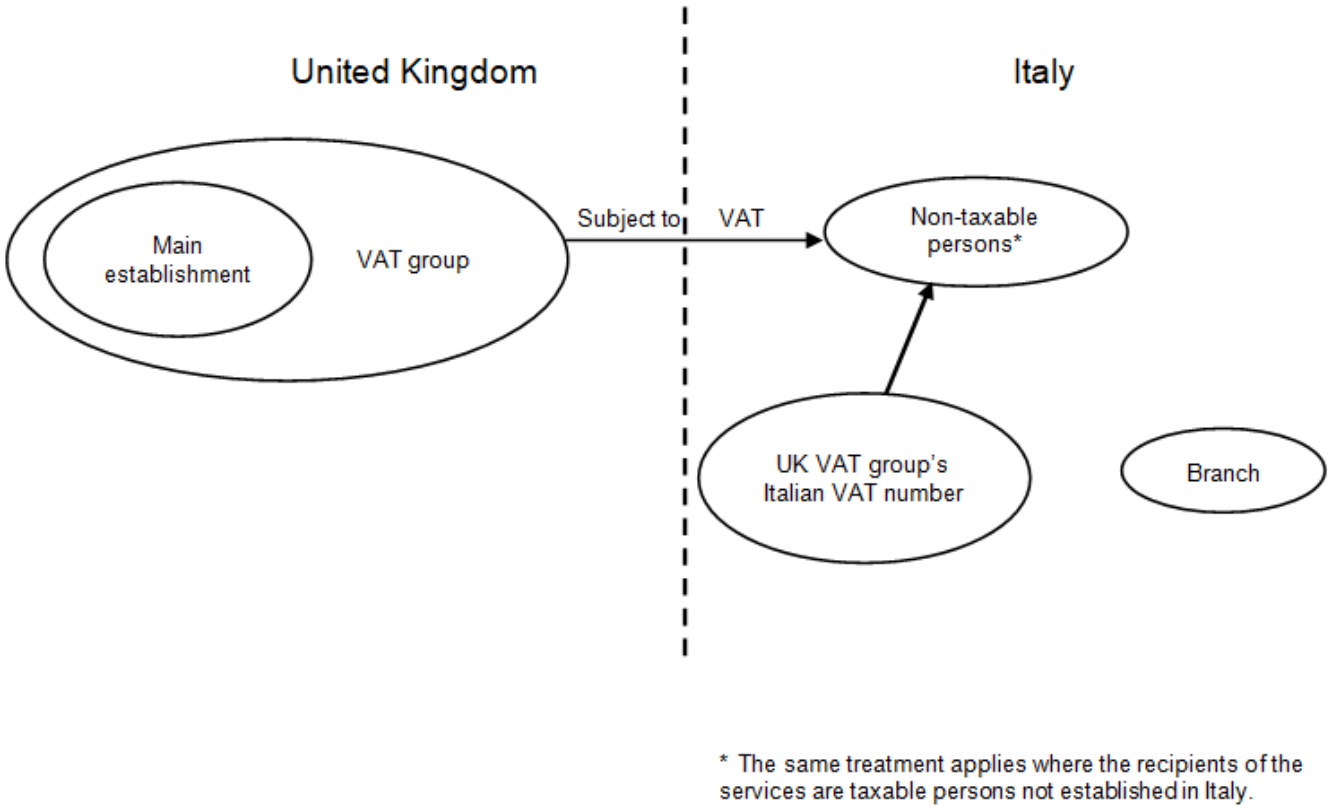
Case 2: Services between the UK main establishment and Italian taxable persons



Due to the participation of the main establishment in a UK VAT group, no "force of attraction" of the Italian branch applies, even if the transaction directly involves the participation of the latter.

The recipients (Italian VAT-taxable persons) apply Italian VAT through the reverse charge mechanism.

Case 3: Services between the UK main establishment and non-taxable persons (or taxable persons not established Italy



Due to the participation of the main establishment in a UK VAT group, the VAT group (as a taxable person) will have to ask for an Italian VAT identification number in order to apply Italian VAT to the recipients.

6. Conclusions and Final Remarks

From 2019 onward, taxable persons established in Italy can be part of an Italian VAT group, which, according to the new Italian VAT legislation, will be in line with the *Skandia* decision. All the principles laid down in this decision (as exemplified through flow-charts in sections 4.2. and 5.) — in particular the principle that the need to consider the members of a VAT group (including a main establishment or a branch) as a single taxable person prevails over the circumstance that the main establishment and its branch are part of the same person from a legal point of view — will also be realized in Italy.

On the contrary, the cross-border transactions between the main establishment and branch will remain outside the scope of VAT in the different case where no VAT group is in place, since in such case, the principle that the transactions are carried out by the same legal person would not be derogated (according to the *FCE Bank* case).

Even if not published, the commented ruling issued by the Italian tax authorities is relevant because it contains the thoughts of the Italian tax authorities in respect of the application of the *Skandia* principles (even if referring to a specific scenario), which appears to be in line with the new rules introduced at the end of 2017 in the Budget Law for 2018 (transposing *Skandia*'s principles in the Italian VAT-grouping legislation), which have not yet been commented on by the tax authorities.

In any case, it is important for the multinational groups (mainly for those in the financial sector), already having an entity in Italy (either the main establishment or a branch) involved in taxable transactions with another entity (branch or main establishment) of the same legal person that is established in another Member State where it belongs to a VAT group, to carefully evaluate the related effects from a VAT point of view.[36]

36. The same evaluations will be necessary in the future with reference to the cross-border transactions between a branch/main establishment belonging to an Italian VAT group (as explained in sec. 1., possible from 2019) and a main establishment/branch established abroad.

It would be necessary to conduct an analysis of the impacts on the right to deduct VAT on cross-border transactions not only for the present, but also for the future, and to not forget the past (also based on the conclusions of the VAT Committee) in order to estimate the possible risks related to VAT, interest and penalties. In the case of a challenge by the tax authorities about past behaviours, however, the taxable persons could rely on the principle of legitimate expectations in order to avoid not only interest and penalties, but even VAT. In the case of challenges by the tax authorities in situations where the application of the *Skandia* judgment and the Guidelines would have determined the payment of more VAT, the taxable person could defend its past behaviour based on the principle of protection of legitimate expectations, which the Member States' tax authorities are obliged to observe (as is strongly recommended by the ECJ, e.g. in the *Elmeka* [37] judgment). Based on this principle, a taxable person subject to assessment could ask for the non-application not only of penalties and interest, but even of VAT. In fact, the *FCE Bank* judgment could have surely generated in the taxable person the conviction for the general irrelevance, for VAT purposes, of the supplies of services between a main establishment and its branch established in another Member State, regardless of the membership of one of the two entities of a VAT group.

Thus, it seems reasonable to expect, through an intervention in the legislation or an interpretation of the tax authorities, the confirmation that the principles expressed in the *Skandia* judgment and in the Guidelines should not apply to the transactions carried out before a certain date in the past, e.g. before the publication of the Guidelines or before the interpretations, if any, rendered by the same authorities with reference to the application of the *Skandia* principles (and of the Guidelines) in their Member State's territory.

For the future, it is reasonable to expect that the Guidelines could be followed at least by the Member States supporting a "narrow" interpretation of the VAT-grouping scheme, as mentioned in section 4.2. Nevertheless, a general application of such principles would, of course, be required in the case of a direct intervention in this sense on the relevant EU VAT law provisions.

Finally, as described in section 4.2., in other situations, the application of the *Skandia* principles could lead to the interesting opportunity to recover input VAT not previously deducted in the past.

37. GR: ECJ, 14 Sept. 2006, Case C-181/04, *Elmeka N.E. v. the Minister for Economic Affairs*, ECJ Case Law IBFD.