

THE CURIOUS CASE OF TP - VAT UPDATE ON DIRECTORSHIP FEES



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On July 13th, 2023 the Advocate General (AG) of the Court of Justice of the European Union (CJEU) Juliane Kokott, in her opinion on the TP case (C-288/22), asserted that a natural person serving as a director of a company is not a taxable person under the VAT directive. According to the AG's opinion, directors by virtue of their role and responsibilities as members of the board of directors of a company do not engage in an independent economic activity as per the VAT Directive.

The AG's opinion highlighted the lack of harmonization across the European Union (EU) and emphasised the necessity for a unified approach based on objective criteria. It is important to note at this point that, whilst the majority of Member States do not consider the remuneration of directorship fees as remuneration for a taxable activity, six Member States, including Cyprus adopt a contrary stance.

The AG's perspective triggered several discussions within professional circles across Member States and created a sense of anticipation as to whether the CJEU will adopt her position or differentiate altogether.

Finally, on December 21st, 2023 the CJEU issued its long-awaited ruling which is surely expected to create "chain reactions" especially for the six Member States that consider the remuneration of directorship fees a taxable activity as per the provisions of the VAT Directive.



Facts of the case

TP, a lawyer in his profession is a member of the board of directors of several public limited companies incorporated under Luxembourg law. As a member of those boards, he takes part in decisions concerning the amounts, risk management policy and the strategy to be followed by the group and in developing proposals to be put to shareholders' meetings.

The day-to-day management of two of the companies is carried out by an executive committee made up of the chief executive officers or executive directors. The business of the other two companies, do not require an executive committee.

For those activities, TP had received in his capacity as a member of the board of directors, fees in the form of percentage of the profits received by those companies, or a lump sum.

Questions referred to the CJEU for preliminary ruling

1. Is a natural person who is a member of the board of directors of a public limited company incorporated under Luxembourg law carrying out an 'economic' activity within the meaning of Article 9 of the VAT Directive and more specifically, are percentage fees received by that person to be regarded as remuneration paid in return for services provided to that company?
2. Is a natural person who is member of the board of directors of a public limited company incorporated under Luxembourg law carrying out his or her activity "independently", within the meaning of Articles 9 and 10 of the VAT Directive?

The First question

The CJEU held that the answer to the first question is that a member of the board of directors of a public company under incorporated Luxembourg law carries out an economic activity, where he or she supplies services to that company for consideration, provided that that activity is effected on a continuing basis and for remuneration which the procedures for fixing that amount are foreseeable. This was the case for TP.

Ratio Decidendi

The CJEU stated that Article 9(1) of the VAT Directive, provides that the term taxable person means any person who, independently, carries out in any place any economic activity whatever the purpose or results of that activity and that such activity corresponds to one of the chargeable events defined in Article 2(1). [In this particular case scenario, the only relevant event to examine would be the ‘supply of services for consideration’.]

Analysing the above cornerstone, the CJEU stated that:

- a) Economic activity is generally classified as any activity that is permanent (and/or on a continuing basis) and is carried out for remuneration paid to the person carrying out the activity – TP’s appointment for a period of 6 years was sufficient to consider his remuneration to be received on a continuing basis;
- b) Classifying a supply of services as a transaction for consideration requires only that there be a direct link between that supply and the consideration actually received by the taxable person;
- c) The direct link relationship is established if there is a legal relationship between the provider of the service and the recipient pursuant to which there is reciprocal performance; the remuneration received by the provider of the service constitutes the actual consideration for the service supplied;
- d) It does not matter whether the price paid for an economic transaction is higher or lower than the cost price; and
- e) It does not matter that TP’s remuneration was not obtained directly by the Board itself but was set by the shareholders of the company at the AGM, given that the VAT legislation allows for the consideration to be paid by a third party without breaking the ‘direct link’ test.

The CJEU referred to its case law and stated that in assessing the existence of consideration for the supply of a service, the direct link between the supply of services and the consideration is broken when the remuneration is awarded in a voluntary and uncertain way so that its amount is practically impossible to determine. This however was not deemed to be the case for TP as in return for his activity on the Board of Directors, he received remuneration in the form of percentage fees or a lump sum.

In addition, the CJEU also stated that a service which is ab initio set for a definite period of time, does not lose its continuity merely because that service may be terminated at any time and for any reason - by either the supplier of that service or the recipient.

The Second Question

The CJEU held that the answer to the second question is that activity of a member of the board of directors of a public limited company under Luxembourg law is not carried out independently, where - despite the fact that that member is free to arrange how he or she perform their work, receives the emoluments making up his or her income, acts in his or her name and is not subject to an employer -employee relationship – he or she does not act on their own behalf or under their own responsibility and does not bear the economic risk linked to their activity.

Ratio Decidendi

The second question essentially asks whether the activity of a member of a board of directors of a public limited company is carried out independently or whether the activity performed is carried out the context of a relationship of an employer and employee and thus such activity not being per se independent.

The court held that in order to assess whether an employer-employee relationship exists, it is necessary to check whether that person performs his or her activities in his or her own name and under his or her own responsibility and whether he or she bears the economic risk associated with those activities.

As the CJEU stated when determining whether such a member acted in his or her own name, on his own account and under his own responsibility, it is important and necessary to take into consideration the national rules governing the allocation of responsibilities between the members of the board and the company concerned.

In addition, the CJEU stated that even if a member of a board brings his/her expertise and know-how to the board he/she does not appear to bear the economic risk as it is the company which will face the negative consequences of the decisions adopted by the board.

Implications on the Cyprus VAT legislation

The TP judgement will surely exert influence on the position currently adopted by Cyprus, since its current stance - akin to that of Luxembourg, considers that directorship fees are subject to VAT - subject of course to some limited exceptions.

It is imperative in my opinion for the Cypriot Tax Department to re-evaluate this position and issue a new circular documenting in a practical manner the above ratio decidendi which as a matter of European law has immediate effect and is directly applicable across all Member States.

Cyprus as a preferred business destination has a valuable opportunity to act swiftly, further enhance its already coherent and solid VAT framework and ultimately align its stance, on this particular matter, with other Member States who seem to have been obtaining a competitive advantage in terms of attracting new business.





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