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EU Tax Alert

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Highlights in this edition

EU State aid investigation opened into IKEA's tax treatment in the Netherlands

On 18 December 2017, the Commission announced the opening of a formal State aid investigation into two tax rulings concluded by the Netherlands tax authorities with Inter IKEA Systems BV in 2006 and 2011. This investigation concerns individual tax rulings and as such, should not directly impact other taxpayers. Nonetheless, the investigation forms part of the Commission's continuing broader efforts focusing on transfer pricing and valuation issues.
EU State aid rules disallow the granting of a selective advantage by an EU Member State that may distort competition by favouring certain undertakings.
The opening of this new investigation confirms the Commission's commitment to use State aid enforcement as a tool to further a broader tax reform agenda.

The Commission's investigation focuses on various transfer pricing elements accepted by the Netherlands tax authorities:

First of all, the Commission doubts whether the level of licence fees paid by Inter IKEA Systems BV in the period 2006-2011 was at arm's length in view of the activities carried out by Inter IKEA systems BV in the Netherlands. This is not the first time the Commission looks into the level of licence fees; amongst others, it did so in the Starbucks case and in the Amazon case.

The second doubt concerns the acquisition price for intellectual property rights purchased by Inter IKEA Systems BV in 2012 and financed with a loan from a related party. The Commission will analyse more in depth whether the price that Inter IKEA Systems BV has paid for these intellectual property rights was not too high and whether consequently, the interest on the acquisition loan would also not be too high. Recently, Commissioner Vestager indicated she was asking Apple for further details on a similar intra group transaction, following the publication of the Paradise Papers.

The Commission will now verify whether the terms of the various intragroup transactions – licence fees, acquisition price of the intellectual property rights and interest on the intragroup loan – were at arm's length. The decision to open the formal investigation does not prejudice the final outcome of the case.

The Netherlands Minister of Finance issued a press release, which remarkably did not include a statement that according to the Netherlands, no selective advantage had been granted to the beneficiary of the tax rulings.

EU adopts list of non-cooperative jurisdictions for tax purposes (black list)

On 5 December 2017, the Economic and Financial Affairs Council (ECOFIN) determined a list of 17 non-cooperative jurisdictions, i.e., the EU black list. This list was established based on three (screening) criteria: tax transparency, fair taxation (no harmful tax regimes) and implementation of BEPS minimum standards. The Netherlands, Belgium, Luxembourg and Switzerland are not included in this black list. Subsequently, on 23 January 2018, the list was updated with 8 jurisdictions being removed following commitments made at a high political level to remedy EU concerns. The ECOFIN recommends (but does not oblige) that the Member States impose tax sanctions on the listed jurisdictions. The EU may impose non-tax sanctions.

The listed jurisdictions

The jurisdictions which originally appeared on the EU black list were: American Samoa, Bahrain, Barbados, Grenada, Guam, (Republic of) Korea, Macao SAR, Marshall Islands, Mongolia, Namibia, Palau, Panama, Saint Lucia, Samoa, Trinidad Tobago, Tunisia and the United Arab Emirates (UAE). In the meantime, Barbados, Grenada, the Republic of Korea, Macao SAR, Mongolia, Panama, Tunisia and the UAE have been removed from that list.

Furthermore, the screening process of Anguilla, Antigua and Barbuda, Bahamas, British Virgin Islands, Dominica, Saint Kitts and Nevis, Turks and Caicos Islands, US Virgin Islands – has been put on hold and is expected to be completed by the end of 2018.

Sanctions

The black listed jurisdictions may face sanctions (so-called: 'defensive measures') imposed by the Member States in the form of (administrative) tax measures and by the EU in the form of *non-tax* measures.

The *non-tax measures* are linked to EU funding in the context of the European Fund for Sustainable Development (EFSD), the European Fund for Strategic Investment (EFSI) and the External Lending Mandate (ELM). Such EU funding may not be channelled through entities in the black listed jurisdictions.

The ECOFIN *recommends* (but does not oblige) that Member States impose tax sanctions on the listed jurisdictions including: non-deductibility of costs, CFC rules, withholding taxes, limitation on participation exemption, switch-over rules and reversal of the burden of proof. If a Member State takes such measures, this might lead to having to change not only its domestic law but - depending on the measure - also bilateral tax treaties.

The ECOFIN also *recommends* that Member States take administrative tax measures against the EU black listed jurisdictions, such as increased audit risks for taxpayers benefiting from certain regimes or using structures involving those jurisdictions. The ECOFIN does not provide any guidance on when the Member States should impose the recommended sanctions.

In addition to the EU black list, there is a separate list with 47 jurisdictions, including Switzerland. These jurisdictions have undertaken to address concerns raised on one or more of the screening criteria by introducing relevant changes in their tax legislation by year-end 2018 (or by year-end 2019 in the case of developing countries). As those jurisdictions are not black listed, they would not fall within any of the recommended sanctions.

The ECOFIN intends to monitor and update the EU black list at least once a year. It remains to be seen to what extent the Member States will use the EU black list and will introduce the tax sanctions recommended by the ECOFIN. Still, this blacklist is already linked with other EU legislative proposals. For example, the public CbC reporting proposal includes stricter reporting requirements for multinationals with activities in listed jurisdictions. In the proposed Directive of mandatory disclosure rules for intermediaries, a tax scheme routed through an EU black listed jurisdiction will be automatically reportable to tax authorities

Furthermore, the EU Commission is expected to support Member States' work to develop a more binding and definitive approach to sanctions for the EU black list during 2018. In any event, Member States may apply additional sanctions pursuant to their domestic laws as well maintain their own black lists of non-cooperative jurisdictions with a broader scope.

CJ does not allow too general anti-abuse and substance provisions for holding companies (*Deister Holding and Juhler Holding*)

On 20 December 2017, the CJ issued its judgment in joined cases *Deister Holding AG* (C-504/16) and *Juhler Holding A/S* (C-613/16) *v Bundeszentralamt für Steuern*. In this ground-breaking judgment, the CJ confirmed that the German anti-abuse provision for withholding tax relief for dividends paid by a German company to certain parent companies resident in another EU Member State is too general. Therefore, that provision is incompatible with the EU Parent-Subsidiary Directive and the EU freedom of establishment. For the CJ, neither the tax treatment of the EU parent company's shareholders nor the type or composition of economic activities of the EU parent company is relevant for assessing the existence of abuse. This has a strong impact on EU anti-abuse rules and substance requirements for holding companies.

Background

The German anti-abuse provision denies the withholding tax exemption if:

1. *Subjective scope*: the shareholders of the interposed holding company would not be entitled to such relief if they earned the German dividend income directly, and
2. *Three conditions test*: (1) there are no economic or other relevant reasons for interposing the holding company; or (2) the holding company does not generate more than 10% of its gross income through

its own economic activities; or (3) the holding company does not have a business organisation that is adequately equipped for its business purposes.

Judgment

The CJ confirmed that the German anti-abuse provision is not in line both with the EU Parent-Subsidiary Directive and the EU freedom of establishment. According to the CJ, the legislation at stake is too general and does not have the specific objective of targeting wholly artificial arrangements which do not reflect economic reality. Furthermore, the tax treatment of the shareholders of EU parent companies is irrelevant for the purposes of benefiting from the EU Parent-Subsidiary Directive. Nor does this Directive contain any requirement as to the type of economic activity of EU parent companies or the percentage of income derived from own economic activities.

In addition, the CJ stated that the verification of any of the 'three conditions test' creates an irrebuttable presumption of abuse without the possibility of the taxpayer demonstrating valid economic reasons. According to the CJ, those three conditions (individually or as whole) do not imply by themselves the existence of a wholly artificial arrangement which does not reflect economic activity. In any event, the analysis of such artificiality should be made based on a global assessment taking into account the organisational, economic or other substantial features of the group of companies to which the parent company in question belongs and the structures and strategies of that group.

Our observations

This judgment shows a strict approach of the CJ to domestic anti-abuse provisions. If such provisions are too general, apply automatically and therefore create a general presumption of abuse, most likely they are not in line with EU Law. Furthermore, it also provides a fresh view on the existence of substance requirements for EU holding companies, requiring a case-by-case analysis of the overall situation at stake considering economic and organisational characteristics and strategy of the whole group. We expect that this judgment will also have an impact on anti-abuse provisions in other Member States.

Commission proposes new rules on VAT rates and small enterprises

On 18 January 2018 the Commission has published two proposals for new VAT rules, one regarding the VAT rates, the other regarding small enterprises (SMEs). These proposals are part of its 2016 VAT Action Plan which aims to modernize the VAT system in order to make it simpler, more fraud-proof and business friendly. The proposal on rates concerns new rules to give Member States more flexibility to set up VAT rates. The proposal on SMEs aims at reducing VAT compliance costs for SMEs. Businesses with an annual turnover of less than EUR 2 million could benefit from simplified VAT obligations. If adopted, the proposals could have a significant impact. Both proposals will now be submitted to the European Parliament for consultation and to the Council for adoption. It is intended that the SME rules would enter into force on 1 July 2022. No specific starting date has yet been mentioned for the new rate rules.

VAT rates

The current situation is a patchwork of rates which vary from one country to another The proposed rules will introduce a harmonized and less restrictive system. All EU Member States would be allowed to introduce - in addition to a standard VAT rate of minimum 15% - a super reduced VAT rate below 5%. Furthermore, they would be able to introduce two separate reduced rates as well as an exemption/zero rate. There will be a list of products for which the standard rate is mandatory, such as smartphones, fuel and alcoholic beverages.

Small enterprises

Under current rules, the exemption for SMEs is limited to sales in the SME's own Member State. The proposal would enable SMEs to benefit from the exemption also for sales in other Member States. The annual turnover threshold for the exemption is still decided by the Member States, but should not be higher than EUR 100,000. Simplified VAT obligations would be introduced for SMEs with a turnover between EUR 100.000 and EUR 2 million across the EU. The simplification concerns rules regarding registration, bookkeeping and longer tax periods that should lead to less frequent filing of VAT returns.

CJ rules on repayment of customs duties in case of price adjustments between related companies on the basis of Advance transfer price arrangement (Agreed transfer price composed of an amount initially invoiced and a flat-rate adjustment made after the end of the accounting period) (*Hamamatsu Photonics Deutschland GmbH*)

On 20 December 2017, the CJ delivered its judgment in the *Hamamatsu Photonics Deutschland GmbH* case (C-529/16). The case concerns the conditions for repayment of import duties in case of ex-post price adjustments to transfer prices used at importation (actual transaction value) and the situations in which Article 78 of the Community Customs Code (CCC 2913/92 EC) is applicable.

Hamamatsu, a company established in Germany, which belongs to a group of companies active globally whose parent company, Hamamatsu Photonics, is established in Japan. Hamamatsu distributes, inter alia, optoelectronic devices, systems and accessories.

Hamamatsu purchased imported goods from its parent company which charged it for those goods intrAGroup prices in accordance with the advance pricing agreement concluded between that group of companies and the German tax authorities. The total of the amounts charged to the applicant in the main proceedings by the parent company were regularly checked and, if necessary, adjusted, in order to ensure the conformity of the sale price with the 'arms-length' principle laid down in the guidelines of the Organisation for Economic Co-operation and Development (OECD) applicable to transfer pricing for multinational undertakings and the tax authorities (the 'OECD Guidelines').

The referring court, the Finanzgericht München (Finance Court, Munich, Germany) explained that those checks are carried out in a number of stages, based on the method called the 'Residual Profit Split Method', which is consistent with the OECD Guidelines. In the first stage, each participant is allocated a sufficient profit to produce a minimum rate of return. The residual profit is allocated proportionally in accordance with specific factors. In the second stage, Hamamatsu's operating margin range is established. If the profit actually generated falls outside that margin, the result is adjusted to the upper or lower limit of the margin and credits or subsequent debit charges are made.

Between 7 October 2009 and 30 September 2010, the applicant in the main proceedings released for free circulation various goods from more than 1,000 consignments from the parent company, declaring a customs value corresponding to the price charged. A rate of between 1.4% and 6.7% was levied on the taxable goods.

Because, during that period, the operating margin of the applicant in the main proceedings fell below the range for the operating margin, the transfer prices were adjusted as a result. The applicant in the main proceedings thus received a credit of EUR 3,858,345.46.

Having regard to the adjustment of the transfer pricings subsequently made, by letter of 10 December 2012, the applicant in the main proceedings applied for the repayment of the customs duties for the imported goods of EUR 42,942.14. There was no allocation of the adjustment amount to the individual imported goods.

The Principal Customs Office, Munich rejected that application on the ground that the method adopted by the applicant in the main proceedings was incompatible with Article 29(1) of the Customs Code which refers to the transaction value of individual goods, not that of mixed consignments.

The applicant in the main proceedings lodged an appeal against that decision with the referring court.

The referring court considered that the final annual amount constitutes the final transfer pricing, established in accordance with the arms-length principle provided for by the OECD Guidelines. There was thus no point in basing the transfer pricing exclusively on the provisional pricing in the context of an advance transfer pricing agreement concluded with the tax authorities which does not reflect the real value of the goods. Thus, the price declared to the customs authority was only a fictitious pricing and not the price payable for the imported goods pursuant to Article 29 of the Customs Code.

In those circumstances, the Finanzgericht München (Finance Court, Munich) decided to stay proceedings and refer the following questions to the Court of Justice for a preliminary ruling:

'(1) Do the provisions of Article 28 et seq. of [the Customs Code] permit an agreed transfer price, which is composed of an amount initially invoiced and declared and a flat-rate adjustment made after the end of the accounting period, to form the basis for the customs value, using an allocation key, regardless of whether a subsequent debit charge or credit is made to the declarant at the end of the accounting period?

(2) If so: May the customs value be reviewed and/or determined using simplified approaches where the effects of subsequent transfer pricing adjustments (both upward and downward) can be recognised?'

The CJ made the following observations:

By virtue of Article 29 of the Customs Code, the customs value of imported goods is the transaction value, that is to say, the price actually paid or payable for the goods when they are sold for export to the customs territory of the European Union, adjusted, where necessary, in accordance with Articles 32 and 33 thereof (see, to that effect, judgments of 12 December 2013, *Christodoulou and Others*, C-116/12, EU:C:2013:825, paragraph 38, and of 16 June 2016, *EURO 2004*. *Hungary*, C-291/15, EU:C:2016:455, paragraph 24).

Furthermore, the Court has already stated that the customs value had to be determined primarily according to the 'transaction value' method under Article 29 of the Customs Code. It is only if the price actually paid or payable for the goods when they are sold for export cannot be determined that it is appropriate to use the alternative methods laid down in Articles 30 and 31 thereof (see, in particular, judgments of 12 December 2013, *Christodoulou and Others*, C-116/12, EU:C:2013:825, paragraphs 38, 41, 42 and 44, and of 16 June 2016, *EURO 2004. Hungary*, C-291/15, EU:C:2016:455, paragraphs 24 and 27 to 30).

The Court has also stated that, if as a general rule the price actually paid or payable for the goods forms the basis for calculating the customs value, that price is a factor that potentially must be adjusted where necessary in order to avoid the setting of an arbitrary or fictitious customs value (see, to that effect, judgments of 12 June 1986, *Repenning*, case 183/85, EU:C:1986:247, paragraph 16; of 19 March 2009, *Mitsui & Co. Deutschland*, C-256/07, EU:C:2009:167, paragraph 24; of 12 December 2013, *Christodoulou and Others*, C-116/12, EU:C:2013:825, paragraph 39; and of 16 June 2016, *EURO 2004. Hungary*, C-291/15, EU:C:2016:455, paragraph 25).

Article 27 of the Customs code permits the customs authorities, on their own initiative or at the request of the declarant, to amend the declaration.

However, it must be recalled that the cases in which the Court has allowed a subsequent adjustment of the transaction value is limited to specific situations relating, inter alia, to quality defects or faulty workmanship in the goods discovered after their release for free circulation.

The Court has, in particular, already held that it had to be accepted that, where the goods to be valued were bought free of defects but were damaged before their release for free circulation, the price actually paid or payable was to be reduced in proportion to the damage suffered, since it was an unforeseeable reduction in the commercial value of the goods (judgment of 19 March 2009, *Mitsui & Co. Deutschland*, C-256/07, EU:C:2009:167, paragraph 25 and the case law cited).

Similarly, the Court acknowledged that the price actually paid or payable could be reduced in proportion to the reduction in the commercial value of the goods owing to a hidden defect which it was shown to be present before their release into free circulation and gave rise to subsequent repayments under a warranty obligation which, as a result, might result in a subsequent reduction in the customs value of those goods (judgment of 19 March 2009, *Mitsui & Co. Deutschland*, C-256/07, EU:C:2009:167, paragraph 26 and the case law cited).

Finally, it must be stated that, in the version in force, the Customs Code does not impose any obligation on importer companies to apply for adjustment of the transaction value where it is subsequently adjusted upwards and it does not contain any provision enabling the customs authorities to safeguard against the risk that those undertakings only apply for downward adjustments. In those circumstances, it must be held that the Customs Code, in the version in force, does not allow account to be taken of a subsequent adjustment of the transaction value, such as that at issue in the main proceedings.

The CJ ruled as follows:
Articles 28 to 31 of Council Regulation (EEC) No 2913/92 of 12 October 1992 establishing the Community Customs Code, as amended by Regulation (EC) No 82/97 of the European Parliament and of the Council of 19 December 1996, must be interpreted as meaning that they do not permit an agreed transaction value, composed of an amount initially invoiced and declared and a flat-rate adjustment made after the end of the accounting period, to form the basis for the customs value, without it being possible to know at the end of the accounting period whether that adjustment would be made up or down.

The second questions did not need to be considered, given the ruling on question 1.

State Aid/WTO

AG Opinion on German Loss carry forward decision

On 20 December 2017, AG Wahl delivered his Opinion in case *Andres* (*faillite Heitkamp BauHolding*) *v Commission* (C-203/16P). He concluded that the Commission decision on the German restructuring exemption should be annulled. Germany restricted the carrying forward of losses in the case of a substantial change in ownership of a company, but it made an exemption for ailing companies in need of restructuring. The AG effectively sides with the applicant who argued that loss carry-forward is the general rule and being entitled to it does not lead to a benefit, despite his being exempt from the loss carry-forward restriction. In an alternative reasoning the AG side-lined the justification of prima facie selective benefits for reasons related to the nature or general scheme of the tax system, pointing out that prima facie selectivity in tax cases is 'de facto irrefutable', a statement the CJ cannot leave unaddressed.

Registering recovery claims in insolvency proceedings

Recovery of State aid should normally take place within 4 months after a recovery decision has been taken by the Commission and notified to the Member State involved. This may require registering the recovery claim as a liability as part of an insolvency process within that time frame, or requesting an extension by the Commission otherwise if starting such procedure would inevitably require more time. If authorities are unable to recover the entire amount, this procedure should end up in the winding-up of the undertaking and a definitive cessation of its activities. From the above, it can be deduced that - as far as a recovery claim is concerned - only collecting part of that claim, but not the entire amount, is not an option. This is different from tax authorities deciding to waive part of an initial tax claim in light of potential insolvency as to be able to recover the remainder and not lose the entire claim. In the case activities of an insolvent company are sold to another group company, the question remains whether a sale at fair market value at the time would still satisfy the criterion of definitive cessation as now defined by the CJ (C-363/16 of 17 January 2018, Commission v Greece).

Maltese tonnage tax approved, but with recovery of shareholder benefits?

On 19 December 2017, the European Commission decided to conditionally approve of Malta's tonnage tax regime. However, Malta was required to limit its regime to maritime transport (and allowed ancillary activities under EU law) and it needed to remove certain tax exemptions that applied to shareholders of shipping companies. While the decision itself has not yet been published, the Commission's State aid register indicates that recovery of certain tax benefits has been ordered. This will most likely refer to special treatment given to non-maritime activities and some of the unspecified shareholder benefits referred to in the press release as mentioned above, but no information on that is available at this time.

Direct Taxation

AG Mengozzi opines that Danish legislation that denies the exemption for withholding tax on dividends paid to foreign UCITS is not in line with the fundamental freedoms (*Fidelity Funds*)

On 20 December 2017 AG Mengozzi delivered his Opinion in case *Fidelity Funds v Skatteministeriet intervener LL (L) SIVAC* (C-480/16). The case deals with the Danish legislation that grants UCITS established in Denmark which, either in fact or technically, make a minimum distribution to their members, an exemption from tax at source on dividends distributed by Danish companies, to the exclusion of UCITS established in other Member States.

The question in this case was raised concerning several UCITS with registered offices in the UK and Luxembourg, concerning claims for the repayment of tax retained at source on dividends paid to those UCITS by Danish companies between 2000 and 2009. The UCITS in question asked for the repayment of such tax on the ground that identical UCITS established in Denmark would have enjoyed such exemption. Therefore, they claimed that the difference in treatment is contrary to the free movement of capital and the freedom to provide services under EU Law.

AG Mengozzi started by considering that, on the one hand, the different tax treatment of dividends according to, in particular, the UCITS's place of residence may discourage non-resident UCITS from investing in companies established in Denmark and, on the other, investors resident in that Member State from acquiring shares in non-resident UCITS. Consequently he concluded that there is a restriction in principle contrary to the free movement of capital. However, he noted that such difference may be acceptable if refers to situations which are not objectively comparable or is justified by overriding reasons in public interest.

As regards the comparability, the AG started by stating that it should be examined having regard to the aim pursued by the national provision at issue as well as their purpose and content. The aims pursued by the Danish legislation at issue are: (i) to prevent a series of double taxation charges when an investment is made through UCITS; and (ii) to ensure that dividends distributed by Danish companies do not elude Denmark's power to impose tax on account of the exemption they enjoy at the level of resident UCITS and are actually taxed once, namely as regards those undertakings' members.
Regarding the aim at preventing of a series of charges to tax, the AG considered that as from the moment that Denmark imposes a tax to charge on income, not only on residents but also non-residents become comparable. As concerns the aim of making the exemption enjoyed by resident UCITS conditional on taxation being deferred to the level of those undertakings' members, the question may arise as to whether, when examining the comparability of the situations, the tax situation of the members should be taken into account. In this regard, the AG concluded that, regardless of the perspective from which the examination of comparability of the situations is to be conducted, the situations at issue are objectively comparable.

As regards possible justifications, AG Mengozzi started by refusing the justification based on the need to preserve a balanced allocation of the powers to tax between Member States. According to the AG, where a Member State has chosen not to tax resident UCITS in receipt of nationally-sourced dividends, it cannot rely on the argument that there is a need to ensure a balanced allocation between Member States of the power to tax in order to justify the taxation of non-resident UCITS in receipt of such income. As concerns the need to preserve the coherence of the tax system, the AG agreed in general with the argument brought forward by the Danish Government that the direct link between the tax advantage in the form of the exemption from tax at source and its offsetting by means of the immediate taxation of the profits distribution would vanish if that advantage were also granted to UCITS which do not make periodic distributions of their profits. However, the AG considered that such justification was not proportional. For the AG, as the Danish government had conceded that non-resident UCITS may voluntarily satisfy the distribution conditions laid down in Danish legislation, then they should be entitled to enjoy the exemption provided that provided that the non-resident UCITS pay a tax which is equivalent to the one that Danish funds are required to retain as a withholding on the minimum distribution requirement.

AG Wathelet opines that German legislation on taxation of dividends from third countries is in breach of the free movement of capital (*EV*)

On 7 February 2018, AG Wathelet delivered his Opinion in case *EV v. Finanzamt Lippstadt* (Case C-685/16). The case deals with the taxation of dividends received by German companies from non-EU subsidiaries. According to the German legislation, dividends received from domestic companies are exempt from German tax, provided that a minimum of 15% participation is held. Differently, in the case of foreign shareholdings, the exemption is subject to additional rules, notably: the distributing subsidiary mas meet an active business test; the participation should be held uninterruptedly from the beginning to the end of the period at stake; and the exemption is limited to situations where there are no more than three levels in the group structure.

EV is a German resident company which holds several participations in other companies worldwide. During 2009, it received dividends from its Australian subsidiary. EV exempted such income. However, during the course of a tax audit, the German tax authorities considered that such income should be included in EV taxable income. EV considered that the German rules were in breach of the TFEU. The German court decided to refer the question to the CJ.

AG Wathelet started by discussing which freedom was applicable to the present case. In this regard he noted the established CJ case law according to which rules which do not apply exclusively to situations in which the parent company exercises a decisive influence over the company paying the dividends should be analysed based on the free movement of capital. As the German legislation was applicable to situations of a minimum 15% shareholding without any reference to the need of a controlling participation, he concluded that the free movement of capital was applicable in this case.

Subsequently, AG Wathelet assessed whether the standstill clause could be invoked in the present case. In this regard, he recalled that the application of such clause depends on whether situations can be characterized as direct investments. For the AG, the German rules of requiring a minimum of 15% participation can be qualified as a direct investment. However, the AG considered that the standstill clause cannot be invoked in this case. Considering that the German rules on the taxation of foreign dividends were considerably modified from the ones in force on 31 December 1993 - in particular, due to the abolition of the imputation system and the adoption of an exemption system as well as the increase from 10% to 15% participation to benefit from this double taxation relief - the AG concluded that the legislation at stake is not the one existing on 31 December 1993.

Lastly, the AG went to analyse possible justifications for the restriction to the free movement of capital. In this regard, AG Wathelet rejected the justification based on the need to prevent tax avoidance considering that this justification is only accepted when it targets wholly artificial arrangements which is not the situation at stake. Furthermore, the rules at stake create a general and irrefutable presumption of abuse without the taxpayer being given the possibility to demonstrate the existence of commercial reasons. Furthermore. the AG also rejected the need the effectiveness of fiscal supervision as a valid justification considering that there is a treaty in force allowing for mutual assistance in tax matters between Germany and Australia and taking into account that the German government confirmed that there were no difficulties as regards exchange of information with Australia.

AG Sanchez-Bordona considers that Danish legislation allowing a Danish company to deduct losses incurred by foreign PE only in case it opted for the international joint taxation scheme is in breach of the freedom of establishment (*Bevola*)

On 17 January 2018, AG Sanchez-Bordona delivered his Opinion in case *A/S Bevola, Jens W. Trock ApS v Skatteministeriet* (C-650/16). The case deals with the Danish legislation which precludes a Danish company from deducting the losses of a foreign permanent establishment (PE) unless it opts into the international joint taxation scheme.

A/S Bevola is a Danish resident company that had subsidiaries and PEs in a number of Member States including a PE in Finland. Such PE ceased trading in 2009 and relief could not be claimed for its losses in Finland. A/S Bevola applied to deduct such losses in Denmark. The Danish tax authorities refused such deduction considering that Bevola was not entitled to make such deduction because the Danish law did not allow to claim revenue or expenditures attributable to a PE situated in a foreign country unless the company had opted for the international joint taxation scheme. A/S Bevola appealed such decision and the case was referred to the CJ.

The AG started by observing that the *Marks & Spencer* (C-446/03) exception (deduction of cross-border final losses) is a valid starting point for assessing whether Danish law is compatible with EU law. For the AG, there are two issues at stake that were not dealt with by the Court in *Marks & Spencer*. First, the losses which it is sought to deduct in Denmark do not come from a subsidiary but from a non-resident PE in Denmark. Second, the Danish tax system does not absolutely preclude the deduction of those losses, and allows it if a resident company opts for the international joint taxation scheme. The two issues call for separate analysis.

Concerning the first issue, the AG was of the view that, as a general rule, the tax treatment of non-resident PEs and foreign subsidiaries must be equivalent as far as the deduction of definitive losses that cannot be absorbed in the PE's State of establishment is concerned. Furthermore, regarding the objective comparability of resident and non-resident PEs, the AG considered them to be comparable. For the AG, the solution adopted by the Court in cases *Nordea Bank Danmark* (C-48/13) and in *Timac Agro Deutschland* (C-388/14) automatically leads to denial of the objective comparability. The losses examined in those cases were incurred year after year, which promoted the 'cherry picking' of the most favourable periods; by contrast, Bevola's PE was faced with losses in the final year of its existence, the year in which it closed. That for the AG is a decisive factor: when definitive losses are those of a non-resident PE, they may not be transferred to any entity within the State in which that PE was situated. Accordingly, as those losses cannot be deducted from the basis of assessment of the company which set up the PE, they will be left in a vacuum. The AG remarked that is precisely the situation envisaged by the *Marks & Spencer* exception, the application of which is particularly justified when the definitive losses of a non-resident PE are identified as entailing, for the proprietor company, a reduction in its assets which is reflected in a reduction in its economic and, therefore, taxpaying capacity. Accordingly, in the case of definitive losses associated with the closure of a PE, the analysis of the objective comparability of the situations must not lose sight of that factor. The situation of a resident PE and that of a non-resident PE, both having definitive losses, are, specifically for that reason,

comparable from the point of view of the principle of the taxpaying capacity of the parent company. For the AG, there is a difference between this case and the cases *Nordea Bank Danmark* and *Timac Agro Deutschland*. In those two judgments, the comparability of resident and non-resident PEs was based on the existence of provisions from which a link was derived between the non-resident PE and the tax authority of the State of the company responsible for the PE. Here, that link arises as a result of a definitive loss, which must be imputed to the company which has sustained a financial loss as a result, so that the tax levied on that company reflects its actual taxpaying capacity.
Furthermore, and as regards the international joint taxation scheme, the aim of the Danish law does not appear to be to 'prevent or mitigate the double taxation of a resident company's profits', unlike the situation in the judgments in *Nordea Bank Danmark* and *Timac Agro Deutschland*.

As concerns the second issue, the AG analysed whether the fact that the Danish legislation offers resident companies the opportunity of opting into the international joint taxation scheme, with the consequent possibility of deducting, in the context of that scheme, the definitive losses of non-resident subsidiaries and PEs, is enough to counter the breach to the freedom of establishment. The AG noted that a tax scheme which, allows group relief but does not provide for the option of delimiting the 'dimensions of group relief', because it requires all companies and *all* PEs in the group to be part of the scheme, certainly prevents a parent company from 'cherry picking' non-resident entities' profits. However, for the AG the risk that such 'cherry picking' will occur in a case of this kind is minimal. In the present case, the tax year in question was the final year of trading in Finland for Bevola's PE; that is, the year in which the PE closed. Therefore, it is not a situation readily comparable to other situations in which a parent company, which has non-resident subsidiaries or PEs whose survival is in doubt, decides for its own convenience to deduct the losses incurred by the latter.
According to the AG, the solution adopted by the Danish legislature to counteract the *Marks & Spencer* exception is disproportionately onerous for undertakings which, under the protection of Article 49 TFEU, wish to exercise their freedom of establishment in other Member States. That the application of the scheme is optional does not stop it from being excessively restrictive or possibly incompatible with EU law.

Furthermore. the AG added that the minimum period of 10 years during which the international taxation scheme must apply is also disproportionate and constitutes a significant unjustified obstacle to the exercise of the option. In view of the events that may affect the composition of the group (transfers or conversions - substantial or otherwise - of the entities which form part of it), the AG was not persuaded by the Danish Government's line of argument on the necessity of fixing such a long period in order to prevent 'cherry picking'. For the AG, the unwanted conduct which it seeks to combat (the selection of the periods in which the group makes global losses and the exclusion of tax years in which it makes a profit) could be avoided, for example, by requiring the selection of the international joint taxation scheme to be made some time in advance of the tax year in which the scheme will be applied, without requiring participation in the scheme for such a long period, which is unrealistic with regard to the lifespan of a company.

VAT

CJ rules on input VAT deduction right of company placed under liquidation (*Wind Inovation*)

On 9 November 2017, the CJ delivered its judgment in the case *Wind Inovation 1 EOOD* ('Wind Inovation', C-552/16,). Wind Inovation is a Bulgarian company in liquidation. Gräss Solartechnik GmbH & Co. KG ('Gräss Solartechnik') is the sole shareholder of Wind Inovation. Kühling Stahl- und Metallbau GmbH ('Kühling Stahl- end Metallbau') had a claim against Gräss Solartechnik. Since the latter had not settled its debt, Kühling Stahl- end Metallbau sought, in accordance with Bulgarian law, the dissolution of Wind Inovation. The assets of Wind Inovation were to be applied to satisfy the claim of Kühling Stahl- und Metallbau. The tax authorities established that the termination of trading of Wind Inovation and the status 'under liquidation' had been registered in the companies register. Subsequently, the tax authorities issued a notice removing Wind Inovation from the VAT register. After receiving the notice of removal, Wind Inovation submitted a new application for VAT registration, specifying that it had not ceased trading and that, even at the time of the registration of its liquidation in the companies register, its turnover exceeded the threshold value for compulsory VAT registration.

Wind Inovation declared the VAT on its available assets in its VAT return. Subsequently, it submitted an objection against the notice of removal from the VAT register. That objection having been dismissed, Wind Inovation brought an action before the Administrative Court. The Administrative Court decided to stay the proceedings and to refer to the CJ for a preliminary ruling. By its questions, the referring court wished to ascertain whether the EU VAT Directive precludes national legislation, pursuant to which compulsory removal from the VAT register of a company results in the obligation to declare VAT on available assets on the date of dissolution, even where the dissolved company remains party to contracts in force and states that it has not ceased its activity during the period of its liquidation, and which, therefore, makes the right to deduct subject to compliance with that obligation.
The CJ recalled that when a company ceases to carry on a taxable economic activity (except in cases of a transfer of a going concern), the retention of goods by a taxable person may be treated as a supply of goods for consideration, where those goods have given rise to a deduction. This concerns the cessation of taxable economic activities in general and therefore also covers the cessation of the taxable economic activity resulting from the removal of the taxable person from the VAT register. However, according to the CJ, this applies only in the situation the taxable economic activity has ceased and where that person no longer carries out taxable transactions. Therefore, the CJ ruled that if a company continues to generate turnover by carrying out economic activities, that company must be considered to have the status of a taxable person and consequently cannot be required, in order to be able to deduct the VAT calculated on its available assets, to pay the amount of VAT thus calculated. Such an obligation constitutes a restriction on the right to deduct and is therefore contrary to the EU VAT Directive.

CJ rules on reduced VAT rate for pastry goods, cakes and similar goods (*AZ*)

On 9 November 2017, the CJ delivered its judgment in the case *AZ* (C-499/16). AZ is a Polish company which produces pastry goods and cakes with a use-by date exceeding 45 days. Polish national law provides for the application of the reduced VAT rate for fresh pastry goods and cakes whose best-before or use-by date does not exceed 45 days. AZ's products been classified in 2010 as 'preserved' within the meaning of national legislation. However, despite the use-by date of AZ's products exceeding 45 days, the Director of the Customs Chamber classified AZ's products as 'fresh' in 2013.

In response to the qualification of its products by the Director of the Customs Chamber, AZ requested the Minister of Finance for a VAT ruling in order to determine whether it was entitled to apply the reduced VAT rate. AZ, in its application, submitted that national law, contrary to EU law, inserts a criterion for applying the reduced VAT rate which does not follow from the EU VAT Directive or the combined nomenclature. The Minister of Finance did not uphold the view taken by AZ and held that the Polish legislature could legitimately adopt a criterion for applying the reduced VAT rate at issue. AZ brought an action against that decision. Finally, the matter ended up with the Supreme Administrative Court of Poland, which decided to stay the proceedings and to refer to the CJ for a preliminary ruling. By its question, the referring court wished to establish whether national legislation, in the light of the EU VAT Directive and the principle of fiscal neutrality, may let the application of the reduced VAT rate on fresh pastry goods and cakes solely depend on the criterion of their best-before or 'use-by date.

The CJ ruled that in so far as the criterion relating to a certain number of days of shelf life precisely defines the category concerned, the selective application of the reduced VAT rate must, in principle, be found compatible with the EU VAT Directive. However, the principle of fiscal neutrality precludes similar goods or services which are in competition with each other being treated differently for VAT purposes. The CJ ruled that it is for the referring court to assess if, on the Polish market, there are pastry goods or cakes whose shelf life does not exceed 45 days but which, nevertheless, are similar in the eyes of the average consumer to pastry goods and cakes which have a best-before date exceeding 45 days, such as those produced by AZ, and which are interchangeable with the latter. If such goods are found to exist, a shelf life of less than 45 days would not be determinative for the average Polish consumer and that consumer's choice might be affected by the application of different VAT rates. In such a situation, the principle of fiscal neutrality would preclude the national provisions at issue.

CJ rules that undertaking eligible for a tax deduction scheme in its home EU Member State could not rely on a right to deduct input VAT due or paid (*EBS*)

On 15 November 2017, the CJ delivered its judgment in the case *Entertainment Bulgaria System EOOD* ('EBS', C-507/16). EBS is a company established in Bulgaria that provides internet services, such as website design, multimedia development and graphic design. EBS is registered for VAT purposes in Bulgaria. This registration is based on Article 97a (2), of the Bulgarian VAT Act, that provides for the registration of persons established in Bulgaria who supply services to taxable persons established in the territory of other EU Member States. EBS received services supplied by taxable persons established in the territory of EU Member States other than Bulgaria, which it used to provide services in other EU Member States and Switzerland. Based on the reverse charge mechanism, EBS declared the VAT on these purchased services and subsequently deducted this input VAT. During a tax inspection, the tax authorities established that EBS had reached the turnover threshold beyond which undertakings no longer benefit from the Bulgarian VAT exemption and must, under a national provision, register for VAT purposes.

The tax authorities imposed a tax assessment on the ground that national law prohibits deduction of input VAT for taxable persons that are registered based on Article 97a of the Bulgarian VAT Act. The tax authorities imposed a VAT assessment and default interest. EBS lodged a request for annulment of the VAT assessment. The case ended up before the Administrative Court of Bulgaria. The Administrative Court decided to stay the proceedings and to refer to the CJ for a preliminary ruling. By its questions the referring court wished to ascertain whether the EU VAT Directive precludes national legislation that prevents a taxable person from deducting input VAT due or paid in its home EU Member State in respect of services provided by taxable persons established in other EU Member States and used to provide services in other EU Member States, on the ground that that taxable person is registered for VAT purposes under Article 97a of the Bulgarian VAT Act.

The CJ ruled that the EU VAT Directive precludes legislation of an EU Member State that prevents a taxable person, such as in the main proceeding, deducting input VAT due or paid, on the ground that that taxable person is identified for VAT purposes pursuant to one of the two circumstances referred to in Article 214(1)(d) and (e) of the EU VAT Directive. However, since EBS was no longer eligible for the tax deduction scheme in Bulgaria, given the amount of its turnover, it could no longer be identified for VAT purposes, but had to fall within the 'mandatory' registration scheme in Bulgaria. According to the CJ, an undertaking established in the territory of an EU Member State and eligible for a tax deduction scheme in that EU Member State could not rely on a right to deduct input VAT due or paid. Furthermore, according to the CJ, the EU VAT Directive must be interpreted as meaning that it does not preclude legislation of an EU Member State that prevents a taxable person, such as the one at hand, from exercising its right to deduct input VAT due or paid in that EU Member State for services provided by taxable persons established in other EU Member States and used to provide services in EU Member States other than the EU Member State in which that taxable person is established.

CJ rules that EU VAT Directive precludes national legislation which makes right to deduct input VAT subject to indication on the invoice of the address where the issuer carries out its economic activity (*Geissel & Butin*)

On 15 November 2017, the CJ delivered its judgment in the joined cases *Rochus Geissel v Finanzamt Neuss and Finanzamt Bergisch Gladbach v Igor Butin* ('Geissel & Butin', C-374/16 and C-375/16). Geissel is the liquidator of RGEX GmbH i.I. RGEX is a limited liability company that traded in motor vehicles. That company has been in liquidation since 2015. In its VAT return for 2008, RGEX declared VAT exempt intracommunity supplies of motor vehicles and input VAT deductions relating to 122 motor vehicles obtained from EXTEL GmbH. The German tax authorities did not accept RGEX's VAT return and took the view that the intracommunity supplies of motor vehicles to Spain, which had been declared as VAT exempt, were taxable on the ground that the motor vehicles had been sold in Germany. Moreover, the input VAT deductions claimed on the basis of invoices issued by EXTEL were denied, because the latter was considered a 'ghost company', which did not have any establishment at the address mentioned on the invoice.

Mr Igor Butin, who runs a dealership in Germany, relied on invoices to deduct input VAT for a number of vehicles acquired from an undertaking 'Z', and destined for resale. The vehicles were delivered to Mr Butin or his employees, sometimes at the place where Z had its registered office - even though Z did not run a dealership from that address - and sometimes in public places. In the course of a tax audit carried out on Mr Butin, the German tax authorities concluded that the input VAT paid on the invoices issued by Z could not be deducted because the supplier address given by Z on those invoices was incorrect. It was found that the address served merely as a 'letterbox address' and that Z had no fixed establishment in Germany.

The Finance Court, before which court the cases of RGEX GmbH and Igor Butin ended up, decided to stay both proceedings and to refer to the CJ for a preliminary ruling. By its questions, the referring court asks whether the EU VAT Directive precludes national legislation that subjects the right to deduction of VAT to the indication on the invoice of the address where the issuer carries out its economic activity.

The CJ ruled that it is not possible for EU Member States to lay down more stringent requirements than those under the EU VAT Directive. Consequently, it is not allowed for EU Member States to make the exercise of the right to deduct input VAT dependent on compliance with conditions relating to the content of invoices which are not expressly laid down by the provisions of the EU VAT Directive. Furthermore, in the case *PPUH Stehcemp* (C-277/14) the CJ ruled that the fact that no economic activity could be carried out at that company's seat does not mean that that activity could not be conducted in places other than the company's seat. Therefore, the CJ ruled that for the purposes of the exercise of the right to deduct input VAT by the recipient of goods or services, it is not a requirement that the economic activities of the supplier be carried out at the address indicated on the invoice issued by that supplier.

CJ rules on VAT exemption for upgraded buildings (*Kozuba*)

On 16 November 2017, the CJ delivered its judgment in the case *Kozuba Premium Selection sp. z o.o.* ('Kozuba', C-308/16). Kozuba is established in Poland. On 17 September 2005, Kozuba decided to increase its share capital. On the same day, one of the associates contributed to the company a residential building built in 1992 and situated in Poland. In 2006, the building in question was adapted for the purposes of the economic activity carried out by Kozuba, the latter having agreed for that purpose to investments of up to, approximately, 55% of the initial value of the building. After the works were completed, the building in question was registered on 31 July 2007 as a separate fixed asset in the fixed assets register. On 15 January 2009, the building was sold to a third party. As it concerned an old building, Kozuba considered that the sale was VAT exempt and did not declare the profit on that sale.

The tax authorities, however, took the view that Kozuba had to include the profit from the sale given that the costs incurred for the upgrade constituted at least 30% of the initial value and therefore, should be regarded as a supply for 'first occupation'. Kozuba lodged an appeal against that decision before the Director. According to the Director, Kozuba could not claim the VAT exemption for the supply of 'old' buildings, as that sale had been made in the context of the first occupation of the building in question. Kozuba lodged an appeal against that decision. The case finally ended up before the Supreme Administrative Court of Poland which decided to stay the proceedings and to refer to the CJ for a preliminary ruling. By its question, the referring court wished to ascertain whether the EU VAT Directive precludes national legislation under which the exemption of supplies of buildings from VAT is subject to two conditions, namely that the supply is not made in the context of a first occupation arising in the course of a taxable transaction and that, in the case of the upgrade of an existing building, the costs incurred for that purpose are less than 30% of the initial value of that building.

According to the CJ, the EU VAT Directive makes a distinction between the sale of old buildings and new buildings. The sale of an old building is, in principle, not subject to VAT. However, the EU VAT Directive allows EU Member States to lay down the detailed rules for applying the criterion of 'first occupation', to the conversion of buildings. In that way, the EU VAT Directive makes it possible to tax supplies of buildings that have been converted. However, according to the CJ, this cannot be interpreted as meaning that EU Member States have a discretion that allows them to alter the concept of 'first occupation' itself in their national laws, without harming the effectiveness of that exemption. The CJ ruled that the building concerned must have been subject to substantial modifications intended to modify the use or alter considerably the conditions of its occupation. Therefore, according to the CJ, it is for the national court, to assess on the basis of the evidence available to it, the extent to which the 'upgrade' at issue in the main proceedings led to a substantial modification of that building.

CJ rules on artificial transactions and abuse of law (*Cussens and others*)

On 22 November 2017, the CJ delivered its judgment in the case *Cussens, Jennings and Kingston* ('Cussens and others', C-251/16). The case concerns abuse of law. The appellants were co-owners of a development site in Ireland on which they constructed 15 holiday homes for sale. Before making the sales, the appellants carried out a number of transactions with a related company, Shamrock Estates Limited ('SEL'). The appellants entered into a lease for the properties with SEL for 20 years and one month ('long-term lease'). The properties were leased back to the appellants for two years ('short-term lease'). Almost a month later both leases were mutually surrendered by the parties and full ownership of the properties reverted back to the appellants. Subsequently, the appellants sold the properties to third party buyers. According to the national legislation at issue, VAT was chargeable only on the long-term lease.

The Irish tax authorities asked the appellants to pay additional VAT in respect of the property sales. The tax authorities took the view that the leases at issue, provided for the lease and leaseback of the properties, constituted a first supply artificially created in order to avoid the subsequent sales being liable to VAT and that supply should therefore be disregarded for VAT purposes. The appellants challenged the VAT assessment imposed and the case was eventually brought before the Irish Supreme Court. The Supreme Court decided to stay the proceedings and to refer to the CJ for a preliminary ruling seeking guidance on the conditions for abuse of law. Furthermore, it asked how the relevant transactions are to be redefined if the principle of prohibition of abuse of law applies in this case.

According to the CJ, it is settled case law that a taxable person who has created conditions for obtaining a right in a fraudulent or abusive manner is not justified in relying on the principles of legal certainty and the protection of legitimate expectations pursuant to the principle that abusive practices are prohibited. If the transactions at issue should be redefined pursuant to the principle that abusive practices are prohibited, those of the transactions which do not constitute such a practice may be subject to VAT on the basis of the relevant provisions of national legislation providing for such liability. The CJ ruled that in order to determine whether the essential aim of the transactions at issue is to obtain a tax advantage, account should be taken of the objective of the leases preceding the sales of immovable property in isolation. According to the CJ, the supplies of immovable property are liable to result in the accrual of a tax advantage contrary to the purpose of the relevant provisions of the EU Sixth Directive where the properties had, before their sale to third party purchasers, not yet been actually used by their owner or their tenant. Furthermore, the CJ ruled that the principle that abusive practices are prohibited applies in a situation such as at hand, which concerns the possible exemption of a supply of immovable property from VAT.

CJ rules that EU Member State may not make reduction of VAT taxable amount subject to condition that insolvency proceedings have been unsuccessful when such proceedings may last longer than ten years (*Enzo Di Maura*)

On 23 November 2017, the CJ delivered its judgment in the case *Enzo Di Maura* (C-246/16). Due to the fact that one of Mr Di Maura's clients was declared bankrupt without paying an invoice of EUR 35,000, Mr Di Maura made a corresponding reduction of his VAT taxable amount.

The Italian tax authorities did not approve that adjustment on the basis that such an adjustment could be carried out only after the failure of insolvency proceedings or of individual enforcement proceedings, that is to say only once it had become certain that the debt would not be honoured, and not following a simple judgment declaring insolvency, such as that to which Mr Di Maura's debtor was subject. Mr Di Maura brought an action before the Italian Provincial Tax Court and argued that, on the contrary, the reduction of the taxable amount on account of the non-payment of the consideration must be possible to achieve at the time when the debtor is declared bankrupt. The Tax Court decided to stay the proceedings and to refer to the CJ for a preliminary ruling. With its questions the referring court specifically asked whether an EU Member State may make the reduction of the taxable amount for VAT in the event of total or partial non-payment subject to the condition that insolvency proceedings have been unsuccessful when such proceedings may last longer than ten years.

According to the CJ, it follows from the EU Sixth Directive that cases of cancellation, refusal or total or partial non-payment, or where the price is reduced after the supply takes place, require the EU Member States to reduce the taxable amount and, consequently, the amount of VAT payable by the taxable person whenever, after a transaction has been concluded, part or all of the consideration is not received by the taxable person. However, EU Member States are allowed to derogate from this rule in situations of total or partial non-payment. This power to derogate is based on the notion that non-payment of consideration may be difficult to establish or may only be temporary and has the objective to take account of the inherent uncertainty of the definitive non-payment of an invoice. The CJ ruled that the same objective could, equally effective but less onerous to the taxable person, be pursued by granting the reduction when the taxable person demonstrates a reasonable probability that the debt will not be honoured, even if the taxable base is re-evaluated upwards in the event that payment nonetheless occurs. Therefore, according to the CJ, an EU Member State may not make the reduction of the VAT taxable amount in the event of total or partial non-payment subject to the condition that insolvency proceedings have been unsuccessful when such proceedings may last longer than ten years.

CJ rules on UK derogation measure regarding direct selling system (*Avon Cosmetics*)

On 14 December 2017, the CJ delivered its judgment in the case *Avon Cosmetics Ltd* ('Avon Cosmetics', C-305/16). Avon Cosmetics is engaged in the manufacturing and sale of products, mostly cosmetics. Avon Cosmetics uses a direct selling model in the United Kingdom. Under that model, Avon Cosmetics sells its products to its representatives, the Avon Ladies, who in turn, make retail sales to their customers at mark up. The threshold for compulsory VAT registration in the United Kingdom is GPB 100,000. Some Avon Ladies have chosen to VAT register. However, many remain below the threshold for compulsory registration and have chosen not to register. As a result, the profit margins made by those unregistered Avon Ladies would normally not be subject to VAT. So, VAT is charged on the wholesale price, but not on the retail profit margin earned by the unregistered Avon Ladies.

In order to address the problem of the lost VAT arising from the use of the direct selling model, the United Kingdom obtained a derogation from the standard rule that VAT must be charged on the actual sales price. The derogation essentially allows the tax authorities, in cases where the direct selling model is used, to charge VAT not on the wholesale price (which in this case is the price paid to Avon Cosmetics), but rather on the retail price paid by the end customer to the reseller, that is, to the Avon Ladies. The dispute with the tax authorities arises in relation to demonstration products. For VAT registered retailers, the VAT paid on the purchase of those products would normally have been refunded. However, those cost are not taken into account in the application of the derogation. As a result, the impact of VAT in relation to sales made through unregistered Avon Ladies is greater than the impact in the few cases where Avon Ladies are registered. Avon Cosmetics disputes the way the derogation is being applied by the tax authorities. The case ended up before the Tax Chamber which decided to stay the proceedings and to refer to the CJ for a preliminary ruling. By its questions, the referring court essentially asked whether the derogation with respect to the demonstration products infringes the EU VAT Directive.

The objective of the derogation measure is to prevent tax avoidance and to enable the United Kingdom to remedy certain specific problems caused by the direct selling system so far as it concerns VAT. According to the CJ, the derogation measure appears appropriate. The fact that the measure does not take into account the input VAT relating to demonstration items purchased by non-taxable resellers from a direct sales company is merely the consequence of the choice made by such a company to use the direct selling system to market its products. Therefore, according to the CJ, it must be held that the measure effects the principle of neutrality as little as possible.

CJ rules that pharmaceutical company should be allowed to reduce taxable amount in case of discount fixed by law (*Boehringer*)

On 20 December 2017, the CJ delivered its judgment in the case *Boehringer Ingelheim Pharma GmbH & Co. KG* ('Boehringer', C-462/16). Boehringer is a pharmaceutical company which manufactures medical products and supplies those products, subject to VAT, to pharmacies via wholesalers. In Germany, two separate systems exist. In the first system, the pharmacies issue pharmaceutical products to the public health insurance funds and the latter make them available to persons insured by them. The pharmacies grant the public health insurance funds a discount on the price of the medicinal products. In the second system, the pharmacies issue pharmaceutical products directly to persons with private health insurance pursuant to individual contracts with them. In the first system, the pharmaceutical company is, pursuant to German law, held to grant a discount on the price for the medicines to the pharmacies (or to the wholesaler who on their turn have to pass the discount to the pharmacies). These discounts are treated, for VAT purposes, in each stage as a rebate on the purchase price and therefore, lower the amount of VAT due in each stage. The German tax authorities treat this discount for VAT purposes as a reduction of the consideration. In the second system, the private health insurance funds are not themselves the customer of the medicinal products, but merely reimburse the persons insured by it for the costs incurred when they purchase pharmaceutical products. Also in this situation pharmaceutical companies are then bound, pursuant to German law, to grant the private health insurance funds a discount on the price of the medicinal products. The German tax authorities, however, do not treat this discount as reduction of the consideration for VAT purposes based on the argument that the private health insurer was never part of the supply chain.

The case ended up before the German Federal Finance Court who decided to stay the proceedings and to refer to the CJ for a preliminary ruling. By its question, the referring court asked whether or not a pharmaceutical company which supplies medicinal products is entitled to a reduction of the VAT taxable amount in the case were:

- it supplies those medicinal products to pharmacies via wholesalers,
- the pharmacies supply those products, subject to VAT, to persons with private health insurance,
- the insurer of the medical expense insurance (the private health insurance company) reimburses the persons insured by it for the costs of purchasing the medicinal products, and
- the pharmaceutical company is required to pay a 'discount' to the private health insurance company pursuant to a statutory provision.

According to the CJ, the question referred is to be answered in the affirmative. The CJ ruled that as a result of national legislation, pharmaceutical companies could only dispose of a sum corresponding to the sales price of those products, reduced by that discount. Therefore, according to the CJ, it would not be in conformity with the EU VAT Directive and the principle of neutrality if the discount is disregarded, as in that case, the taxable amount exceeds the amount finally received by the pharmaceutical company. Furthermore, the fact that the direct beneficiary of the supplies of the medicinal products in question was not the private health insurance company which reimbursed the insured person but the insured persons themselves, is not such as to break the direct link between the supply of the goods made and the consideration received. Therefore, the CJ ruled that a pharmaceutical company should be allowed to reduce the taxable amount, since the discount is fixed by law and the pharmaceutical company therefore was not able to dispose freely of the full amount received on the sale of its products to pharmacies (or wholesalers).

CJ rules that principles of equivalence and effectiveness allow a refund request of VAT levied in breach of EU law to be refused where that request was submitted after the expiry of the limitation period (*Caterpillar*)

On 20 December 2017, the CJ delivered its judgment in the case *Caterpillar Financial Services sp. z.o.o.* ('Caterpillar', C-500/16). Caterpillar operates as lessor and concludes leasing agreements. Caterpillar offers its lessees the possibility to provide them with insurance covering the leased objects. After the lessees express their wish to benefit from that possibility, the insurance contracts are taken out with an insurance company by Caterpillar, which bears the costs incurred in concluding those contracts, but charges the lessees the costs of the insurance contributions, without adding any mark-up. Caterpillar exempted those contributions from VAT in the invoices it issues to its lessees. Following a judgment of the Supreme Administrative Court of Poland, in which it was held that the person providing the leasing service must include in the taxable amount of those services the costs of insuring the leased object, Caterpillar submitted corrected invoices stating the amounts relating to VAT arrears, plus interest and paid the VAT on the corresponding insurance contributions. After the CJ delivered the BGZ Leasing judgment (17 January 2013, C-224/11), Caterpillar requested the tax authorities for a refund of the subsequent paid VAT.

The tax authorities refused to initiate the procedure for refunding an overpayment of VAT on the ground that the five-year limitation period had expired. The case ended up before the Supreme Administrative Court of Poland. According to the Supreme Administrative Court, Polish law does not provide for any legal basis allowing a party, who has relied on national institutions for a finding that VAT was payable, to receive a refund of that VAT, levied in infringement of EU law by the tax authorities, after the expiry of the limitation period for the right to submit such a request for a refund. The Supreme Administrative Court decided to stay the proceedings and to refer to the CJ for a preliminary ruling. By its question, the referring court asked whether the principles of equivalence and effectiveness must be interpreted as precluding a national legislation which allows a request for a refund of overpayment of VAT to be refused under circumstances as in the case at hand.

According to the CJ, it is settled case law that the interpretation which the CJ gives in its judgments, should be regarded such to clarify and to define the meaning and scope of a rule of EU law as it should have been understood and applied from the time of its entry into force. Furthermore, it follows from settled case law that the right to a refund of charges levied in a EU Member State in breach of the rules of EU law is the consequence and complement of the right conferred on individuals by provisions of EU law as interpreted by the CJ. The EU Member State is therefore required, in principle, to repay charges levied in breach of EU law. In the absence of harmonized rules governing the reimbursement of charges imposed in breach of EU law, the EU Member States retain the right to apply procedural rules provided for under their national legal system, in particular concerning limitation periods, subject to observance of the principles of equivalence and effectiveness. The CJ ruled that as the Polish limitation rule applies in the same way both to domestic actions and to actions seeking safeguard rights which individuals derive from EU law, it cannot be considered to be contrary to the principle of equivalence. Furthermore, according to the CJ, it is compatible with EU law to lay down reasonable time limits for bringing proceedings in the interest of legal certainty which protects both the individual and the authorities concerned, even if the expiry of those periods necessarily entails dismissal of the action. By way of example, limitation periods of two or three years have been held to be compatible with the principle of effectiveness.

CJ rules that a single supply consisting of one principal and one ancillary element must be taxed at VAT rate applicable to principal element (*Stadion Amsterdam*)

On 18 January 2018, the CJ delivered its judgment in the case *Stadion Amsterdam CV* ('Stadion Amsterdam', C-463/16). Stadion Amsterdam acts as an operator of a multi-purpose building complex, known as 'the Arena'. The Arena consists of a stadium with associated facilities and a museum of the football club AFC Ajax. Stadion Amsterdam offers a so-called 'World of Ajax tour'. This tour consists of a guided tour of the stadium and a visit, without a guide, to the AFC Ajax museum. The World of Ajax tour was the only opportunity for visitors to visit the AFC Ajax museum. It was therefore not possible for visitors to visit the museum without participating in the guided tour of the stadium. The tour was offered for a total price of EUR 10. At the time of the proceeding, the reduced VAT rate was applicable for the admission to public museums, theme parks, playgrounds and other similar facilities that are primarily and permanently intended for entertainment and daytime recreation. Stadion Amsterdam took the view that the guided tour should be considered a service intended for entertainment and that the reduced VAT rate, therefore, was also applicable to the guided tour.

The Netherlands tax authorities however took the view that the World of Ajax tour was subject to the normal VAT rate. Stadion Amsterdam challenged that view and the case eventually ended up before the Netherlands Supreme Court. The Netherlands Supreme Courts stated that it was clear from the national proceedings that the World of Ajax tour consists of two elements, namely the guided tour of the stadium and the visit to the AFC Ajax museum. In this respect, the guided tour should be considered the principal component and the museum visit the ancillary component of one single supply. The Netherlands Supreme Court also stated that in the case the two elements of the services are separated, EUR 6.50 of the total price should be attributed to the guided tour and EUR 3.50 to the museum visit. The Netherlands Supreme Court eventually decided to stay the proceedings and to refer to the CJ for a preliminary ruling. By its question, the referring court wished to ascertain whether a single supply that is comprised of one principal and one ancillary element, which, if they were supplied separately would be subject to different VAT rates, must be taxed to the rates of VAT applicable to those separate elements or to one single VAT rate.

The CJ considered that it follows from EU case law that every transaction must normally be regarded as being distinct and independent and that a transaction which comprises a single supply from an economic point of view should not be artificially split in order not to cause any distortion of the EU VAT system. According to the CJ, it follows from the characterization of a transaction with several elements as a single supply that that single supply will be subject to one and the same VAT rate. If EU Member States would have the option to subject various elements of one singe supply to different VAT rates, it would cause artificially splitting of that supply which leads to a risk of distortion of the function of the EU VAT system. The CJ ruled that a single supply consisting of two distinct elements, one principal and one ancillary, which, if they were supplied separately, would be subject to different VAT rates, must be taxed solely at the VAT rate applicable to the principal element of the single supply. The facts that the price of each element of the supply can be identified does not result in a different conclusion.

CJ rules that fraudulent intent of supplier should not have consequences for VAT deduction right of recipient, unless recipient was aware of fraudulent intent (*Kollroß and Wirtl*)

On 30 January 2018, the CJ delivered its judgment in the joined cases *Achim Kollroß and Erich Wirtl* ('Kollroß and Wirtl', C-660/16 and C-661/16). The first case concerned Mr Kollroß who has ordered a combined heat and power unit from company G. Company G confirmed the order of Mr Kollroß two days later and issued an advance invoice with VAT to Mr Kollroß. Mr Kollroß paid the invoice one week after receipt. However, the delivery date of the unit was not yet clear at that time. Eventually, the unit was never supplied to Mr Kollroß. The second case covers a comparable situation. Also Mr Wirtl ordered a combined heat and power unit from company G. The expected delivery date of the unit was two weeks after payment. Mr Wirtl paid the full amount including VAT, but the unit was never supplied to Mr Wirtl. In both cases, Company G became subject of insolvency proceedings. This procedure was closed on the ground of a lack of assets. The persons acting for G were convicted of different criminal offences. However, those persons were not convicted of tax evasion.

Mr Kollroß and Mr Wirtl claimed a VAT deduction for the VAT that they have paid to company G. The tax authorities refused the VAT deductions of Mr Kollroß and Mr Wirtl. Both unsuccessfully lodged objection against that decision. The cases eventually ended up before the Federal Finance Court in Germany. This court decided to stay both proceedings and refer them to the CJ for a preliminary ruling. By its questions, the referring court essentially asked whether a taxable person is entitled to deduct input VAT on purchased goods that have never been supplied to the taxable person as a result of fraud on the side of the supplier. Furthermore, the referring court wished to ascertain to what extend it is allowed to require a taxable person to adjust its input VAT deductions.

The right to deduct input VAT arises at the time the VAT becomes chargeable. The general rule is that VAT becomes chargeable when the goods or the services are supplied. However, where payments are made on account, VAT becomes chargeable upon receipt of the payment and on the amount received. According to the CJ, fraudulent intent of the supplier should not have any consequences for the VAT deduction right of the recipient, unless the recipient was or should have been aware of the fraudulent intent. Furthermore, the fact that there is no date of delivery is irrelevant in this respect. With respect to the second question, it needs to be held that the taxable person could never use the purchased goods for its taxable activities. It follows from the EU VAT Directive that in that case an adjustment of the deducted input VAT is required. However, such adjustment is optional in the case of 'theft of property'. In other words, an adjustment is not required unless an EU Member State decides otherwise. According to the CJ, fraud should be regarded 'theft of property'. Therefore, the CJ ruled that a derogation from that principle is allowed when the failed delivery of the goods purchased is due to a fraud perpetrated by the supplier. In such situation, the taxable person's expenditure relates to his economic activities. The facts that those goods were ultimately not used for the purposes of taxable transactions is purely accidental.

AG opines that EU Member State is allowed to consider that normal VAT regime applies in case a taxable person does not explicitly chooses for special scheme (*Dávid Vámos*)

On 23 November 2017, AG Wahl delivered his Opinion in the case *Dávid Vámos* (C-566/16). From 2007 until 22 January 2014, Mr Dávid Vámos made 778 sales of electronic items on two online platforms. He did not register as a VAT taxable person and did not declare the income from these sales. The Hungarian tax authorities carried out an inspection in respect of Mr Vámos. The tax authorities found that Mr Vámos had not complied with the obligation to register as laid down in the national legislation, as a result of which they imposed on him a financial penalty. On 22 January 2014, Mr Vámos registered as VAT taxable person and opted for the Hungarian VAT exemption scheme for small enterprises. Independently of the first inspection, the tax authorities carried out a second inspection with regard to Mr Vámos' VAT returns for the years 2012 to 2014. As a result, the tax authorities found a VAT debt and imposed on Mr Vámos financial penalties and interest for late payment.

As far as the VAT exemption is concerned, the tax authorities took the view that national law did not allow taxable persons to opt for that exemption retroactively. Mr Vámos challenged that decision before the Administrative and Labour Court arguing that the tax authorities should have asked him whether he wished to opt for the application of the VAT exemption to the sales he made before registering as taxable person, given that he complied with the material conditions to benefit from the scheme. The Administrative and Labour Court decided to stay the proceedings and to refer to the CJ for a preliminary ruling. By its question the referring court asks whether the EU VAT Directive precludes national legislation that makes it impossible for a taxable person to request a retroactive application of the exemption scheme when the taxable person fulfilled all the material requirements for it, but did not declare the commencement of his activities at the appropriate time and did not explicitly opt for the application of that scheme.

The AG opined that the CJ had ruled in a previous case that the requirement under Hungarian law to declare the commencement of activities to the domestic tax authorities is lawful under EU law. According to the AG, the EU VAT Directive does not *explicitly* grant small enterprises an unfettered right to enjoy the application of an exemption scheme. In particular, in the view of the AG, there is no textual basis in the EU VAT Directive for the view that a taxable person should have the right to enjoy such a scheme retroactively, in the absence of an express choice on its part. Furthermore, there is no basis to consider that, when an VAT exemption scheme for small enterprises exists, the application of that scheme to the taxable persons fulfilling the requirements is or should be automatic. Therefore, the AG opined that, as the special schemes for small enterprises constitute an (optional) exception to the ordinary regime, there is no reason why an EU Member State should not be allowed to consider that, in the absence of a choice expressed by the taxable person, the applicable regime should be the normal VAT arrangements.

AG Bobek opines that principle of fiscal neutrality requires EU Member State to recover an unduly granted VAT deduction (*SEB bankas*)

On 20 December 2017, AG Bobek delivered his Opinion in the case *Valstybinė mokesčių inspekcija prie Lietuvos Respublikos finansų ministerijos joined parties: Akcinė bendrovė SEB bankas* ('SEB bankas', C-532/16). SEB bankas purchased plots of land from VKK Investicija UAB ('the seller') for which the latter issued an invoice for payment — inclusive of VAT. At the time of the sale, both parties considered the land at issue to be 'building land', and subject to VAT. Subsequently, SEB bankas obtained a deduction corresponding to the VAT charged. Three years later, the seller took the view that the supply of land at issue should actually have been exempted from VAT. It therefore sent SEB bankas a credit note for the original amount invoiced. It also issued a new invoice for the same amount which did not include any VAT. According to SEB bankas, at the time of the transaction, the land supplied was considered, under national law, to be 'building land' and thus subject to VAT. That followed from the official commentary to the VAT law, published by the State Tax Inspectorate, and from information issued by the tax administration to SEB bankas.

On the basis of a subsequent tax inspection, the Lithuanian tax authorities issued a decision that required SEB bankas to reimburse the amount corresponding to the deduction initially granted. It also required payment of a part of the accrued default interest, and imposed a fine. The case eventually came before the Supreme Administrative Court of Lithuania. This court decided to stay the proceedings and to refer to the CJ for a preliminary ruling. By its questions, the referring court wished to ascertain whether or not the recovery sought from SEB bankas falls under the mechanism of adjustment of deductions provided for in the EU VAT Directive.

The AG opined that the adjustment mechanism provided for in the EU VAT Directive aims to enhance the precision of VAT deductions by monitoring the extent to which the taxable person actually uses those goods for deductible purposes. However, the question is whether that adjustment mechanism can apply to correct an initial error in the determination that a given transaction is a taxable one while it is not. According to the AG, it follows from the EU VAT Directive that the adjustment mechanism does not apply where an initial deduction of VAT could not have been made at all because the transaction at issue was exempted from VAT. However, the AG opined that it follows from the EU VAT Directive that similar goods and services have to bear the same VAT burden and that burden must be imposed equally on taxpayers who are in similar situations. According to the AG, that neutrality is not respected if it is established that a taxable person benefited from an incorrectly granted VAT deduction. The AG, therefore, opined that the principle of fiscal neutrality requires that the EU Member State whose tax authorities have granted that deduction is therefore obliged to make sure that the undue VAT advantage is corrected.

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