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VAT NEWSLETTER

ECJ: Penalties for conduct in breach of contract subject to VAT?

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1 Facts of the case

The plaintiff, in the legal case C-90/20 (*Apcoa Parking Danmark A/S*, ECJ, judgment of 20 January 2022), operates car parks on private land pursuant to contracts with site owners. The car parks are open to the public. The plaintiff manages them and, in particular, lays down the regulations for their use in the general terms and conditions, e.g. duration of parking. The plaintiff charges consideration for the use of some of the parking spaces. A sign at the entrance to the car parks states that the area is operated in accordance with the rules of private law. In the event of a breach of the agreed parking regulations, the plaintiff charges a control fee amounting to the equivalent of approx. EUR 70 (in those cases where regular parking fees are charged, in addition to that fee).

The plaintiff denied that the control fees were liable for VAT. Therefore, the Danish court referred the question to the ECJ as to whether the control fees constituted consideration for a supply of services. This question was expressly limited to the relationship between the plaintiff and the motorists using the car park, from a VAT perspective, and did not concern the relationship between the plaintiff and the car park owners.

2 ECJ decision

The ECJ ruled that the control fees constituted remuneration for a supply of services for consideration. A supply of services is carried out "for consideration" if there is a legal relationship between the supplier and the recipient pursuant to which there is reciprocal performance/ reciprocal supplies for consideration are carried out. In addition, the remuneration must constitute the actual consideration for the identifiable services supplied.

Dr. Thomas Streit, LL.M. Eur.
Lawyer

+49 (0) 89 217 50 12-75
thomas.streit@kmlz.de

In the present case, the payment of parking fees – insofar as a fee was charged by the plaintiff – undoubtedly constituted consideration for the provision of a parking space. However, the control fee for parking in breach of the regulations was also part of the consideration. By choosing to make use of the car park, the motorists had effectively agreed to the parking conditions. These conditions included the payment of the control fee for parking in breach of the regulations. The person parking in breach of the regulations also used a parking space. Thus, there is a direct link between the use of the parking space and the control fee as consideration. The amount of the control fee necessarily takes into account the higher cost of operating car parks which is caused by parking that does not satisfy the normal terms and conditions for use of the service offered.

The fact that the amount of the control fee is predetermined and, according to the plaintiff, does not have any real economic link to the value of the parking service supplied, does not lead to a different conclusion. For the circumstances as to whether the amount of the consideration is higher or lower than the costs incurred by the plaintiff for the provision of the supply of services, is irrelevant.

Even though the control fee qualifies as a penalty under national law, this does not change the fact that it is a consideration from a VAT perspective. The approach taken under Union law is relevant, rather than a national assessment.

3 Consequences for the practice

In its decision, the ECJ interprets the concept of consideration quite broadly. It also deems penalties to qualify as consideration, which the recipient must pay to the supplier, in accordance with the agreement, if he acts in breach of contract.

Regulations on how payments for breach of contract are to be treated for VAT purposes can also be found in the German VAT Circular. The German tax authorities have so far assumed, in sec. 1.3 para. 3 of the German VAT Circular, that contractual penalties are to be regarded as compensation for damages and are therefore non-taxable. The increased transport charge for journeys taken without a ticket (sec. 10.1 para. 3 sentence 11 of the German VAT Circular) or the compensation for reduced value of the car when returning a leasing car (sec. 1.3 para. 17 sentence 2 of the German VAT Circular) have also previously been considered by the tax authorities to be outside the scope of VAT. If the ECJ's requirements are applied, this view could find itself losing ground.

Insofar as the supplier is taxed on the corresponding penalty/damage compensation payments, the recipient must consequently also be entitled to input VAT deduction from the procured goods and services. The supplier, himself, is also entitled to input VAT deduction from his procured goods and services in this regard and this is ultimately independent of whether, in the case of his sales/output transactions, he renders non-taxable or taxable output supplies.

Taxable persons who may have questions about the demarcation between non-taxable penalties/compensation for damages and consideration for supplies of services should think about appropriate VAT clauses when concluding or amending contracts.

KMLZ Rechtsanwaltsgesellschaft mbH | www.kmlz.de | office@kmlz.de
D-80331 München | Unterer Anger 3 | Tel.: +49 89 217501220 | Fax: +49 89 217501299
D-40221 Düsseldorf | Speditionstraße 21 | Tel.: +49 211 54095320 | Fax: +49 211 54095399