



04 | 2013

KMLZ VAT NEWSLETTER

VAT deduction and legitimate expectation – the ECJ continues its business-friendly jurisdiction

Tax courts currently have to decide on several cases in which the supplier committed tax fraud. Often, the fiscal authorities attempt to impose the VAT-related consequences on the customer by denying a VAT deduction. After all, the customers have chosen their own business partners and it could be said that they failed to exercise sufficient care in doing so. The jurisdiction is looking for an appropriate distribution of the risk between the customers and the fiscal authority. The European Court of Justice (ECJ) continues its most recent business-friendly jurisdiction regarding the legitimate expectation when deducting VAT with two judgments which it handed down on 31 January 2013 (C-642/11 – *Stroy trans EOOD* and C-643/11 – *LVK - 56 EOOD*).

1. Former judgments by the European Court of Justice

The ECJ passed several judgments regarding this matter in the last few months (ECJ, judgment of 21 June 2012 – C-80/11 and C-142/11 – *Mahagében Kft* and *Péter Dávid*;

VAT deduction when the fiscal authority doubts receipt of supply

On 31 January 2013 the European Court of Justice has passed two more judgments in cases regarding legitimate expectation when deducting VAT. Principally, the customer has the right to deduct VAT even if the tax authority assumes that the supplier has not carried out any supply. If the tax authority wants to deny the deduction of VAT, even in such cases it is for the tax authority to prove that the customer knew or should have known about a tax fraud related to the supply.

judgment of 06 September 2012 – C-324/11 – *Gábor Tóth*; judgment of 06 December 2012 – C-285/11 – *Bonik EOOD*). In the cases of *Mahagében Kft* and *Péter Dávid* (para. 49) the ECJ stated clearly and for the first time that the fiscal authority has the obligation to prove that the customer knew or should have known that the supplies received were related to a tax fraud.

2. Facts regarding *Story trans EOOD* and *LVK - 56 EOOD*

The recent decisions were based on the following facts: Both companies, the *Story trans EOOD* and *LVK - 56 EOOD*, had deducted VAT from invoices for the purchase of diesel fuel and other products. The Bulgarian tax administration requested the supplier and sub-supplier to submit documents which demonstrate the supply of goods. The suppliers were unable to completely comply with the request itself and were further unable to submit the documentation they did have within the specified time. *LVK - 56 EOOD* submitted incorrect delivery notes, weight certificates and bills of

Contact: Thomas Streit, LL.M. Eur.
Lawyer, Specialist lawyer for Tax Law
Tel.: 089 / 217 50 12 – 75
thomas.streit@kmlz.de



lading. From the Bulgarian tax administration's point of view, the customers failed to reasonably demonstrate the actual supply of goods and therefore denied VAT deduction. *Stroy trans EOOD* and *LVK - 56 EOOD* assured the tax authorities that a supply of goods had actually taken place. They referred to, *inter alia*, the fact that the tax administration imposed VAT on the supply of goods. For this reason, the supplies had to be considered as having been carried out.

3. Tax authority bears burden of proof

If the fiscal authority assumes, as a result of the documents produced, that supplies have not been carried out and, if the customer denies this assumption, the national court is required to carry out an examination in accordance with the particular country's rules of evidence. This entails a full assessment of all points of view as well as consideration of the actual circumstances. However, even in a case such as this, it would not be compatible with the basic principles of VAT legislation, to deny a VAT deduction to a taxable person who was unaware or incapable of becoming aware that the relevant supply constituted part of a tax fraud committed by the supplier or sub-supplier. The fiscal authority has to prove whether the customer knew or should have known about the tax fraud committed based on an objective viewpoint.

As in the cases of *Mahagében Kft* and *Péter Dávid* (para. 60, 61, 66), the ECJ points out that the fiscal authorities cannot generally require the customer to check whether the issuer of an invoice is a taxable person, has

had the relevant goods in his possession and has fulfilled his tax obligations.

Furthermore, the ECJ has clarified that, in cases in which there are irregularities (*i. e.* incomplete accounting) on the supplier or sub-supplier's part, the consideration of evidence shall not result in an indirect obligation being placed on the customer to check on the activities of the other party. The customer is principally not obliged to do so.

4. Conclusion

The ECJ continues its business-friendly jurisdiction with its latest two judgments. The ECJ's statements make it more difficult for the fiscal authority to deny VAT deduction to customers in cases in which the fiscal authority does not consider the transaction to actually have been carried out.

In the meantime, the first German tax courts have now picked up the ECJ's jurisdiction of the last few months in the course of interim legal protection. According to the ECJ's statements, the fiscal courts now demand the fiscal authorities to prove that the customer knew or should have known about the tax fraud before denying a VAT deduction.

There are still some legal questions that need to be clarified regarding VAT deduction and legitimate expectation. Further high court decisions will have to be made. However, in contentious cases, entrepreneurs should make use of the decisions in the cases of *Stroy trans EOOD* and *LVK - 56 EOOD*.