



ECJ: scope of necessary checks and attribution of knowledge of tax evasion in supply chains

1 Facts of the case

The activities of the plaintiff, *Aquila Part Prod Com*, included trading in the EU food industry, particularly in Hungary. The plaintiff concluded a contract in Hungary, for the performance of its business activities there, with *Corpinvest Srl*. *Corpinvest Srl*'s legal representative was Mr. KG. While represented by KG, the plaintiff purchased edible oil from *Rilax Kft.* for several months and resold it to *Strongfood sro*. The plaintiff claimed input VAT deduction with respect to these transactions.

After a five-year audit, the Hungarian tax authorities claimed back the plaintiff's input VAT deductions because the plaintiff had participated in a carousel fraud with the corresponding supplies. The tax authorities cited numerous irregularities which they had identified during their audit, and which they claimed evidenced the plaintiff's involvement in the tax evasion or, at the very least, the plaintiff's knowledge of it. The authorities also argued that the managing director of the company with which the plaintiff had concluded a contract of assignment, KG, should have realised, in the exercise of his due diligence, that he was participating in tax evasion regarding the supplies in question.

One of the things the referring court wanted to know was whether a taxable person could be obliged, in order to secure his input VAT refund claim, to examine such circumstances that even the tax administration could only ascertain by official means in the course of a five-year extensive examination. Furthermore, it wanted to know whether it is compatible with EU law that the knowledge of a natural person (in this case KG) who has a legal relationship with an independent legal person commissioned by the taxable person – without the natural person (in this case the limited partnership) having a legal



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relationship with the taxable person – is attributable to the taxable person, in the absence of any examination. In this context, the referring court wondered whether such an attribution should rather be examined based on the contract of assignment and the relevant foreign legal provisions.

2 Decisions of the ECJ

The ECJ first explicitly states – as it has done several times before – that a taxable person may be required to take increased due diligence measures in circumstances where there are indications of irregularities or tax evasion regarding his supplies and / or suppliers. The tax authorities must provide proof of this. According to the ECJ, presumptions are not sufficient to satisfy the evidential requirements. In particular, the mere finding that the supplies in question form part of carousel transactions is not sufficient to prove the taxable person's involvement in tax evasion or the knowledge / the need to know of the existence of tax evasion.

The ECJ now points out in this context that the taxable person cannot be required to carry out complex and comprehensive checks, such as those that can be carried out by the tax administration. The ECJ had not previously stated this so clearly. As expected, however, the ECJ did not render further guidance on what can and cannot be expected of the taxable person but instead referred to the national courts and the circumstances of the individual case.

The ECJ then quite succinctly answers the question of attributing knowledge of the existence of tax evasion in the case at hand. It stated that a taxable person cannot rely on the existence of a contract of assignment and the national provisions applicable to it and claim that he was unaware of the liability for fraud if knowledge of the liability for fraud concerning the supplies has been established, so to speak, "on his side" (by virtue of the knowledge of the person commissioned by him). According to the ECJ, such a possibility of exculpation would run counter to the objective of combating VAT evasion.

3 Consequences for the practice

In its letter of 15 June 2022, the German Federal Ministry of Finance states that a taxable person is to have the knowledge or the need to know of his employees attributed to him in analogous application of section 166 of the German Civil Code. Generally, however, an employer has significantly greater possibilities to select, influence and control his employees than a taxable person has regarding a commissioned third party.

The ECJ's statement on the attribution of the knowledge of a commissioned third party can result in a variety of liability options for taxable persons. Many taxable persons have commissioned third parties for various parts of their purchasing or sales process. If the knowledge of the third parties can be proven, taxable persons cannot blindly rely on them. Rather, they must give them precise instructions as to which verifications are to be carried out and documented, when additional verification measures are necessary (and which ones) and when, if applicable, supplies may not ultimately be carried out. Against this background, depending on the sector and the supplies, the taxable person may also be required to carry out his own verification of the supplies as regards fraud liability.

It is recommended that corresponding processes (if required within the framework of the Tax Compliance Management System) be established.