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Substantive and formal requirements in the VAT case law of the CJEU

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Table of contents

Summary.....	1
Preface.....	2
Abbreviation list.....	3
1. Introduction	4
1.1. Background.....	4
1.2. Aim.....	5
1.3. Method and material.....	5
1.4. Delimitation.....	5
1.5. Outline.....	6
2. The EU VAT system	6
2.1. General overview.....	6
2.2. Fundamental principles of EU VAT.....	7
2.2.1. VAT as a General Consumption Tax.....	7
2.2.2. Fiscal neutrality.....	7
2.3. Right to deduct.....	8
2.4. Right to exempt.....	9
2.5. Legal requirements.....	9
2.5.1. Substantive requirements.....	9
2.5.2. Formal requirements.....	10
3. European case law developments	11
3.1. Introduction.....	11
3.2. Invoicing.....	12
3.3. Reverse charge mechanism.....	15
3.4. VAT registration.....	17
3.5. Time limits.....	22
3.6. Fraudulent behaviour.....	23
3.7. Exempt intra-Community transactions.....	25
4. Amendments to be made in the VAT system	29
4.1. Introduction.....	29
4.2. Commission Proposal overview.....	30
4.3. VAT identification number amendments.....	30
5. Conclusions	31
Bibliography.....	33
Table of cases.....	34

Summary

The VAT system has been operating since 1967 across the European Union and is currently still in need to be adopted as definitive. Some issues should be confronted in 2018 before the implementation towards a fairer and simpler system. The proposal from the Commission set up in 2016 details the changes taken into account.

As a cornerstone of the mentioned VAT system, this thesis will analyse the view of the CJEU when it comes to exercising the right to deduct. More specifically, it will analyse the European jurisprudence when applying the various conditions, either the substantive and the formal requirements are laid down in the previous Sixth Directive or the VAT Directive currently in force.

The aforementioned is a practical approach which will allow for case by case review of all the details exposed by both the CJEU and national courts in multiple situations. The process will entail comprehensive reviews of simple wrongfully made invoices to taxpayers involved in fraud when exercising the right to deduct or occasionally, the right to exempt VAT.

Over the years, the CJEU has given more priority to the substantive requirements over the formal ones, establishing the principle of “substance over form” as an interpretative aid. However, such principle involves many exceptions that have been discussed in case law and will be clarified and classified in this paperwork.

Preface

The European and International Tax Law Master's Programme provided by Lund University is a complete programme that is expected to cover all areas related to tax law. This purpose is fulfilled mainly through a practical approach and thorough analysis of jurisprudence from the European Court of Justice. Since it happens to be such an exhaustive topic, there is no real time in one year to review each specific area comprehensively but is enough to obtain a significant overview of the main achievements and tax issues facing both national and international courts.

The VAT system is imperative around the European Union but has been notably incomplete in achieving its purpose. Since the establishment of the VAT system in 1967, its European Institutions have been working towards achieving a harmonised and fraud-proof system. As this is a vast and complex topic, the issue exposed in the present thesis focuses on just one of the many challenges that the European Union is facing.

I would like to express my gratitude to all the outstanding lecturers within the Department of Business Law at Lund University for being a comprehensive source of knowledge and for facilitating the successful fulfilment of this thesis. I would also like to thank the supervisor, Ben Terra, and examiner, Marta Papis-Almansa, for their usage guidelines. Finally, I would like to extend the thanks to my parents, Ramon and Carme, and to my partner, Daniel, for their constant support and encouragement not only over these last months throughout the entire programme.

Abbreviation list

B2B	Business-to-business
CTP	Certified Taxable Person
CJEU/Court	Court of Justice of the European Union
Commission	European Commission
Commission Proposal	Proposal for a Council Directive amending Directive 2006/112/EC as regards harmonising and simplifying certain rules in the value-added tax system and introducing the definitive system for the taxation of trade between the Member States. COM (2017) 569 final.
EU	European Union
Sixth Directive	Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment
Treaty of Rome	Treaty Establishing the European Economic Community (1957-93).
VAT	Value Added Tax
VAT Action Plan	Action Plan on VAT – Towards a single EU VAT area – Time to decide
VAT Directive	Council Directive 2006/112/EC on the common system of value added tax as amended by Directive 2008/8/EC
VIIES database	VAT Information Exchange System database

1. Introduction

1.1. Background

The harmonisation of the common VAT system established in EU in 1967 has played an essential role in the achievement of the European Common Market created by the Treaty of Rome in 1958.

On June 1985, the Commission presented the White Paper for the completion of the internal market by 1992. The paper laid down a series of measures in the field of the VAT. These included, among other things, the removal of economic barriers applied to intra-Community trade. Therefore, the current VAT rules for cross-border trade between businesses in EU Member States date back to 1993, right after the creation of the Single Market.

At the time, those rules were meant to be transitional but always with a view of adopting a definitive VAT system for the EU. Recently, the European Commission has resumed such long-standing commitment to become an EU single VAT area with the adoption of the *Action Plan on VAT – Towards a single EU VAT area – Time to decide*¹ (VAT Action Plan) on 7 April 2016.

Later on, in 2017 a legislative proposal was included in the Commission Work Programme² to attain such simpler and fraud-proof definitive VAT system for intra-Union trade. The proposal is to be elaborated further, and the main focus of this thesis will be to clarify if its adjustments will modify or affect the still controversial “substance over form” principle in EU VAT.

Therefore, the primary objective of the thesis in question will be the developments over the years of what is newly known as the “substance over form” principle in the VAT case law of the CJEU. The so-called “substance over form doctrine”³ maintains that the “substance,” rather than the form, of a transaction, is what governs the tax consequences of such transaction. In other words, it allows the tax authorities to ignore the legal form of an arrangement and to look to its actual substance to prevent artificial structures from being used for tax avoidance purposes.

Such a concept will be better illustrated along the thesis through the case law analysed. It is a concept rarely found in the EU legal acts as Treaties or Directives. There have been multiple and diverse interpretation issues when it comes to exercise the right to deduct, a principle that is a cornerstone of the EU VAT system and this is limited only in exceptional cases. Consequently, specific guidelines of the substance over form

¹ COM (2016) 148 final.

² Commission Work Programme 2017: Delivering a Europe that protects, empowers and defends, COM (2016) 710 final.

³David Klasing (2014) ‘What is the substance over form doctrine’, <<https://klasing-associates.com/question/substance-form-doctrine/>>

concept are found in the jurisprudence of the CJEU. Subsequently, it has been recently used as an interpretive principle by such a Court in its rulings.

1.2. Aim

Having analysed a wide range of CJEU jurisprudence, it has been seen that a lack of clarity on national legislation when dealing with the deduction and exemption of VAT, and further formalities on the invoicing procedure has to be accomplished. Even though it seems clear by the Court that substantive requirements prevail over formal conditions, it is not as easy to determine when the Member States have some discretionary powers on establishing its criteria. Therefore, the EU must attain a uniform approach. Thus, the purpose of this thesis is twofold: Firstly and the primary focus of the present thesis is to find out the treatment of substantive and formal requirements and its differences when dealing with the deduction of EU VAT; moreover, the substance over form will be analysed as well when applying the right to exempt VAT. The latter will be necessary in order to see later on whether the suggestions made by the Commission will have an impact on the VAT system in the area mentioned.

1.3. Method and material

The traditional dogmatic legal method will be used to achieve the purpose of this thesis. The research will be based mainly on the cases that the CJEU ruled on. These will follow a chronological order structure. Furthermore, they are divided into some sub-categories to place each of the cases in the group that best fits the central issue of the case.

Moreover, the binding provisions of the expired Sixth Directive and the VAT Directive currently in force will be continuously mentioned. National legislation might be taken into account in certain situations to illustrate the existence of divergences concerning European legislation. Besides, some non-binding documents such as the Commission proposal, recommendations and scholar opinions will be necessary for the determination of a topic like “substance over form” that is more present in soft law rather than in legal acts.

1.4. Delimitation

Assuming that the user reading this thesis has some background knowledge of the EU VAT system, basic definitions will be limited to focus on the primary goal of the thesis entirely. However, there will be a brief general overview of the EU VAT system to placing ourselves in the subject. Furthermore, regarding chapter 4, it is not within the scope of this thesis to provide a full explanation of all the amendments proposed by the Commission, but it will take into account only the ones related with formal or substantive conditions.

1.5.Outline

This thesis is divided into five different chapters. After the introduction, chapter two provides an initial overview of the EU VAT system from its origins and up to the current day, outlining the focus on the fundamental principles governing such a system. Moreover, it includes two brief sections regarding the right to deduct and the right to exempt VAT since such rights will constantly be commented on the thesis. Lastly, in this chapter theoretical explanation of both the formal and the substantive requirements will be presented based on the VAT Directive currently in force. Moving into chapter three, a thorough analysis of cases will be presented dealing with the material and formal requirements when applying rules to exercise the right to deduct VAT always preserving the mentioned principles. The primary focus of this last chapter is on the most recent developments including the recognition by the Court of the newly established principle of “substance over form”. However, a brief view of exemption cases will also be seen to be able to proceed to the next chapter. The fourth chapter will mention the latest arrangements made by the Commission about the substantive and formal requirements and that will also allow seeing if that is consistent with the case law examined. Finally, it will draw to an ultimate conclusion.

2. The EU VAT system

2.1.General overview

In 1967, the commitment was made to establish a definitive VAT system operating within the European Community in the same way as it would within a single country. The need to abolish the fiscal frontiers between the Member States by the end of 1992 made it necessary to reconsider the way in which goods were taxed during trading in the European Community⁴. The goal was to correctly reflect the idea of a genuine internal market by taxing goods in the country of origin so that the same conditions that apply to domestic trade would also apply to intra-Community trade.

However, more than 20 years later, the objective of taxation in the Member State of origin is still unachievable. Therefore, in 2016, the Commission, supported by the European Parliament and the Council, proposed to adopt a definitive VAT system⁵ based on the destination principle as a more realistic solution. If such definitive system is achieved, it will create a robust single European VAT area which will be able to support a more in-depth and fairer single market.

2.2.Fundamental principles of EU VAT

2.2.1. VAT as a General Consumption Tax

The First VAT Directive already enshrined the principle in its Article 2⁶. This provision states that *‘the principle of the common system of value added tax involves application*

⁴ COM (2017) 569 final, p. 2

⁵ COM (2017) 569 final

⁶ First Council Directive 67/227/EEC of 11 April 1967 on the harmonisation of legislation of Member States concerning turnover taxes.

to goods and services of a general tax on consumption'. Moreover, it has also been consistently reiterated by the Court in cases dating back to the early 1980s⁷. In the more recent *My Travel*, the Court stated⁸:

'It is to be remembered that the basic principle of VAT is that it is a consumption tax designed to be borne only by the final consumer.'

VAT is a general tax levied on all goods and services bought and sold for use or consumption within the EU. VAT is a multi-stage tax charged at each stage of the supply chain. The collection takes place through a system of partial payments. It allows taxable persons to deduct, from the VAT due, the amount of VAT that they have paid for business purchases in the preceding (production) stage. This system ensures that the tax is neutral, regardless of the number of transactions.

The principle of VAT as a general tax on consumption has two corollaries, namely the principle of strict interpretation, as developed by the Court when interpreting exemptions, and the destination principle, as set out in the current VAT Directive⁹.

2.2.2. Fiscal neutrality

The principle of VAT as a neutral tax was also enshrined in the First VAT Directive and was quickly developed by the CJEU as the principle of fiscal neutrality in its early case-law. In *Hong Kong*, one of the Court's earliest judgments on the VAT, it stated¹⁰:

'[The Preamble to the First Directive] refers to the need to achieve such harmonisation of legislation concerning turnover taxes as will eliminate factors which may distort conditions of competition, and therefore, to secure neutrality in competition, in the sense that within each country similar goods should bear the same tax burden, whatever the length of the production and distribution chain.'

Therefore, in the abovementioned judgment, it can be seen as a first factor related to the fiscal neutrality principle, which is that similar goods should bear the same tax burden.

More recently, in *EMS-Bulgaria Transport*¹¹ the Court observed that the conventional system of VAT seeks to ensure the complete neutrality of taxation of all economic activities, whatever their purpose or results, provided they be themselves subject to the VAT. Therefore, in this case, it is seen the second factor regarding the neutrality principle.

⁷ See, inter alia, CJEU Judgment of 26 March 1987, Case C-235/85, *Commission v Netherlands*

⁸ CJEU Judgment of 6 October 2005, Case C-291/03, *My Travel*

⁹ Rita de la Feria (2006). *EU VAT principles as interpretative aids to EU VAT rules: the inherent paradox*, p. 6.

¹⁰ CJEU Judgment of 1 April 1982, Case 89/81, *Hong-Kong*

¹¹ CJEU Judgment of 12 July 2012 in Case C-284/11 – *EMS-Bulgaria Transport*

In other words, neutrality means a right of deduction and is only applicable to taxed operations or if there are benefits from a suspension of tax for international operations. However, at the same time, neutrality is only a principle of interpretation to be applied concurrently with the principle of strict interpretation of the VAT exemptions¹².

Furthermore, the sub-principles of VAT uniformity, equality, and elimination of distortions in competition, have been developed as corollaries of the principle of fiscal neutrality¹³. On the one hand, their existence was already somewhat implicit in several early cases. The Court concluded that the principle of fiscal neutrality precluded Member States from treating lawful and unlawful transactions differently for VAT purposes. On the other hand, their existence was explicitly stated by the Court in *Commission v France*¹⁴.

2.3. Right to deduct

The Court has developed the right to deduct as both a corollary of the fiscal neutrality principle and of the principle of VAT as a general tax on consumption.

This right to deduct is laid down in Articles 167 and 168 of the VAT Directive¹⁵. According to settled case law, the right of taxable persons to deduct input VAT due or already paid on goods and services is a fundamental principle of the common system of EU VAT¹⁶. Consequently, a great deal of jurisprudence has been ruled over the years about its application.

As the Court has repeatedly held the right to deduct as provided for in Article 167 of the VAT Directive, it is an integral part of the VAT scheme and in principle may not be limited¹⁷. In particular, the right to deduct is exercisable immediately for all the taxes charged on transactions relating to inputs.

As regularly recalled by the CJEU, it is meant to relieve the operator entirely of the burden of the VAT paid or payable in the course of all his economic activities and by so doing it ensures the neutrality of taxation of all economic activities¹⁸.

2.4. Right to exempt

The right to exempt VAT from transactions is laid down in the VAT Directive in title IX of Directive 2006/12, which is entitled “Exemptions” and is composed of 10

¹² Christian Amand (2013) *VAT neutrality: a principle of EU law or a principle of the VAT system?*, World Journal of VAT/GST Law, 2:3, p. 170.

¹³ Rita de la Feria (2006). *EU VAT principles as interpretative aids to EU VAT rules: the inherent paradox*, p. 6.

¹⁴ CJEU judgment of 3 May 2001 in Case C-481/98 – *Commission v France*

¹⁵ Council Directive 2006/112 of 28 November 2006 on the common system of value added tax, O.J. L 347/1, 11 December 2006.

¹⁶ AG Léger Opinion in C-185/01 *Auto Lease*, para 8

¹⁷ Newsletter (2012) ‘*New ECJ court case after the case of Mahageben (C-324-11) Tóth case*’.

<https://accace.com/wpcontent/uploads/2012/09/2012_Hungary_New_ECJ_court_case_after_the_case_of_Mahageben.pdf>

¹⁸ See for example *EMS-Bulgaria Transport*, para. 43 and the case law cited; and *Mahagében and Dávid*, paras. 37 and 38 and the case law cited.

chapters. The first of these chapters sets out general provisions. Article 131 in Chapter 1 provides:

'The exemptions provided for in Chapters 2 to 9 shall apply without prejudice to other Community provisions and by conditions which the Member States shall lay down to ensure the correct and straightforward application of those exemptions and of preventing any possible evasion, avoidance or abuse.'

However, the case law analyzed in section 4.7 is referred to intra-Community transactions, resulting in being the exemptions that will be taken into account in the present section.

An intra-Community supply, which is the corollary of the intra-Community acquisition, is exempt from VAT if the conditions laid down in Article 138(1) of the VAT Directive are satisfied¹⁹. Under this provision, the Member States are to exempt supplies of goods dispatched or transported to a destination outside their respective territories but within the European Union. They do so by or on behalf of the vendor or the person acquiring the goods, for another taxable person, or for a non-taxable legal person acting as such in a Member State other than that in which dispatch or transport of the goods began.

2.5. Legal requirements based on the VAT Directive

2.5.1. Substantive requirements

In order to be able to exercise the right to deduct the VAT, the substantive requirements must be first met. The taxpayer must be a taxable person, and he has to use the purchased goods and services for taxable economic activities. So, the substantive requirements determine that there must be a connection between the purchasing of goods and/or services and the taxable economic activities of the taxpayer.

The substantive requirements for the right to deduct the VAT are those which govern the actual substance and scope of that right, such as those provided for in Chapter 1 of Title 10 of the VAT Directive 2006/112/EC, entitled 'Origin and scope of the right to deduct'. Under Article 167 the VAT arises at the time the deductible tax becomes chargeable. Moreover, Article 168 lists some circumstances when the taxable person is entitled to deduct the VAT paid. Besides, the next article describes other situations when the VAT is deductible depending on the purpose given to the good or service purchased. Finally, in this chapter, Articles 170 and 171 establish the requirements when a taxable person is entitled to obtain a refund of the VAT. Equally, the Sixth Directive already established the exact conditions under the same title in its article 17.

When it comes to exemptions of the VAT, the substantive requirements are laid down in Article 138 of the VAT Directive²⁰.

¹⁹See *Mecsek- Gabona* case, para. 29

²⁰ See section 2.4.

2.5.2. Formal requirements

The formal requirements must also be met to exercise the right to deduct. These conditions regulate the rules governing its exercise and monitoring thereof and the smooth functioning of the EU VAT system, such as the obligations relating to accounting, invoicing and tax declarations. The VAT Directive establishes these rules under the provisions 178 and 179 in Chapter 4 of Title X. Since holding a complete invoice is the only formal requirement in order to deduct VAT paid, also articles 220 and 226 entitled “issue of invoices” and “content of invoices” respectively, are constantly taken into account by the CJEU.

By virtue of Article 178(a) of Directive 2006/112, exercise of the right of deduction pursuant to Article 168(a) thereof is subject to the single formal requirement that, in respect of the supply of goods or services, the taxable person must hold an invoice drawn up in accordance with Articles 220 to 236 and Articles 238, 239 and 240 of the Directive²¹.

The VAT regulations list in detail the mandatory entries for a correct invoice.²² They concern, amongst others, the date of issue, serial number, name, address and VAT number of customer and supplier, the date of the taxable event, description of the goods and/or services delivered, unit price, taxable amount, rate and amount of VAT, any reason for exemption or application of special arrangements.

Regarding the right to exempt, the provisions related to invoicing mentioned for the right to deduct will also apply. In Chapter 3 of Title XI, Article 220(1) provides:

‘Every taxable person shall ensure that, in respect of the following, an invoice is issued, either by himself or by his customer or, in his name and on his behalf, by a third party:

(3) Supplies of goods carried out in accordance with the conditions specified in Article 138;

Article 226, also in Chapter 3 provides:

‘Without prejudice to the particular provisions laid down in this Directive, only the following details are required for VAT purposes on invoices issued pursuant to Articles 220 and 221:

(4) the customer’s VAT identification number, as referred to in Article 214, under which the customer received a supply of goods or services in respect of which he is liable for payment of VAT, or received a supply of goods as referred to in Article 138;

Therefore, compliance of formal requirements has brought a great deal of controversy in the jurisprudence of the CJEU regarding mainly invoicing issues, VAT registration and time periods that will be discussed in detail from now on.

²¹ CJEU judgment of 21 October 2010 in Case C-385/09 – *Nidera Handelscompagnie BV*, para. 47.

²² See article 226 of the VAT Directive.

3. European case law developments

3.1. Introduction

It is well-established by the Court that failure to comply with some of the formal requirements cannot be an obstacle to the exercise of the right to deduct if the substantive requirements have been satisfied. Otherwise, that would not be following the principle of fiscal neutrality inherent to the EU VAT system.

However, as this is not always the case or at least not a fixed rule, it would not make sense to establish formal requirements²³. The CJEU has been stating that formal requirements work merely as a control measure for the exercise of deduction and the proper functioning of the VAT system. Also, the Court leaves in the hands of the national body to decide whether there is a fraudulent invocation of the right to deduct for non-compliance with the formal requirements, a case where it is legitimate to deny the exercise thereof.

The upcoming pages will proceed to a thorough analysis of judgments of the CJEU where substantive and formal requirements were discussed and put into question in many different circumstances.

3.2. Invoicing

Starting off with one of the oldest cases in the field, in 1988 the CJEU ruled in *Léa Jorion*²⁴ a judgment against the Belgian State where it put into question invoicing legal requirements. The Sixth VAT Directive in force at that time provided in Article 18.1(a) that for a taxable person to exercise the right to deduct it must be followed Article 22.3 of such Directive. Under this provision, the invoice must state clearly the price exclusive of tax and the corresponding tax at each rate as well as any exemptions (subparagraph b) and the Member States are to determine the criteria for considering whether a document serves as an invoice (subparagraph c)²⁵. Moreover, paragraph 8 of the same provision, contain that Member States can impose other obligations for the correct collection of VAT as long as they are limited to what is necessary to ensure it²⁶.

Bearing the above in mind, the Sixth Directive does no more than require an invoice containing specific information but does not preclude the Member States to establish some additional criteria. Consequently, the Directive allows a Belgian taxpayer, in this case, to hold a document which contains not only the information typically included in an invoice as traditionally defined in commercial law but also other information established by Belgium.

²³Javier Galván (2016) *Exclusion of the right to deduct VAT for non-compliance with formal requirements and fraudulent activity: Judgment of the ECJ of 28 July 2016*. <<http://diligens.es/?p=1147&lang=en>>

²⁴ CJEU Judgment of 14 July 1988 in Joined Cases 123 and 330/87, *Léa Jorion and Société anonyme d'étude et de gestion immobilière 'EGI'*.

²⁵ CJEU Judgment of 14 July 1988 in Joined Cases 123 and 330/87 - *Léa Jorion*, para. 14.

²⁶ See also in this effect, para 25 of *Collée* case, C-146/05.

Several years later, the CJEU ruled a similar judgment on the *Bockemühl* case²⁷. The Court reiterated that under article 18(1)(a) of the Sixth VAT Directive, a taxable person could only invoke the deduction described in article 17(2)(a) of such Directive when he is in possession of a correctly issued invoice.

Later on, in 2010, there was a significant judgment²⁸ regarding the entry into force of the new VAT legislation in 2008 and content of invoices was put into question again but this time in relation with this transitional period.

A construction workers contract was concluded on June 2006. However, the work did not begin until the spring of 2007. The invoices relating to the work completed during this period were correctly issued. The new VAT law from February 2008 allowed its provisions to be applied retrospectively to invoices issued during the financial year 2007, so the contractors requested the new provisions to be applied to its VAT declaration for 2007. However, the tax authority stated that such invoices did not comply with the provisions of the new VAT law. Subsequently, they were asked to amend the invoices issued and the VAT declaration using a supplementary declaration. In other words, the national legislation made the deduction of VAT conditional upon the amendment of invoices and the submission of a supplementary tax declaration²⁹.

The tax authorities concluded, in that case, the denial of the right to deduct even though they knew that the applicant fulfilled the substantive conditions to benefit from such right. They did so because they had failed to amend the tax declaration for 2007.

Therefore, such reasoning is contrary to articles 167, 168 and 178 of the VAT Directive. These provisions do not allow imposing formal requirements as the amendment mentioned when they can render ineffective the right to deduct and the substantive conditions are proven to be met.

The CJEU came to the same conclusion in *Idexx Laboratories*³⁰, a case from 2015 where amendment of the invoices had to be made by the taxpayer. In such a case, an Italian company, Idexx Laboratories affected intra-Community acquisitions in Italy from a French and a Dutch company but failed to carry out the formalities required by Italian national law. It notably failed to record in the VAT register specific invoices drawn up by the French company. The invoices created by the Dutch company had not been recorded in Idexx's register of issued invoices but only in its register of purchases. Moreover, they were marked on it as VAT exempt. After a tax inspection, the tax authorities concluded that those transactions were subject to VAT. Thus, the tax authorities penalised Idexx for the failure to comply with their obligations.

²⁷ CJEU Judgment of 1 April 2004 in Case, C-90/02 – *Bockemühl*.

²⁸ CJEU Judgment of 30 September 2010, in Case C- 392/09 - *Uszodaépítő kft*

²⁹ *Ibid*, para. 33

³⁰ CJEU Judgment of 11 December 2014 in Case C-590/13 – *Idexx Laboratories Italia*

Nevertheless, the formal amendment requirement laid down by national law when it renders the right to deduct ineffectively will not be consistent with the VAT Directive, and therefore, Idexx will be able to recover its VAT after the correction of its invoices³¹.

Another reason that might have the effect of denying the right to deduct is the case where the taxable person does not provide the identification VAT number of the supplier in its invoices. That was the case of *Senatex*³², a wholesale textile business based in Germany. Senatex reclaimed VAT on commission statements from its sales representatives and invoices from a designer. In 2013 the German tax authority performed numerous spot checks of the accuracy of Senatex's tax returns. The authority discovered that these particular invoices were incomplete since they did not show the supplier's VAT number. Senatex corrected the documents, but the German tax authority took the view that the lack of the supplier's VAT number on the original documentation at the time that the claims were made meant that they were invalid. Therefore, the input tax claims could be reinstated only when corrected invoices were available. For that reason, Senatex obtained a deduction once the invoices were corrected, but the disallowance of the original claims resulted in the imposition of interest³³.

The CJEU held that the right to VAT deduction must be allowed when VAT is paid in the course of economic activities as long as the substantive requirements have been met. In this case, as the supplier's VAT number was only a formal requirement, the right to deduct arose at the moment when he met all substantive requirements. Senatex was therefore allowed to deduct VAT from the moment that the original invoice was received. The Court also decided that German legislation relying on disallowing EU law preclude the original input tax claim. Hence, the correction of the invoices had retrospective effect and validated the original claims³⁴.

A second CJEU decision reinforced the previous position. The Court issued it on the same day, and it was about the insufficient information on the invoices that issued a Portuguese company named Barlis³⁵. This company run hotels and restaurants in Lisbon and it received VAT invoices from its lawyer in which the services were described as "legal services". The Portuguese tax authority claimed that the description on the invoices was insufficient and disallowed the input VAT claimed by Barlis. Under the Portuguese legislation, "invoices must contain the common name of the goods or services supplied, together with a specification of the information necessary to determine the applicable tax rate".

The CJEU agreed that the description "legal services" was not detailed enough and might not be sufficient to identify the nature of the supply³⁶. However, although the

³¹ *Ibid*, para. 43 to 45

³² CJEU Judgment of 15 September 2016 in Case C-518/14 - *Senatex*

³³ Ruth Linehan (2017) *Latest EU Developments in Relation to VAT Recovery*.

³⁴ *Ibid*, para. 43

³⁵ CJEU Judgment of 15 September 2016 in Case C-516/14 – *Barlis 06*

³⁶ *Ibid*, para. 31- 33

judgment confirms that the invoices were deficient, the Court went on to say one more time that EU law does not allow the refusal of input tax where the tax authority has all the information needed to validate the claim, even when there are defects in the actual invoicing³⁷.

More recently, the matter seen above has been revised in the joined cases of *Geissel and Butin* regarding two German car dealers that were deprived of its right to deduct³⁸.

In the case of *Geissel*, the German tax authorities refused VAT recovery because EXTEL, the car provider, had no establishment at the address provided on the invoices.

On its part, *Butin*, who also traded in motor vehicles, relied on invoices issued by an internet dealer to recover its VAT. The tax authorities again refused VAT recovery as the supplier's address shown on the invoices was incorrect and that nothing at that address indicated the presence of an actual business. However, the CJEU found that, in light of advances in technology and changes in business practices, the existing national case-law which they relied on was outdated. Moreover, *Butin* verified the supplier's status as a business and the accuracy of the content of the invoices acting diligently on its part.

As stated before by the Court, it recalls in the present judgment that the requirement of holding an invoice which shows the full name and address of the supplier and the customer is a formal condition. Thus, the deduction of the VAT is to be allowed if the substantive conditions are satisfied.

The indication of the address of the issuer of the invoice, therefore, cannot be a decisive condition for purposes of the deduction of the VAT. Subsequently, it follows that the VAT Directive³⁹ precludes national legislation from requiring an invoice to show the address where the supplier carries out its economic activity.

The last case⁴⁰ judged on the field was a case concerning goods that were supplied to Volkswagen AG between 2004 and 2010 in Slovakia. At the time of the supplies, the suppliers issued invoices but did not include VAT on them. They considered the transactions not as supplies of goods but as 'financial compensations', which are exempt from the VAT. When the suppliers realised that they were wrong in the year 2010, they issued new invoices charging VAT. The suppliers also filed additional tax returns for all years from 2004 to 2010 and they paid the VAT due to the State Treasury. Volkswagen filed a claim to recover the input VAT on all revised invoices. However, the tax authorities from Slovakia denied part of the VAT recovery. They held that the entitlement to VAT recovery arose on the date of delivery of the goods.

³⁷ *Ibid*, para. 42- 44

³⁸ CJEU Judgment of 15 November 2017 in Joined cases C-374/16 and 375/16 – *Geissel and Butin*

³⁹ See Article 226(5) of the VAT Directive.

⁴⁰ CJEU Judgment of 21 March of 2018 in Case C-533/16.- *Volkswagen AG*

Consequently, the right to claim VAT for the period from 2004 to 2006 had expired under the national legislative limitation period of 5 years⁴¹.

The CJEU ruled that although under article 167 of the VAT Directive the right to deduct VAT arises at the same time as VAT becomes chargeable, within the meaning of article 178 of the VAT Directive it only can be exercised appropriately once the VAT taxable person holds an invoice which mentions that VAT⁴².

In this case, the suppliers did not make any adjustments for VAT purposes until 2010. Under these circumstances, it was not objectively possible for Volkswagen to exercise its right to a refund before this adjustment since it had neither been in possession of the invoices nor was it aware that the VAT was due. The CJEU also noted that the risk of tax evasion was non-existent in the case at hand as VAT had already been accounted for by the supplier in the framework of the regularisation.

Consequently⁴³, the CJEU ruled that if a taxable person can demonstrate that it was objectively impossible to exercise the right to recover VAT before the federal limitation period expired, the EU member state in question cannot deny recovering the VAT solely because that national limitation period had expired.

It can be concluded from the previous cases that the formal requirements for VAT deduction have been eased over the years and they continue to do so. Even though the documentation of deduction claims with invoices is the crucial element, when the taxpayer fails to provide complete invoices, the CJEU accept amendments or additional evidence to avoid arbitrary limitations by the Member States.

3.3. Invoicing and reverse charge mechanism

Invoicing issues have also been giving rise to cases where the reverse charge mechanisms apply which is in multiple kinds of transactions. These cases can be seen in transactions where the supplier is not established nor has a fixed establishment in the country of the customer. In such cases, the purchaser, instead of the seller, is who is liable to pay the VAT due directly to the tax authorities. Under these circumstances, the treatment given to the formal requirements is different since article 178(f) of the VAT Directive provides the option to apply such procedure. However, the substantive requirements will not be seen affected by the mentioned mechanism.

In a judgment from 2004, the court specified that to deduct VAT on purchases under the reverse charge mechanism the taxpayer must comply with the formalities imposed by each Member State. The only exception pointed out is when an additional condition makes the exercise of the right to deduct impossible. In this case, the CJEU ruled in *Bockemühl* case that the power to impose formalities must be exercised to ensure the

⁴¹ *Ibid*, para. 25 to 28

⁴² *Ibid*, para. 42

⁴³ *Ibid*, para. 49

collection of the VAT and its verification by the tax authority. However, due to the extent and technical nature of these formalities must not make the right to deduct practically impossible or excessively difficult to exercise it.⁴⁴

Furthermore, the CJEU also ruled in *Ecotrade*⁴⁵ that in the case of a reverse charge procedure, obligations arising from formalities laid down in national legislation as well as the obligations relating to accounts and tax returns cannot lead to the denial of the right to deduct. Such mechanism is just a pure formal obligation, and a misunderstanding could not deprive *Ecotrade* of its right to an input VAT deduction⁴⁶.

A more recent case is *Fatorie*⁴⁷, a company which concluded a contract with Megasal in January 2007 and it concluded the works in February 2008. Megasal, as the services provider, issued several invoices and *Fatorie* paid the VAT due to Megasal and applied for repayment of the VAT. There was an invoice from 3rd March 2008 on which the VAT should be recovered since the measures governing the reverse charge system were not applied anymore. However, Megasal was declared insolvent and did not pay the VAT on such invoice which had been paid to the tax authorities by *Fatorie*⁴⁸.

Nevertheless, the CJEU stated that the incorrect invoicing by the supplier, in drawing up the invoice of March 2008 cannot affect *Fatorie*'s deduction of the VAT to that invoice. Moreover, the Court recalled again that the principle of fiscal neutrality permits deduction to be allowed if the substantive requirements are met⁴⁹.

To sum up, in *Fatorie* Case⁵⁰, the CJEU stated that a taxable person could not deduct VAT paid when that tax was not due to the services or/and goods if an invoice was incorrectly drawn-up by the supplier. This denial was due to the VAT fiscal regime being applied inaccurately. The Court ruled that in a transaction subject to the reverse charge regime the VAT Directive and the principle of fiscal neutrality do not preclude the recipient of the services from being deprived of the right to deduct the abovementioned payment.

One more example is the *Farkas* case⁵¹, where the taxable person requested the reimbursement of VAT paid when it was not due.

At an electronic auction organised by the Hungarian tax authorities, Mr Tibor Farkas purchased a mobile hangar from an insolvent company. The seller issued an invoice with VAT and Farkas paid the invoice including the amount charged as the VAT. However, the Hungarian tax authorities refused to refund the amount to Farkas. They

⁴⁴ See *Bockemühl* case para. 50 to 53

⁴⁵ CJEU Judgement of 8 May 2008 in *Joines* cases C-95/07 and C-96/07 - *Ecotrade*.

⁴⁶ *Ibid*, para. 60 to 65

⁴⁷ CJEU Judgment of 6 February 2014 in Case C-424/12 - *Fatorie*

⁴⁸ *Ibid*, para. 11-16

⁴⁹ *Ibid*, para. 35

⁵⁰ *Fatorie* case, para. 44

⁵¹ CJEU Judgment of 26 April 2017 in Case C-564/15 - *Farkas*

stated that a reverse charge was applied, so that not the seller, but Farkas himself should have paid the VAT directly to the tax authorities. The national court found that this VAT was incorrectly charged. As a result, Farkas was not allowed to deduct this amount as input VAT.

The CJEU, however, considers that the tax authorities could be obliged to reimburse Farkas this amount under specific circumstances⁵². Firstly, it must be impossible or complicated to recover the VAT paid by the seller. The seller was insolvent, so he met this condition. Secondly, the treasury should not suffer a loss. He also fulfilled this requirement, as the seller remitted the VAT paid by Farkas to the tax authorities. Thirdly, the transaction should not involve any form of tax evasion. However, he did not comply with this last condition, as there was no evidence supporting any signs of tax evasion.

This judgment shows that recovering unduly paid VAT can be quite difficult. The purchaser is wholly dependent on whether the seller has paid the VAT to the tax authorities before being able to recover the VAT.

It has to be noted from this section that, given the case law⁵³, when the reverse charge mechanism applies, the formal conditions relating to invoicing for the right to deduct do not have to be satisfied. Instead, in the exercise of the option conferred by Article 178(f) of the VAT Directive is the condition laid down by each Member State that must be fulfilled when such procedure is applicable.

3.4. VAT registration

Identification as a taxable person under a VAT registration number is a condition laid down in Article 214 of the VAT Directive⁵⁴. This requirement is obliged for businesses that carry out supplies of goods or services taxed with VAT as well as companies that make intra-Community transactions. Invoices will mention such to identify the tax status of the customer, the place of taxation or merely the real existence of a legal entity.

When it comes to exercise the right to deduct significant controversy has been given such a VAT number over the years in the CJEU. Besides, similar discussions will be seen later on in section 4.7 when examining intra-Community case law.

The first example exposed is *Nidera Handelscompagnie* case⁵⁵, where a company was purchasing wheat in Lithuania and exporting it to non-Member States between February and May 2008. Since Nidera was not registered as a taxable person in Lithuania, it was not obliged under national law to be registered as a VAT payer. However, to exercise the right to deduct, a company in Lithuania must be registered for VAT purposes.

⁵² *Ibid*, para. 54- 56

⁵³ See *Bockemühl* case.

⁵⁴ See article 214 of VAT Directive for full details.

⁵⁵ CJEU Judgment of 21 October 2010, *Nidera Handelscompagnie BV* Case, C-385/09.

Hence, later in August, Nidera registered itself as a VAT payer since it wanted to deduct the input tax paid on its purchases made before its registration.

Therefore, the CJEU stated in *Nidera*⁵⁶, that the right to deduct of that company was denied because it was not registered at the time of the purchase was made. However, under the VAT Directive it is necessary to deduct VAT when carrying out a taxable activity and to provide the correct documents. Thus, the Court clarified that within the meaning of Articles 213 and 214 of the VAT Directive the identification of a company cannot be considered as a measure giving rise to the right of deduction but merely a formal requirement for purposes of verification⁵⁷.

It seems that Nidera meets the substantive conditions of the right of deduction. Thus, the fact that it was registered for VAT purposes later in the time it is just a formality that cannot have the effect of limiting such right and rendering it ineffective because this goes away from the purpose of the VAT system⁵⁸.

Even though it is not considered a vital condition for deduction of the VAT, the exercise of the right to deduct should be limited in time. Therefore, the identification for VAT purposes has to be done within a reasonable period to ensure legal certainty of the VAT system. Otherwise, such measure would be meaningless for taxpayers.

Another case judged in the same year was *Polski Trawertyn*⁵⁹. Polski was founded on 26 April 2007. Before the date, an invoice was issued to its partners. Also, a second invoice was issued on the foundation day. Because of national legislation, the company does not have the right to deduct the VAT on the first invoice. Conversely, within the meaning of the Sixth Directive, partners of a partnership carrying out investment transactions for a future economic activity must be regarded as taxable persons and thus, entitled to exercise the right to deduct its input VAT⁶⁰. With regards to the second invoice, even though it was issued on the day of the foundation of Polski, the company was not registered in the companies register until later in June 2007. Consequently, that invoice was apparently issued to a non-existent entity.

Similarly than in *Nidera* case, in *Polski*⁶¹, the taxable person again was being denied the right to deduct input VAT because the invoices had been drawn up in the name of the founding partners at a time when the company was not yet registered.

However, Article 226 of the VAT Directive states that only the conditions set up in that provision are required for VAT purposes. Thus, Member States are not allowed to exercise the right to deduct VAT dependent on compliance with conditions relating to

⁵⁶ *Ibid*, para. 42; see also *Ecotrade* case para 64 and *Uszodaepito* case para. 40

⁵⁷ *Ibid*, para. 50

⁵⁸ *Ibid*, para. 54

⁵⁹ CJEU Judgment of 1 March 2012 in Case C- 280/10 - *Polski* case

⁶⁰ *Ibid*, para. 30 to 32

⁶¹ *Ibid*, para. 43

the content of invoices which are not explicitly laid down in the provision mentioned since that would be considered to be a formal obligation.

Moreover, it follows from the judgment that under Article 226(1) and (5) of the VAT Directive, the date of issue of the invoice and the full name of the taxable person must appear on the invoice. However, the CJEU declared that since the invoice is just a formal requirement, if the missing data is legitimately acquired by other means, it must be accepted in order always to ensure the least limitation of the right to deduct input VAT.

Notwithstanding the previous cases, sometimes what is denied is not the right to deduct but the VAT registration number on itself. That was the case of a Latvian company named *Ablessio*⁶² that applied to the Latvian tax authority to be entered on the register of taxable persons subject to VAT. However, its registration was refused because *Ablessio* did not have the material, technical and financial capacity to carry out its economic activity. Moreover, another reason for the denial was that the owner of the shares had historically obtained an identification number for companies which never carried out any real economic activity. Due to this second reason, the CJEU pointed out⁶³ that in the VAT Directive there is no limitation on the number of applications made by the same person acting on behalf of different legal entities for individual VAT identification.

As *Ablessio* is a taxable person, there is established case law stating the abovementioned concept as broadly as possible. Hence, taxable persons are not only persons who already carry out an economic activity but also persons who plan to start such an activity. Regarding that definition, it is evident that someone in the position of *Ablessio*, starting off a business is unable to prove that they already have all the resources to carry out such an activity⁶⁴. Following that consideration from the CJEU, it concluded that the refusal made by the national authorities is not compatible with articles 213 and 214 of the VAT Directive.

Since *Ablessio* met the material conditions, and the registration is just a formal requirement, the company cannot be prevented from exercising its right to deduct on the ground that he had not been identified as a taxable person for VAT purposes before using the goods purchased in the context of its taxed activity. The CJEU stated that a refusal to identify a taxable person only would be considered proportionate when under objective evidence it is probable that the taxable person uses its VAT identification number fraudulently⁶⁵. However, the lack of resources when *Ablessio* was at the very beginning of its business is not sufficient to demonstrate that it pretends to commit tax evasion.

⁶² CJEU Judgment of 14 March 2013 in Case C-527/11 – *Ablessio*

⁶³ *Ibid*, para. 37

⁶⁴ *Ibid*, para. 26

⁶⁵ *Ibid*, para. 34

A recent case from 2015 deals again with the lack of the VAT number on the invoices issued by the taxable person⁶⁶. In this judgment, the tax authorities denied the right to deduct VAT to the partnership *Salomie and Oltean* because it was not identified for VAT purposes at the moment when it carried out the transactions (because the partners wrongfully thought they did not have to register). Following the line of previous judgments as *Nidera*, the Court decided that if the tax authority has the information necessary to confirm that the substantive requirements concerning the right to deduct have been satisfied, it cannot impose additional conditions that may have the effect of rendering the exercise of that right ineffective.

Moving on into such a recent decision of the Court⁶⁷, it was clarified the VAT deduction right in connection to acquisitions of goods and services from suppliers whose VAT number is inactive.

By a contract for supplies of services concluded on 3 January 2011, a company named *Rom Packaging* established in Bucharest had supplied services to *Paper Consult*, also established in Romania, excluding VAT. However, *Rom Packaging* had been declared inactive since October 2010 as well as removed from the register of persons subject to VAT from November 2010 for failure to submit the tax declarations required by law. Therefore, the tax authorities refused to *Paper Consult* the right to deduct off the amount of VAT paid for the supplies of services provided by *Rom Packaging*.

From 1 January 2017, the VAT legislation allows taxable persons to exercise the right to deduct in connection to acquisitions performed from suppliers during the period when their VAT number was inactive based on the corrected invoices issued by the supplier after re-registration. The measure does not apply retrospectively and only applies to suppliers which re-register for VAT purposes as of 1 January 2017.

Thus, in the opinion of the Court, as long as no fiscal fraud has been proven in a transaction, a taxable person should not be denied the VAT deduction right in connection to an invoice issued by a supplier declared inactive. An essential argument of the Court in this respect is that the supplier, even if inactive from a VAT perspective, paid to the state budget the VAT amounts related to the contract concluded with the client. Therefore, refusal of the beneficiary's right to deduct in connection to the contract would represent an infringement of the VAT neutrality principle⁶⁸.

Since this decision is meant to clarify what concerns the VAT legislation in force, the CJEU also mentions that such interpretation must apply retroactively.

⁶⁶ CJEU Judgment of 9 July 2015 in Case C-183/14 – *Salomie and Oltean*

⁶⁷ CJEU Judgment of 19 October 2017 in Case C-101/16 – *SC Paper Consult*

⁶⁸ *Ibid*, para. 47-50

Finally, the most recent case, the *Dobre* case from 7 March 2018, it deals with possible tax fraud in relation to the omission of the VAT registration number⁶⁹.

This Romanian company named Dobre had failed to submit VAT returns relating to the fourth quarter of 2011 and the first quarter of 2012. Consequently, its VAT identification number was revoked from 1 August 2012 but Dobre continued issuing invoices without submitting the relevant VAT returns. However, later in 2014 Dobre finally submitted its pending tax returns and claimed for a deduction to the tax authorities but they rejected such claim. Besides, they made Dobre pay for the corresponding VAT it had collected during the period in which it was not identified for VAT purposes⁷⁰.

As it has been seen in the previous judgment of *Ablessio*, the condition laid down under article 214 of the VAT Directive to be identified for VAT purposes it is considered a purely formal requirement just for the purpose of control. Therefore, under EU law view, the national authorities cannot prevent Dobre from exercising its right to deduct on the ground that it had not been recognised as a taxable person.

The VAT Directive does not prevent national law to impose such refusal of deduction if failure to satisfy formal requirements prevents national court to have the necessary information to know that Dobre had met the substantive conditions. This situation might be a case of tax evasion, and it is for the EU VAT system to avoid it⁷¹. Hence, under possible fraudulently circumstances, denial of the right to deduct is not considered a penalty that goes further than is necessary. However, such conclusion does not seem following the outcome established in a case like *SC Paper Consult*. In this last judgment mentioned, the CJEU stated that since no fiscal fraud had been proven, national courts cannot deny the right to deduct. Nevertheless, in *Dobre*, the Court established that the denial of the right to deduct was proportionate since there was some suspicion of fraudulent behaviour.

To summarise, it must be pointed out in this section that registration for VAT purposes provided for in Article 214 of the VAT Directive is typically a formal requirement for control. Hence, failure to comply with it at the time of the supply cannot be an obstacle to the exercise of the right to deduct when the substantive conditions which give rise to that right are satisfied⁷².

Therefore, it should be also concluded that the EU VAT system is getting harder when it comes to avoiding tax fraud. There is no need of a complete proof that fraudulent behaviour is taking place; only suspicions may lead to the refusal of the right to deduct, and that, without being contrary to EU law.

⁶⁹ CJEU Judgment of 7 March 2018 in Case C-159/17 - Dobre

⁷⁰ *Ibid*, para. 17- 21

⁷¹ *Ibid*, para. 41

⁷² *Ibid*, para. 60

3.5. Time limits

A well-known judgment from 2004 establishes the case of this Italian company named Ecotrade, specialised in synthetic gypsum and ashes used for the manufacture of cement. Ecotrade carried out an incorrect invoicing of some transactions made between the other Member States over the tax periods of 2000 and 2001. The company had recorded the invoices only in the register of purchases and not in the register of invoices issued⁷³. Due to such mistake, Ecotrade lost the right to deduct VAT on account of the time-bar. By the time the authorities made this decision (within 4 years under national legislation) it had already prescribed the time limit (2 years for the taxable person under national law) to exercise its right to deduct.

The main issue, in this case, was whether the exercise of such right could be conditional upon compliance with a time-limit stated under national law. When it comes to the Sixth Directive, it does not impose any time limit on the right to deduct since the guarantee of that right is the cornerstone of the VAT system. However, it is a formality that may be laid down by the Member States and, if they impose such time limitation, they can never go further as to render ineffective the right to deduct.

Therefore, the wrongfully made invoicing by Ecotrade, as purely a formal condition, would not have been an issue if the company had corrected it within the period established by Italian legislation. However, it did not accomplish with the national conditions. Even though it is not a formality laid down in the Sixth Directive, it is compatible with it as well as it is allowed by national legislation to impose such timing conditions as long as they do not render impossible the right to deduct⁷⁴.

Several years later a similar case was judged dealing again with time limitations when exercising the right to deduct input VAT⁷⁵.

In such a case an intra-Community transaction gave rise when a Spanish company sold second-hand lorries and traction vehicles to EMS, established in Bulgaria. Nevertheless, the latter was not registered for VAT purposes until 12 January 2009, and the mentioned transaction took place on 14 November 2008. However, the settlement by EMS was not affected until June 2009. Therefore, taking into account such delay, EMS was required by the tax authorities to pay a sum by way of default interest. Moreover, they refused its right to deduct the VAT for the same reason⁷⁶.

As stated previously in *Nidera*⁷⁷, the registration of the company is just a purely formal condition. Therefore, regarding the late registration of the company, considered as such,

⁷³ See *Ecotrade* case, para. 20

⁷⁴ *Ibid.*, para. 72

⁷⁵ CJEU Judgment of 12 July 2012 in Case C-284/11 – *EMS-Bulgaria Transport*

⁷⁶ *Ibid.*, para. 30-31

⁷⁷ See *Nidera Case*, para. 50 to 54

the tax authorities may not require to fulfil it when they have the information necessary to establish that the substantive requirements are met⁷⁸.

It can be summarised that penalising a taxable person who has failed to claim the deduction of input VAT within a proportionate limitation period, cannot be seen as incompatible with the VAT Directive since this practice does not preclude the exercise of the right to deduct. However, such penalty must not go further than is necessary. Furthermore, as regards a penalty consisting of an absolute refusal of the right to deduct would be a disproportionate measure where no fraudulent behaviour is ascertained, and in this case, a breach would be seen in the principle of fiscal neutrality.

3.6. Fraudulent behaviour

Based on case law⁷⁹, where the taxable person intentionally participates in tax evasion the exercise of his right to deduct will probably be limited since this situation might have the effect of jeopardising the operation of the common system of the VAT.

To start with, for instance, there is the case of Mr R⁸⁰, a national from Portugal who was the manager of a German company engaged in the luxury car trade. Its buyers were mostly car dealers established in Portugal. From 2002 he was issuing false invoices in the name of fictitious purchasers who appeared as recipients of the cars sold. In other words, Mr R was concealing the real identity of the purchasers to enable the Portuguese distributors to evade the payment of VAT. This practice allowed him from benefiting from a more advantageous price of the vehicles.

EU law always tries to limit as little as possible the right to deduct VAT or to be exempted, as a principle for the correct collection of the tax. However, in such a case where the taxable person has manipulated invoices that shows his real transactions, the Member State of departure of the intra-Community supply is allowed, under Article 28c(A) of the Sixth Directive, to refuse to grant the exemption in order to prevent tax evasion and for the proper functioning of the common system of VAT⁸¹.

Similarly, some years later it was judged the *Astone* case⁸², where in the course of a tax inspection it was detected that *Astone* had not submitted the relevant VAT returns corresponding to several periods. Moreover, he did not have the corresponding VAT ledgers of invoices issued. Thus the Tax Authorities did settle the corresponding VAT debt.

The CJEU mentions that articles 180 and 182 of the VAT Directive allow the exercise to the VAT deduction by the taxable person in subsequent financial years although it

⁷⁸ See, inter alia, CJEU Case C-284/11 – *EMS -Bulgaria Transport* paragraph 62; *Ecotrade*, para. 63 and 64; *Nidera Handelscompagnie*, para. 42

⁷⁹ See, inter alia, *Plockl Case*, para. 44

⁸⁰ CJEU Judgment of 7 December 2010 in Case C-285/09 - *R*

⁸¹ *Ibid*, para. 48-49

⁸² CJEU Judgment of 28 July 2016 in Case C-332/15 - *Astone*

has not been exercised in the period in which it was born. Nevertheless, this deadline cannot be without time limitation. Therefore, the existence of an expiration term for the deduction is not incompatible with the VAT Directive⁸³.

On the other hand, it is true that the criterion of the CJEU is aimed at not limiting this right by the mere failure to comply with the formal requirements. It must be noted, that such a massive failure (absence of declaration, invoices register and accounting) can result in fraudulent activity by the taxable person. However, such a situation must be judged by the national court who can rightfully deny the exercise of the right to deduct when it is fraudulently invoked⁸⁴.

Nevertheless, not always tax evasion is committed intentionally and that was the case for *Mahagében* in 2012⁸⁵. A contract concluded on 1 June 2007 between Mahagében and RK for the supply of unprocessed acacia logs. Both companies declared all the invoices in its tax return also paying the VAT due in the case of RK and exercising the right to deduct by Mahagében.

However, after an inspection by the tax authorities concluded that the number of acacia logs purchased during the contract (1 June to 31 December 2007) was insufficient to fulfil the orders invoiced to Mahagében. Moreover, a tax debt was imposed on the part of Mahagében as well as a fine and late payment surcharge on the ground that such company had no right to deduct RK's potentially unauthenticated invoices.

Furthermore, RK was unable to provide evidence by other means to prove the transactions carried out; Mahagében, for its part and in the view of the tax authorities, had not acted with due diligence since it did not check whether RK was an existing taxable person and whether it was in possession of the goods due to be purchased. For these reasons, its right to deduct was refused⁸⁶.

Therefore, in such a case the material and formal conditions required by the VAT Directive are met. However, the national legislation requires additional documents over and above the invoices to prove that the purchases took place and RK did not supply this proof⁸⁷.

Given these circumstances, national authorities refused the right to deduct to Mahagében because they may have been aware of taking part in a transaction connected with fraudulent evasion of the VAT, so as a participant of fraud, the tax authorities penalised the company refusing its right to deduct.

To conclude this section it has to be stressed that intentionally evasion of tax may result in the loss of the right to exempt VAT and that would never be incompatible with the

⁸³ *Ibid*, para. 32-39

⁸⁴ *Ibid*, para. 56

⁸⁵ CJEU Judgment of 21 June 2012 in Joined cases C-80/11 and C-142/11 – *Mahagében and Dávid*

⁸⁶ *Ibid*, para. 17-18

⁸⁷ *Ibid*, para. 51

VAT Directive. However, such decision would preclude the rules governing the right to deduct under the European legislation when the taxable person is unaware of its improper actions. Moreover, it also precludes a national practice that refuses the right to deduct from a taxable person that did not act diligent enough.

3.7.Exempt intra-Community transactions

According to settled case-law of the CJEU, the substantive conditions for VAT exemption of an intra-Community supply are met when the right to dispose of goods as an owner has been transferred to the buyer. For its part, the seller determines that the goods have been dispatched or transported to another member state and that as a result of shipping or transport the goods physically left the territory of the member state of supply.

Therefore, it will be seen in the following cases the treatment given by the CJEU to the formal conditions on intra-Community transactions when the substantive requirements are met.

To begin with, *Collée*⁸⁸, a taxable person potentially exempt from VAT who carried out an intra-Community supply of goods in the Spring of 1994. One of the interveners in the transaction wrongly reclaimed the input tax invoiced on its tax return. The tax authorities thus refused such deduction, and then the dealer proceeds to correct its VAT return for 1994. Again, the right of exemption was refused to Collée on the grounds that the prescribed records had not been updated regularly and immediately after the relevant transaction had been completed, which was a national condition settled down from case-law.

The CJEU stated that such national practice is not compatible with the Sixth VAT Directive since they are refusing to allow an intra-Community supply to be exempt from the VAT solely on the ground that the accounting evidence of the supply in question was belatedly produced⁸⁹. In other words, such foundation is making the right of exemption subject to compliance with formal obligations and without taking into account substantive requirements fulfilled in the present case⁹⁰.

Moreover⁹¹, the concealment by the dealer that an intra-Community supply had occurred should be taken into account. In this case, the exemption may be conditional upon the good faith of that person. However, this is up to the national courts to determine whether the delay in the production of the accounting evidence could lead to a loss in tax revenues or jeopardise the levying of the VAT. In such case of loss, Member States can impose penalties to the taxable person, and the Sixth VAT Directive does not prevent them from doing so.

⁸⁸ CJEU judgment of 27 September 2007 in Case C-146/05 – *Collée*

⁸⁹ *Ibid*, para. 29

⁹⁰ *Ibid*, para. 30 to 31

⁹¹ *Ibid*, para. 34 to 36

Some years later, in 2012, a similar judgment was released. In the case of *Mecsek-Gabona* (MG)⁹², in August 2009 a company had sold 1000 tonnes of rapeseed to an Italian company that was registered for VAT purposes. The seed was collected from MG's Hungarian premises. Subsequently, the buyer sent MG some consignment notes, which proved that the seed had been transported to a destination outside Hungary.

MG issued two invoices to the buyer concerning the transaction. On the assumption that the sales had been made "intra-Community" and were therefore exempt from the VAT, MG did not include any VAT in its invoices to the buyer. Subsequently, the company paid no VAT to the Hungarian tax authorities.

The Italian tax authority discovered that the Italian company could not be found and had never paid any VAT in Italy. It therefore decided, in January 2010, to remove the Italian company's VAT identification number from the register with effect from 17 April 2009. The Hungarian tax authority then decided that the rapeseed sold by MG could not be regarded as a VAT-exempt intra-Community sale and ordered MG to pay VAT in relation to the two sales.

The CJEU found that MG showed to the necessary standard that he had acted in bad faith, and had known that a fraud was in operation. Hence, under these circumstances, the authorities would be at liberty to refuse the right to VAT-exemption⁹³.

It is up to the Hungarian courts to apply the CJEU's judgment to the facts of this case. However, it is clear that, where a buyer is responsible for transporting goods to another Member State and has failed to do so, the seller will not be held liable for VAT.

The same year the Court carried out another judgment⁹⁴ regarding intra-Community transactions where the CJEU reasserts the view of the two previous judgments exposed. The situation is as follows:

In 1998 a branch of VSTR established in Germany sold two machines to Atlantic, an American company. The latter had a subsidiary in Portugal but was not registered in any Member State for VAT purposes. Moreover, Atlantic had sold those two machines on to a finish company and gave to VSTR the VAT identification number of such company. Subsequently, VSTR issued an invoice to Atlantic without VAT for the supply. However, that exemption was not possible since VSTR did not provide the VAT identification number of Atlantic.

A similar situation has been seen in *Collée* and in *Mecsek-Gabona* where the CJEU recalled that although a VAT identification number provides proof of the tax status of the taxable persons, it only constitutes a formal requirement which cannot undermine

⁹² CJEU Judgment of 6 September 2012 in Case C-273/11 – *Mecsek-Gabona*

⁹³ *Ibid*, para. 54 and 55

⁹⁴ CJEU Judgment of 27 September 2012 in Case C-587/10 – *VSTR*

the right of exemption from VAT where the substantive conditions for an intra-Community supply are satisfied. Hence, a national measure refusing such right is not realistically proportionate that the supplier did not provide the VAT identification number if he was acting in good faith and can demonstrate by other means that the person acquiring the goods is a taxable person acting as such⁹⁵.

It seems that the same criteria have been followed over the years, since in 2016 a similar state of affairs took place and the outcome of the CJEU was the same that, among other cases, in *VSTR*.

In *Mr Plöckl* case⁹⁶, a sole trader acquired a vehicle which he assigned to his undertaking. On October 2006, he dispatched the vehicle to a dealer established in Spain intending to sell it in Spain. He only declared a transaction for 2007. Upon a VAT audit, the VAT authorities found that the exemption for intra-Community supply was not applicable to the transfer made in, as Mr Plöckl could not provide a Spanish VAT number.

Based on earlier jurisprudence⁹⁷, the Court found that the exemption for intra-Community supply may not be denied because only formal requirements were not met. Moreover, the Court kept stating that such a national measure goes further than is necessary.

In the dispute in this proceeding, it was clear that the authorities had the information to find that the conditions for the transfer were met. Therefore the fact that Mr Plöckl failed to provide a VAT identification number could not form the reason to refuse to grant the exemption.

A different case⁹⁸ was judged in 2014, where the main issue was that the taxable person's VAT number was removed from the register.

This case concerns *Traum*, a taxpayer who made intra-Community supplies of goods from Bulgaria to a Greek company in 2009, being a period when the Greek customer was deregistered from Greek VAT. The Bulgarian tax authorities refused the VAT exemption on the intra-Community supplies, contending that there was no evidence of the transport of the goods from Bulgaria and no written confirmation of receipt of the goods by the purchaser, nor any documentation stating the exact address where the goods were received. The Court held that it is contrary to the principle of proportionality for the supplier to be held liable for VAT solely because the purchaser's VAT number had been removed from the register with retroactive effect⁹⁹.

⁹⁵ *Ibid*, para. 51-52

⁹⁶ CJEU Judgment of 20 October 2016 in Case C-24/15 - *Plöckl*

⁹⁷ See, *inter alia*, *Collée* Case.

⁹⁸ CJEU Judgment of 9 October 2014 in Case C-492/13 - *Traum*

⁹⁹ *Ibid*, para. 36

Following the line of the conclusions of the previous judgments, the Court stated that the exemption would not apply only in the case that Traum knew or should have known that his customer was involved in fraud and had not taken every reasonable step to prevent that fraud from having been committed¹⁰⁰.

Moving now to the most recent cases from 2017, two remarkable judgments are to be highlighted to see that the CJEU is still following the “substance over form” principle.

*Euro Tyre BV*¹⁰¹ was a Dutch company whose right to exempt VAT was refused by the tax authority on some sales transactions to a Spanish company. They based such decision on the grounds that at the time of the transactions, the contractor, the Spanish company, was neither registered for intra-Community transactions in Spain nor entered in the VIES database.

According to the Court¹⁰², the substantive conditions of the existence of intra-Community supply do not include the obligation for the buyer to have a VAT number as well as the obligation to register the purchaser for intra-Community transactions. These are only formal requirements that cannot undermine the right of the seller to VAT exemption if the material conditions concerning intra-Community supply have been met¹⁰³.

The last judgment subject to analysis is *Santogal M-Comércio e Reparação de Automóveis*¹⁰⁴. Such a case demonstrates an important procedural aspect that applies on intra-Community supplies: where the tax authority has already examined the affected transaction and the existing documentation and did not object, it may not retroactively deny tax exemption due to the principle of legal certainty¹⁰⁵.

Santogal is a motor vehicle dealership in Portugal that sold a new vehicle to an Angolan national allegedly residing in Spain. Santogal claimed a VAT exemption on the sale under Article 138(2) of the VAT Directive, which requires an exemption at origin on supplies of new means of transport between the Member States. The Portuguese tax administration later concluded that¹⁰⁶: (a) the purchaser in fact resided in Portugal rather than Spain; (b) the purchaser had never carried out any economic activity in Spain, and (c) there was no evidence that any VAT was later paid in Spain on the vehicle.

In the Court’s opinion, it is irrelevant, that the recipient is not a resident of the country of destination. Further, it is, according to the CJEU, also irrelevant, that the recipient

¹⁰⁰ *Ibid*, para. 40-42

¹⁰¹ CJEU Judgment of 9 February 2017 in Case C-21/16 – *Euro Tyre BV*

¹⁰² See, to that effect, *Mecsek- Gabona* Case

¹⁰³ *Ibid*, para. 29

¹⁰⁴ CJEU Judgment of 18 January 2016 in Case C-26/16 - *Santogal*

¹⁰⁵ *Ibid*, para. 75

¹⁰⁶ *Ibid*, para. 19

had only temporarily registered the vehicle in the Member State of destination¹⁰⁷. Again, mere registration is not a requirement for a VAT exemption.

Therefore¹⁰⁸, in a win for the vendor, the CJEU held that the exemption under Article 138(2) cannot be disallowed merely based on lack of proof that the purchaser is established in the Member State of acquisition, or on a mere suspicion that a vendor has colluded with a purchaser to commit VAT fraud.

Apparently, from the preceding, the exemption of an intra-Community supply of a new means of transport is not subject to the condition that the purchaser resides in the Member State of destination.

To conclude, this section notes that the CJEU has followed the same criteria than for the right to deduct. Substantive requirements generally prevail over formal conditions, such as the VAT registration number, a formality that has been discussed by the Commission for its high importance in the aim of preventing tax evasion.

4. Amendments to be made in the VAT system

4.1. Introduction

Having seen the case law mentioned above relating to intra-Community transactions, it is clear that national authorities seem to treat the identification of the taxpayers as taxable persons stricter than the CJEU. Conversely, the position of the latter over the condition in question is rather consistent with the case law.

The mere registration as a taxable person is considered as a formal requirement which means that even if a company does not provide its VAT registration number on the invoices or if such number has been refused, they can exercise the right of exemption if the substantive conditions are met. Therefore, this consideration makes the identification slightly meaningless since it will never lead to a refusal of the right of exemption. Consequently, in the Commission proposal from 2017 amendments regarding the VAT registration number have been proposed to be made during 2018 to maintain the neutrality of the VAT System and to prevent fraud cases.

4.2. Commission Proposal overview

As part of the VAT action plan launched on 7 April 2016, the EU Commission announced a legislative proposal for the definitive VAT system for Cross-Border EU Trade. Such proposal was published on 4 October 2017 and introduces the cornerstones of the definitive VAT system for Cross-Border B2B EU trade. The actual proposal from 2018 provides detailed technical provisions in this respect.

¹⁰⁷ KMLZ VAT Newsletter (2017) *ECJ: tax authorities bound to examination decisions*. <https://www.kmlz.de/sites/default/files/VAT%20Newsletter%2018_2017.pdf>

¹⁰⁸ *Ibid.*, para. 70-77

The current VAT system is characterised by splitting in two each EU B2B cross-border supply of goods. On the one hand, into an exempt intra-Community supply in the Member State of departure; on the other hand, into a taxable intra-Community acquisition in the Member State of the arrival of the goods. However, the proposal foresees in the introduction of one taxable supply in the Member State of the destination of the goods, the so-called intra-Union supply. As a first step of the Definitive VAT system, the proposal introduces the concept of a Certified Taxable Person or CTP.

In order to meet the request of the Council as stated in the Council conclusions of November 2016¹⁰⁹, the proposal also foresees further amendments of the VAT Directive in respect of the VAT identification number, chain transactions and call off stocks. The Council also requested the Commission to draft a common framework as regards to the documentary evidence required to claim an exemption for intra-Community supplies. The latter is included in the proposal amending the VAT implementing regulation.

4.3.VAT identification number amendments

One of the amendments proposed by the Commission concerns the legal value of the VAT identification number of the customer as regards the exemption for the intra-EU supplies of goods in the Member State of the departure of the goods.

Regarding the proposal, providing a valid VAT identification number of the purchaser should become a substantive condition (and not merely a formal condition, as stated by the CJEU with regards to the current VAT rules) for applying the exemption of intra-EU supplies of goods. This modification would be proposed in reply to the demand made by the Member States to amend the current VAT Directive to allow for better monitoring of the flow of goods using the recapitulative statements and the VIES system¹¹⁰.

Therefore, the customer will be obliged to provide the supplier with his VAT identification number attributed by the Member State of taxation. To combat fraud, the location of the goods will need to be mentioned on the invoice/recapitulative statement and information would be exchanged via the recapitulative statement to be submitted by the supplier¹¹¹.

Subsequently, through the introduction of the mandatory reference of the VAT identification number of the customer, it is expected to improve the quality of data exchanged between the Member States as well as to diminish tax fraud¹¹².

¹⁰⁹ COM (2017) 569 final, p. 4

¹¹⁰ Impact Assessment on the Proposal, p. 41

¹¹¹ *Ibid.*, p. 47

¹¹² *Ibid.*, p. 49

5. Conclusions

The Court has recalled over the years that both substantive and formal conditions must be met for the right to deduct to arise. As regards substantive conditions, the Court cites Article 168(a) of the VAT Directive, which provides that the goods or services relied on to give entitlement to that right, must be used by the taxable person for its own taxed output transactions. With regards to formal conditions for the exercise of that right, the Court cited Article 178(a) of the VAT Directive, which requires the holding of an invoice drawn up by Article 226 of such directive.

However, intending to guarantee the neutrality of the VAT system, the CJEU has been developing a line of case-law whereby substance should somehow prevail over form concerning the exercise of the right to deduct¹¹³. Similarly, the same principle of “substance over form” has been reflected and confirmed by the CJEU when applying exemptions for intra-Community transactions.

Therefore, it is apparent from recent case-law that the CJEU has sharply diminished the importance of non-compliance with all formal conditions. That means that if an invoice does not fully comply with specific mandatory invoicing requirements, this does not automatically mean that the VAT on that invoice would not be deductible or exempt. Even though the invoice is the crucial element, the VAT authorities cannot restrict themselves to examine the invoice itself, but must also take into account additional information provided by the taxable person. If a taxable person can prove, by any other means, that all material conditions are fulfilled, the input VAT should be deductible.

It has been seen in case law another example of the “substance over form” principle when it comes to the VAT registration number and time limitation periods. The CJEU has concluded that these two conditions are formal requirements that cannot be conditional upon the exercise of the right to deduct or exempt VAT. However, when dealing with time-bar, a penalty imposed by a Member State will be compatible with the VAT Directive as long as does not preclude the exercise of such rights.

Another finding of the Court is the case of the reverse charge mechanism. Such procedure is also considered a formal requirement. However, when it applies, the Member States do not have to follow the common invoicing requirements but the conditions that themselves can establish under the discretion of Article 178(f) of the VAT Directive.

Nevertheless¹¹⁴, the case may be different if this non-compliance with formal requirements effectively prevents the production of conclusive evidence that the

¹¹³Marie Lamensch (2018) *The principle of ‘substance over form’ with respect to the exercise of the right to deduct input VAT – A critical analysis of the Barlis jurisprudence*, World Journal of VAT/GST Law, 6:2, 129-137, DOI: 10.1080/20488432.2017.1407126

¹¹⁴ See *Collée*, para. 31; *EMS-Bulgaria*, para 71; *Idexx Laboratories*, para 39; *Astone*, para. 46

substantive requirements have been satisfied. In that case, there might be a refusal of the right to deduct or to exempt VAT compatible with the VAT Directive.

Moreover, such rights may be seen as completely limited when the taxpayer intentionally takes part in a transaction connected with fraudulent evasion of the VAT¹¹⁵.

Regarding this last situation mentioned, the CJEU has generally been consistent over the years as it may be understood from the judgment of *Ablessio* or *SC Paper Consult*. However, in the most recent judgment of *Dobre*, the need of proof was no longer essential to refuse the right to deduct. *Dobre* was denied of this right just because the CJEU had some suspicions of this taxpayer being involved in fraudulent transactions. Therefore, it reached the conclusion that the CJEU has been recently stricter when it comes to avoiding possible tax evasion. That seems to be in the line of what the Commission is seeking with its Proposal of a fairer VAT system.

Contrary to that finding by the Court is the case of the identification for VAT purposes where the case law is not in line with the Commission. Such European body has proposed to consider the VAT identification number as a substantive requirement when it comes to intra-Community transactions.

In doing so, the Commission is supporting the national courts' view regarding the identification requirement, but not the CJEU, which has been consistent over the years with its judgments considering the registration a pure formality. Therefore, if finally such a condition is approved it would be able to make the right to exempt dependent on the registration of companies for VAT purposes. However, having been seen in case law the equal treatment given to the right to deduct by the Member States, it might be supposed that similar amendments will be required regarding the right to deduct VAT.

Nevertheless, this is only a hypothesis that is not currently confirmed nor even suggested, however, may open new discussions about the topic concerned in the present thesis.

¹¹⁵See *Mahagében*, para. 45; *R.*, para. 48 -49.

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