



VAT Neutrality v. Equality

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November 26, 2020

Case C-549/11, *Orfey Bulgaria*

33 It is also settled case-law that the ***general principle of equal treatment***, of which the ***principle of fiscal neutrality*** is a particular expression at the level of secondary EU law and in the specific area of taxation, requires similar situations not to be treated differently unless differentiation is objectively justified (Case C-309/06 *Marks & Spencer* and Case C-174/08 *NCC Construction Danmark*)

Neutrality = Equality ?

or

Neutrality \neq Equality ?

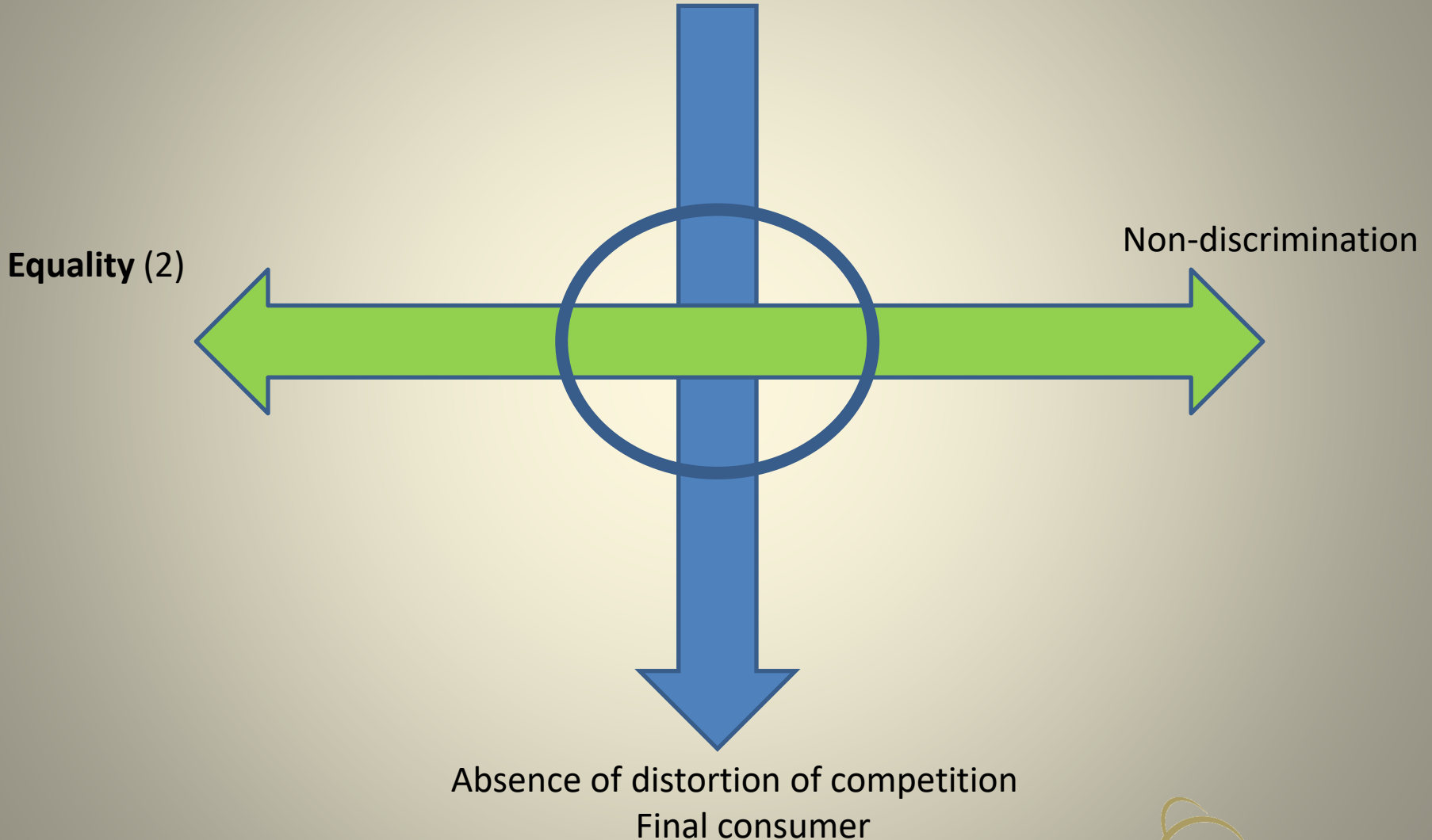
Neutrality

Equality

- | | |
|---|---|
| <ul style="list-style-type: none">• Purpose of the VAT-System | <ul style="list-style-type: none">• General Principle of national and of EU Law |
| <ul style="list-style-type: none">• Same consumption value should bear the same tax | <ul style="list-style-type: none">• Similar situations should be treated on the same way |
| <ul style="list-style-type: none">• Absence of distortion of competition<ul style="list-style-type: none">– At consumption level– In an internal market– With third countries | <ul style="list-style-type: none">• Similar situations should be treated on the same way<ul style="list-style-type: none">• Distortion of competition is irrelevant |
| <ul style="list-style-type: none">• Protected by Tribunals only when specifically mentioned in a Directive | <ul style="list-style-type: none">• Right protected as such by Tribunals except if the Directive allows a discrimination |

Neutrality

Tax planning should not influence business decisions,
Place of production, vertical integration (1)



National v. international Neutrality

- *1916 : German Umsatzsteuer*
 - *Taxation of each transaction /Incentive to vertical concentrations*
- *1920 : French Taxe à la production*

Incentives to vertical integration

- **1947: GATT Agreement**
 - Refund of indirect taxes at the time of exports
- **1952: ESC Treaty**

- *1954: French TVA*
 - *Deduction ensures neutrality of taxes collected at each stage of production*
- **1954-1957: OECC study on productivity**
 - Single tax on consumption is neutral on production
- **1957: Treaty of Rome**
- **1962: First proposals of an European VAT**
- **1966: German Umsatzsteuer considered as discriminatory**
- **1967: Adoption of the First and Second VAT Directives**

In search of solution for national and international neutrality

Neutrality as purpose of the EU VAT

- Same tax burden, whatever the place of production
 - Single market
- **Single tax** on consumption
 - Absence of distortion of competition at retailer's level
- Conciliate freedom of business to organize its activity with economic efficiency
- Deduction of the VAT on costs related to supplies that are themselves taxed
 - Reduce the incentive to fraud ie the collection of the tax at each stage of the production

Exemptions

The obstacle to Neutrality

(or the same tax whatever the place of production)

VAT exemption = limitation of the right of deduction by business /taxation on production

- 1962 European Parliament (Deringer Report)
 - Freedom of Member States (exemptions, special taxes, out of the VAT scope) as far as no impact on intra-EU Trade (in exchange of an immediate introduction of VAT)
- 1967 proposals to tax banking and insurance services + immovable property transactions
- 1977 Sixth VAT Directive
 - Summary of existing VAT exemptions + exceptions
 - 12 specific provisions mitigating the lack of neutrality

Neutrality in more than 460 VAT cases before the CJEU

- Neutrality “Reflects”, “Translates”, “transposes” the Principle of Equality (and linguistic discordances between the versions of the cases)
- Neutrality is used in different senses (Case C-174, *Zimmerman*)
- Fiscal Neutrality includes the Principles of VAT Uniformity and of elimination of distortion of competition (Case C-481/98, *Commission v. France*)

Acceptable distortions of competition and discriminations

- The Court interpretes existing EU rules (e.g. Case C-36/99, *Ideal Tourisme*)
 - “The present state of harmonization”!
 - Objective motivations
- Subsidiarity of the EU rules
- Strict interpretations of the VAT exemptions
 - Elimination of all exemptions ?

Unacceptable distortions of competition and discriminations

- Direct effect of Treaty provisions
- Specific provision of the Directive about “distortions of competition”
- The text of the Directive
 - Right of deduction
- Principle of Equal treatment
- Other Principles of EU law

VAT exemptions at national level

- Any limitation of the right of deduction during the process of production produces distortions of competition at retailers level
 - Not possible to determine with precision the actual level of the tax (probably 5-4% for the social sector)
 - Increase of the compliance cost

VAT exemptions in an international context

- Taxation in the country of the supplier combined with exemption in the country of the customer
 - Non taxation (e.g. Case *BBL*)
- Exemption in the Country of the supplier and taxation in the Country of the purchaser
 - Double taxation (e.g. Case *Eurodental*)
- VAT grouping and cross-border VAT grouping
 - Reduction of the level of taxation by VAT exempt taxable persons (e.g. Case *FCE Bank*)

International VAT/GST Guidelines of the OECD (2017)

- VAT should not lie on business, except when explicitly provided for by legislation
- Business in similar situations carrying similar transactions should be subject to similar levels of taxation
- VAT rules should be framed in such a way that they are not the primary influence on business decision
- Foreign business should be not advantaged or disadvantaged compared to domestic business

Alternative to VAT exemptions and improvement to neutrality

- Zero-rating
 - But objections raised in the early 1960's
 - VAT should not be a tool in order to refund taxes
 - Distorts competition
 - Political pressures against Member States where it is not applicable
 - Impact on determination of own resources
- VAT mechanism in order to collect social security contributions
 - Reduce the cost of the exported goods and services from the social security charges
 - Finance social security contributions by the actual consumption

Consequences of the distinction neutrality v. equality (1)

- Intense business lobbying in favour of VAT grouping goes against the historical objective of the VAT neutrality and equality between large business and SME's
- As long as the principle of equal treatment is respected, tax authorities have no legal means to challenge VAT tax planning

Consequences of the distinction neutrality v. equality (2)

- It is doubtful that procedures in order to limit double taxation are compatible with the principle of equality (e.g. Cross-border rulings)
- Any proposal should be assessed in the light of the Principle of non-discrimination, combined with other EU General Principles, such as the Principle of Proportionality
 - Have discriminatory provisions a legal force in case of absence of justification ?
 - And are the justifications of discriminations not purely formal ?
- Only political intervention can promote neutrality

The Treaties

(art. 113 TFEU, ex-93; ex-99)

Article 93TEC (ex Article 99)

- The Council shall (...) adopt provisions for the harmonisation of legislation concerning turnover taxes, excise duties and other forms of indirect taxation to the extent that such harmonisation is **necessary to ensure the establishment and the functioning of the internal market** within the time-limit laid down in Article 14 (ie 31 December 1992).

Article 113 TFEU (ex Article 93 TEC), as applicable since December, 1 2009

- “The Council shall (...) adopt provisions for the harmonisation of legislation concerning turnover taxes, excise duties and other forms of indirect taxation to the extent that such harmonisation is *necessary to ensure the establishment and the functioning of the internal market* **and to avoid distortion of competition.**”

For more details

Neutrality v. Equality
in “*Virtues and Fallacies of VAT*”,
R.F. Van Brederode Ed.

(to be published by Kluwer Law International
May 2021)

Thank you !



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