

# Public Broadcasting Services and VAT: Some Issues to Be Solved

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In a prior blog, the author highlighted some of the most frequent debates arising from VAT and the public bodies' activities or, more generally, the activities subsidised by public bodies.

One key point for establishing whether public bodies' activities must be subject to VAT or not relates to the aim of preventing distortions of competition that may arise where similar economic activities are carried out by private operators, being these privately performed activities subject to VAT.

One remarkable example of the potential distortions of competition in this regard is the provision of public broadcasting services. The Court of Justice of the European Union (CJEU) will decide in 2021 a crucial pending case regarding these activities, which is expected to clarify the VAT treatment of such activities.

## Public broadcasting services: pending Case C-21/20, *Balgarska natsionalna televizija (BNT)*

The Bulgarian National Television (BNT), a legal person, is the national public provider of audio-visual media services (radio and TV) in Bulgaria.

In the course of its activities, the BNT receives two different streams of income:

1. A subsidy from the state budget, in the form of a flat rate per programme hour, fixed by the Council of Ministers. The consequences of this source of funding for VAT purposes is the crucial point for the CJEU to decide.
2. Self-generated income from advertising and sponsorship. These activities are, without doubt, subject and non-exempted from VAT. Accordingly, they generate a right to VAT deduction. To what extent they create a right to VAT deduction is another critical point for the CJEU to decide.

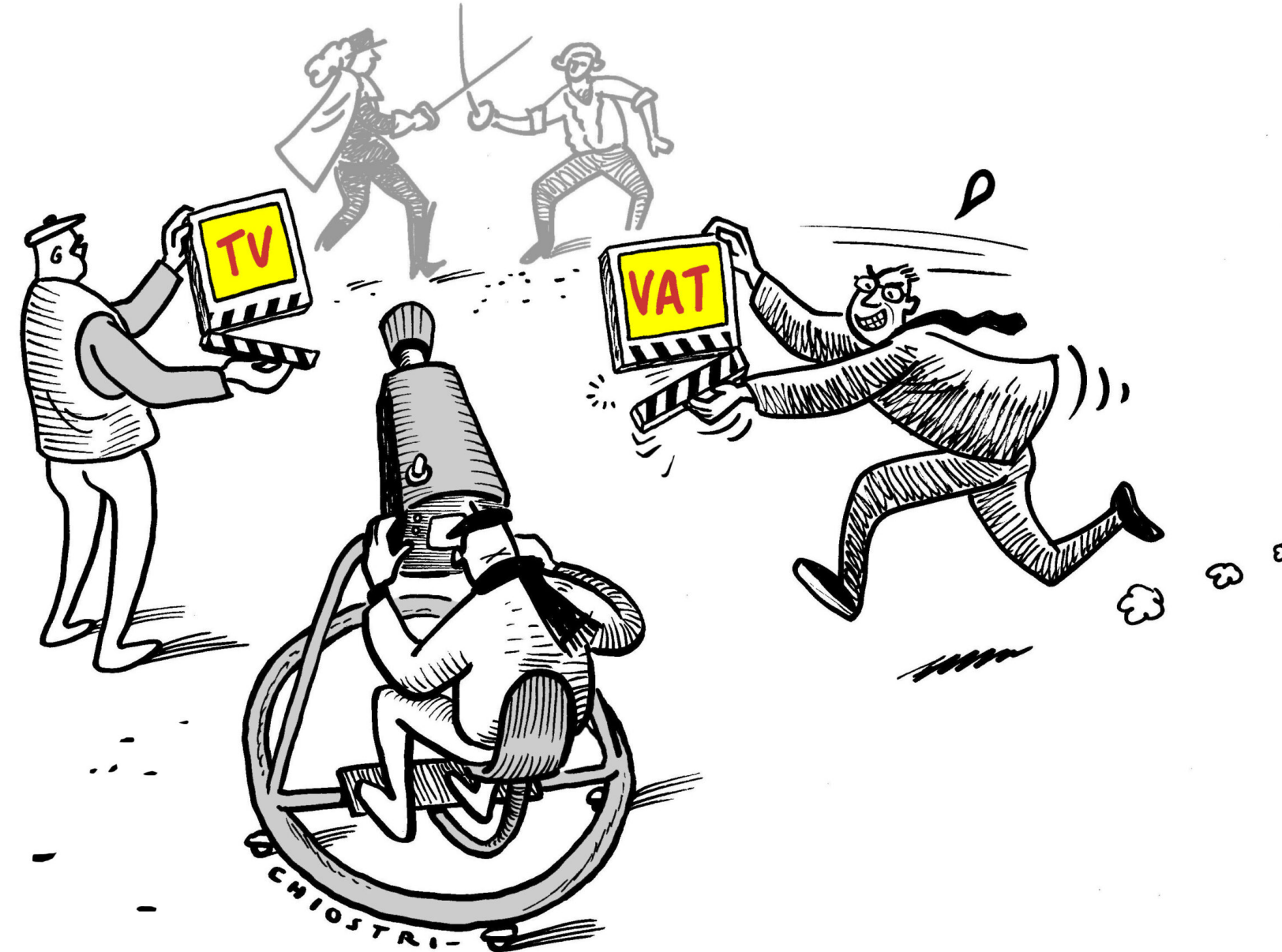
Significantly, the amount of the subsidy exceeded the revenue obtained from taxable supplies many times over.

As a result of a tax audit, the Bulgarian tax authorities recognised only a partial input tax deduction for the indicated supplies, regarding which BNT had made a full input tax deduction.

BNT believes having the right of full input tax deduction concerning the purchases used for its commercial activity. In contrast, it claims partial input tax deduction concerning the purchases used simultaneously for activities of a commercial nature and activities of a non-exclusive commercial nature.

The Bulgarian tax authorities consider that BNT provided both taxable supplies, namely advertising activities, and exempt supplies, namely broadcasting of programmes, and that, in the exercise of the right to an input tax deduction, it could not be established whether the purchases were only connected with exempt supplies or instead with taxable supplies.

The referring Court takes note of prior Bulgarian court's cases issued in 2018. In those previous Bulgarian Court's decisions, the domestic Court decided that BNT was entitled to a full input tax deduction only if it could prove that certain purchases it made, which were intended for its commercial activity, were financed entirely by advertising or other revenues related to the broadcasting activity and not by the public subsidies received. In this connection, the Bulgarian Court stressed that the funds generated by the sale of advertising time had to cover the expenditure for the purchase of programme products, namely films among other things, broadcasted in one of the BNT programmes. However, BNT did not carry out detailed analytical accounting of which part of the television broadcaster's expenditure was borne by the public subsidies and which amount was instead paid by the sale of advertising time. Thus, previous national Court's rulings recognised to BNT only a partial right of VAT deduction.



The referred case raises four main questions for the CJEU to decide, briefly summarised by the author as follows:

1. whether the subsidies received constitute the consideration for the public broadcasting services or whether those services are instead rendered for no consideration at all;
2. in case the subsidies constitute the consideration for the services, whether Article 132(1)(q) of the VAT Directive applies so that the subsidies are exempted from VAT;
3. whether the right of an input tax deduction for purchases is dependent not only on the use of the purchases (for taxable or non-taxable activity) but also on how those purchases are financed (namely, self-generated income and subsidies received);
4. in case of public television broadcaster's activities consisting of both taxable and exempt supplies, having regard to its mixed financing, the scope of the right to an input tax deduction in respect of those purchases and the criteria applicable in this regard.

It is not easy to predict what the CJEU will reply to the above queries in the pending case. Even how the questions are referred to the CJEU is confusing, especially when asking for guidance on calculating the right of VAT deduction. The referring Court invokes, initially, the criteria of effective use of the inputs (inbound supplies) and, posteriorly, for the same purpose, it refers to the way the activities are financed ("a kind of" outbound supplies).

What is clear is that, as noted in our previous post, there is an evident lack of symmetry, in terms of VAT, in pretending on the one hand that the subsidies received (the main source, by far, of income for BNT) do not constitute the consideration for the services, while on the other hand, claiming for a full right of input VAT deduction.

This permanent lack of symmetry between the output VAT and the input VAT was also present in the leading CJEU's case invoked by the parties as a precedent, i.e. the Czech Case C-11/15. In that case, the Court eventually decided that public broadcasting activities, funded by a compulsory statutory charge paid by owners or possessors of a radio receiver and carried out by a radio broadcasting company created by law, do not constitute a supply of services "effected for consideration" within the meaning of that provision and, therefore, fall outside the scope of that directive.

From this, one can conclude either that subsidies are out of the scope of VAT, being activities rendered for no consideration at all, or that the perception of subsidies of that scale is an indication of the non-commercial nature of the activities at hand, which would make these activities exempted from VAT. From any of these two possible interpretations, it follows that a substantial part of the activities shall not be subject to VAT. And indeed, this conclusion might have a relevant influence on limiting the right of input VAT deduction.

Nevertheless, in light of recent CJEU's cases regarding the qualification of subsidies as a consideration for the services rendered, even where these subsidies are in the form of a lump sum (see French Case C-151/13, *Le Rayon D'or*), one cannot dismiss the possibility that the Court would conclude that the overall activity of BNT is subject to VAT. From the summary of the referral to the CJEU made by the Bulgarian Court, it appears that this was the decision taken by the Bulgarian courts in prior cases regarding BNT's activities.

Should the CJEU decide that the subsidies received constitute the services' consideration, this interpretation will grant BNT a full right of input VAT deduction. However, it would also increase the company's output VAT significantly. Thus, in terms of VAT net position (output VAT minus input VAT), this second approach will probably be less favourable to BNT.

The CJEU could also take into account the principle of neutrality, holding in favour of any possible interpretation that will not provoke significant distortions of competition when comparing the VAT treatment of public radio and TV services, such as BNT, and the VAT treatment of privately operated broadcasting services, receiving little or no subsidies at all.

## Author's conclusions

The treatment for VAT purposes of public bodies' activities or, more broadly, activities subsidised by public bodies is a permanent source of conflict amongst taxpayers and tax authorities.

The range of conflicts concerns both output VAT (i.e., if the activities are subject to VAT and if those activities are exempted from the tax) and input VAT (i.e., to what extent these taxpayers can exercise their right to deduct VAT).

In this connection, the current EU VAT legal framework needs continuous interpretation. This reveals that the existing legal framework is probably not consistent or clear enough to offer all stakeholders legal certainty. Even after the interpretative guidance offered by numerous CJEU's decisions on the topic, new debates arise every year.

From the author's point of view, any possible legal solution or interpretative guidance can be inspired by two possible and non-compatible general principles:

1. The prevalence of the promotion of activities for the public interest, such as those provided by the public bodies or financed by the public budget. This first approach would grant a generous right of input VAT deduction, while at the same time concluding that most of the output activities do not have to bear any VAT.

With this purpose in mind, one possible solution would be to zero-rate these activities for VAT purposes, although this would require a significant legislative amendment of the VAT Directive.

A second possible solution, following this inspiration, would be to treat these activities for VAT purposes as any commercial or private activity, but granting to these entities additional public funding covering the VAT that they would not be able to deduct. This seems to be the EU Member States approach, although this could create problems in terms of state aids under the EU competition framework.

2. The prevalence of the principle of neutrality, so that any activity of a similar objective nature is treated alike for VAT purposes. This second general principle has the advantage to prevent any distortion of competition from a VAT point of view.

Activities such as broadcasting, the supply of freshwater, research and investigation, social-housing construction, public road building, education, healthcare, etc., would be treated the same for VAT purposes regardless of the status of the service or goods provider. Suppose the activity at stake is out of the scope of VAT because no consideration is received. In that case, if it is provided by a public body acting as such or it is considered exempt from the tax, the input VAT on the related purchases would not be deductible.

The solutions to this second principle could probably be based on the VAT Directive's current provisions reinforced by a consistent and clear interpretation from the CJEU. In this interpretation, the right of input VAT deduction should be connected with the activities subject to VAT in terms of a rule of effective use of inputs or, in cases where the effective use of inputs cannot be appraised, by using an arithmetic symmetry between the percentage of activities subject to VAT compared with the total income of the entity, as a sort of pre pro-rata rule.

In the author's opinion, the most recent CJEU's jurisprudence tends to support the second approach described above, thus giving prevalence to the neutrality principle and the prevention of distortion of competition.

The CJEU's decision in pending Case C-21/20 will undoubtedly be worth reading. In the end, however, the main issue is not how the activities of public bodies are to be treated for VAT purposes, but instead what is the right way of sufficiently financing the activities performed in the public interest.