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The Economic Activities Subsidised by the Public Budget and Their Right Treatment under VAT: The Case of Public Television Services

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The legal framework of the activities carried out by public bodies

The Value Added Tax (VAT) is a consumption tax paid by entities or individuals who, independently, carry out an economic activity, whatever the purpose or results of that activity.

Although Council Directive 2006/112/EC (the VAT Directive) does not establish a definition of economic activity for VAT purposes, Article 9(1) Second Indent of the VAT Directive considers that:

> Any activity of producers, traders or persons supplying services, including mining and agricultural activities and activities of the professions, shall be regarded as 'economic activity'. The exploitation of tangible or intangible property for the purposes of obtaining income therefrom on a continuing basis shall in particular be regarded as an economic activity.

In the case of activities carried out by public bodies, Article 13 of the VAT Directive establishes that public bodies are not regarded as taxable persons when two cumulative conditions apply:

1. the activities at stake are performed by public bodies, mentioned such as "states, regional and local government authorities and other bodies governed by public law" (the so-called "subjective" condition); and
2. public bodies engage in the transactions at stake as public authorities and not as private economic operators (the so-called "objective" condition).

Even when those two cumulative conditions apply, the activities of public bodies will be subject to VAT in any of these two alternative situations:

1. their treatment as non-taxable persons would lead to significant distortions of competition; or
2. the specific activity is included in the list of Annex I of the VAT Directive, provided that those activities are not carried out on such a small scale as to be negligible. For this comment, it is essential to recall that one of the activities included in Annex I (at point 13) relates to "activities

carried out by radio and television bodies in so far as these are not exempt pursuant to Article 132(1)(q)".

In respect to the activities of public broadcasting, Article 132(1)(q) of the VAT Directive includes amongst the VAT exemptions for certain activities in the public interest "the activities, other than those of a commercial nature, carried out by public radio and television bodies". Where a taxpayer supplies services exempted under Article 132(1)(q), his right to deduct VAT on the acquisitions of goods or services used for these activities is limited accordingly.

Besides the existence of activities not subject to VAT or exempted from the tax by a specific rule, to be subject to VAT the supplies of goods or services carried out within an economic activity must be provided for consideration. The existence of consideration is a pre-condition for granting the taxpayer the right to deduct the VAT incurred in acquiring goods and services.

As the Court of Justice of the European Union (CJEU) has consistently stated[1], for a transaction to be classified as a transaction made for consideration for VAT purposes, a direct link must exist between the supply of goods or the provision of services and the consideration received by the taxable person.

Such a direct link is established where there is a legal relationship between the service provider and the recipient, according to which there is reciprocal performance, the remuneration received by the service provider constituting actual consideration for the service supplied to the recipient.

Trying to summarise the existing EU VAT rules for the activities of public bodies, we can conclude as follows:

1. in some cases, economic activities are not subject to VAT, either because they are carried out by public bodies acting as such and/or because their activity is rendered for no consideration at all;
2. when those activities are subject to VAT, some rules containing specific exemptions may apply: education, healthcare, non-commercial broadcasting activities etc.; and
3. the right to deduct the VAT incurred is conditional to the fact that the rendered supplies are subject to VAT (and not exempted).

VAT and activities carried out by public bodies: the primary sources of a debate

Although, at first sight, the legal framework concerning the application of VAT to public bodies' activities seems to be clear enough, it has been a frequent source of debate, with almost every year new cases reaching the CJEU. Within the list of debated topics before the CJEU in this regard, one can find questions concerning:

1. What types of entities should be considered as "public bodies" for these purposes? Leaving aside the activities of the State itself, the regional or the local governments, this question frequently arises in the case of "other bodies governed by public law" as per wording of Article 13(1) of the VAT Directive. For instance: is a company wholly owned by a State, regional or local government a "public body" for VAT purposes? In most cases, the answer to this question will depend on the rules (private law or public law) governing the company's activity. However, in real life, companies controlled by mixed rules exist, both private and public. Besides, the rules governing the public sector vary significantly from one EU Member State to another.
2. What should be considered as amounting to "distortions of competition" and, further, to which extent one can assume that these distortions are "significant"? Is it enough for VAT purposes that

there is any market competition to consider existing competition distortions, regardless of the relative importance of the public provision of those goods or services? Who must appreciate the existence of significant distortions of competition, the taxpayer, its competitors, or tax authorities?

3. As for the publicly subsidised activities, is there a direct link between the supplies made and the subsidies received so that the latest can constitute the supplies' consideration? Is the answer to this question influenced by the fact that the amount of the received subsidies is not connected with the number of goods or services supplied, but instead it is calculated as a lump sum?
4. When the taxpayer supplies goods and/or services and only some of the transactions are subject to VAT (either because Article 13 of the VAT Directive becomes applicable or because the transactions are rendered for no consideration at all), how shall the right of the incurred VAT deduction be calculated? If the subsidies received cannot be considered remuneration for the supply rendered, does this conclusion influence the VAT deduction calculation?

The number of cases dealing with these and other similar issues regarding the VAT and public bodies' activities or activities financed by public bodies, referred by national courts to the CJEU, is very high. To name but a few, the CJEU already decided: *Lajver Meliorációs Nonprofit Kft* (Hungarian Case C-263/15, rendered by the CJEU on 2 June 2016), *Surgicare* (Portuguese Case C-174/14, rendered by the CJEU on 29 October 2015), *Le Rayon Dór* (French Case C-151/13, rendered by the CJEU on 27 March 2014), *Gmina Wroclaw* (including two different Polish cases: C-276/14, rendered by the CJEU on 29 September 2015, and C-665/16, rendered by the CJEU on 13 June 2018), *Gmina Ryjewo* (Polish Case C-140/17, rendered by the CJEU on 25 July 2018), *Odvolací finan?ní ?editelství vs ?eský rozhlas* (Czech Case C-11/15, rendered by the CJEU on 22 June 2016), *Ntp. Nagyszénás* (Hungarian Case C-182/17, rendered by the CJEU on 22 January 2018), *Gemeente Borsele* (Dutch case C-520/14, rendered by the CJEU on 12 May 2016), *Gemeente Woerden* (Dutch case C-267/15, rendered by the CJEU on 22 June 2016).

The big number of referred cases, the variety of the topics discussed and the number of Member States where these debates have grown give a clear indication that the VAT treatment of public bodies' activities, or more broadly, activities financed with public funds, is far from being clear and probably deserves a more comprehensive and also common approach at the EU level.

Is it relevant that certain activities carried out by public bodies are subject to VAT?

Although there is a wide range of debated topics referred to the CJEU regarding VAT and public bodies' activities, many of those topics have a typical pattern: taxpayers claiming for a full right of VAT deduction (i.e., the inbound transactions), while at the same time considering that many of their supplies are not subject to VAT (i.e., the outbound transactions).

Lack of symmetry between the outbound and the inbound transactions for VAT purposes frequently called the national tax authorities' attention, which contested such an approach.

In the author´s experience, and further to the CJEU's cases as mentioned above, this permanent lack of symmetry for VAT purposes can arise in activities such as research and development (when performed by public bodies like universities or private research entities subsidised by the public budget), the supply of fresh water and/or household waste collection by companies owned by municipalities or by private entities entering into a contract with the municipalities, tourism promotion by entities owned by local or regional authorities, public financing of the construction of houses or roads, etc.

Note that most of those activities (research, education, healthcare, waste collection, etc.) are financed by the Public Treasury precisely because they are considered of society's general interest and beneficial to citizenship.

Should this be the case, whether it makes sense for tax authorities to be so strict with VAT rules when the amount of VAT that could be collected from those entities must be reimbursed to the entity, in the shape of public subsidies, can be questioned.

At least two reasons advocate in favour of following the general VAT rules also for the activities of public bodies:

1. as a general statement, VAT is a consumption tax. Although collected by the taxpayer at each step of the production of goods or services, the VAT deduction's mechanism allows the final consumer to bear the tax burden from an economic point of view. If a taxpayer exercises the right of VAT deduction on its acquisitions (input VAT) and charges no VAT on its supplies (no output VAT), the final consumption remains untaxed; and
2. for those activities where there is a market with different suppliers and customers, the said lack of symmetry for VAT purposes, as regards the activities of public entities, introduces significant distortions of competition detrimental to private suppliers or, more broadly, to taxpayers who cannot receive any kind of public support in the form of subsidies or public funding.

One example of the risk of potential distortion of competition where the VAT treatment is asymmetric for public entities is the public provision of broadcasting (radio, TV) services, specifically discussed in an upcoming blog.

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[1] S*ee*, e.g., paragraph 43 of the CJEU's decision in Case C-528/19, *Mitteldeustche Harstein-Industrie AG*.

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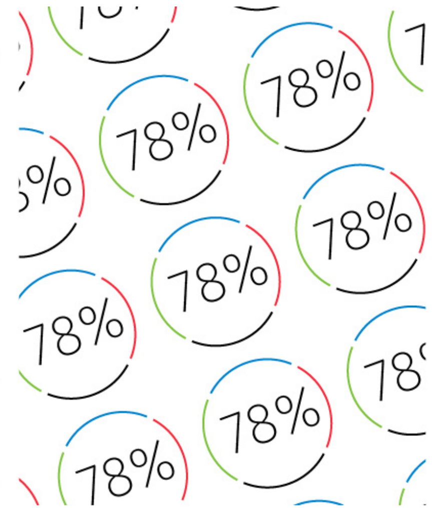

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