Kluwer International Tax Blog

The Contents of Highlights & Insights on European Taxation Issue 8, 2022

Giorgio Beretta (Editor) (Amsterdam Centre for Tax Law (ACTL) of the University of Amsterdam; Lund University) and Dennis Weber (Editor) (Amsterdam Centre for Tax Law (ACTL) of the University of Amsterdam; Loyens & Loeff) · Tuesday, August 30th, 2022

Highlights & Insights on European Taxation

Please find below a selection of articles published this month (August 2022) in Highlights & Insights on European Taxation, plus one freely accessible article.

Highlights & Insights on European Taxation (H&I) is a publication by Wolters Kluwer Nederland BV.

The journal offers extensive information on all recent developments in European Taxation in the area of direct taxation and state aid, VAT, customs and excises, and environmental taxes.

To subscribe to the Journal's page, please click **HERE**

Year 2022, no. 8

TABLE OF CONTENTS

INDIRECT TAXATION, CASE LAW

VAT rate on repair and renovation services for lifts in residential buildings. Court of Justice

(comments by **Luis Aires**) (H&I 2022/240)

– ***DGRFP Bucure?ti* (C-146/21)**. Condition of VAT registration for the application of reverse charge mechanism. Court of Justice

(comments by **Natalia ?vidchi**) (H&I 2022/212)

STATE AID

– ***UK and ITV v Commission* (T-363/19 & T-456/19)**. UK Group Financing Exemption scheme not in line with EU State aid rules. General Court

(comments by **Raymond Luja**) (H&I 2022/214)

FREE ARTICLE

– ***DGRFP Bucure?ti* (C-146/21)**. Condition of VAT registration for the application of reverse charge mechanism. Court of Justice

(comments by **Natalia ?vidchi**) (H&I 2022/212)

Historical background

Under the Romanian tax legislation, the arrangement under which the Value Added Tax (VAT), related to certain domestic transactions, is payable by the customer is regulated in an article with the marginal denomination of ‘simplification measures’, although, in practice, it is better known as ‘reverse charge’.

The ‘simplification measures’ have a pre-accession history in Romania, being enacted for the first time by a Government Ordinance, no. 83/2004, with effect from 1 January 2005 (Article 161.1 from the Romanian Tax Code, adopted by Law no. 571/2003, in force until 31 December 2015). The measures were initially intended to apply regarding supplies of waste, ferrous and non-ferrous waste, and land and buildings. The introduction of this special arrangement, requested by the business sector and by the tax authorities, was justified by the intention to mitigate the VAT evasion related to transactions with such goods, resulting from the non-payment of the VAT by the supplier, who disappeared after the supply, combined with the right of the customer, who was in possession of a valid invoice, to deduct the related input VAT.

By Law no. 494/2004, approving Ordinance no. 83/2004, starting on 2 January 2005, the material scope of this special arrangement was extended to other categories of transactions, including the supply of wood. It should be pointed out that the legal provision of the Romanian Tax Code left the determination of the goods included in the category of ‘wood’ to the Implementing Rules and that the list of such goods had not been enacted through the Implementing Rules until 18 February 2005 (the Implementing Rules of the Romanian Tax Code were adopted by a Government Decision, their purpose being to guide the taxpayers in applying the provisions of the Tax Code. Due to their place in the hierarchy of the legislative acts, the Implementing Rules cannot amend or add to the legal provisions of the Romanian Tax Code. Also, as a constitutional rule, the Implementing Rules cannot be used to regulate matters in the tax field. These rules have been breached over time).

A peculiar aspect of this special pre-accession arrangement was represented by how the reverse charge mechanism was applied. As such, both the supplier and the customer had to apply the reverse charge. It was provided that the deduction of the VAT by the supplier was similar to its collection, and the collection of the VAT by the customer was similar to its payment. In reality, the VAT was not paid effectively by the customer, although the supplier had to issue the invoice with VAT.

Starting on 1 January 2007 (the date of Romania's accession to the European Union), the provisions in the VAT field underwent significant changes (Law no. 343/2006). The material scope of the 'simplification measures' (regulated from that moment by Article 160 of the Romanian Tax Code) narrowed and has been subject to various amendments. As defined within the Implementing Rules, the supply of wood continued to be subject to this special arrangement, although such supplies were not listed in Article 199(1) of the VAT Directive. The author also found no evidence that Romania has received authorization to subject the supply of wood to a derogation arrangement under Article 395(1) of this Directive.

The next critical moment is represented by the amendment made to Article 160 of the Romanian Tax Code on 1 January 2010 (Government Emergency Ordinance no. 109/2009). For this analysis, as a result of the amendment, the 'wood' was no longer defined by the provisions of the Implementing Rules; instead, to determine the scope of the 'wood', reference was made to the Romanian Forest Code (Law no. 46/2008).

It was not until September 2009 that the European Commission received a letter from Romania requesting authorization to derogate from Article 193 of the VAT Directive regarding the supply of different wood products and to designate the customer of such supplies as the person liable to pay the VAT. The authorisation was granted by the Council Implementing Decision no. 2010/583/EU, issued on 27 September 2010. This Decision has no mention regarding its date of entry into force or the date from which the derogation applies; it merely indicates the expiry date, which is 31 December 2013 (the derogation was extended successively by Implementing Decision 2013/676/EU – 31 December 2016 –, Implementing Decision (EU) 2016/1206 – 31 December 2019 – and by the Implementing Decision (EU) 2019/1593 – 31 December 2022. According to the last-mentioned Implementing Decision: 'Derogations that permit use of the reverse charge mechanism are only granted exceptionally for specific areas where fraud occurs, and constitute a means of last resort. Romania should therefore implement other conventional measures to fight and prevent further spreading of VAT fraud in the sector of timber and wood and consequently, should no longer need to derogate from Article 193 of Directive 2006/112/EC with regard to such supplies. It is therefore not necessary at this stage to include specific provisions in Implementing Decision 2013/676/EU concerning further requests to extend the derogation authorized by that Implementing Decision beyond 31 December 2022'.

Therefore, is it highly questionable that Romania was entitled to apply the derogation measures regarding the supply of different wood products between 1 January 2007 and the date the Implementing Decision No. 2010/583/EU was notified to it, which could not have been earlier than 27 September 2010, the date of its issue (See CJ 13 February 2019, C-434/17 *Human Operator*,ECLI:EU:C:2019:112).

The special derogation for the supply of wood and timber is still in force and is regulated by Article 331 of the Tax Code (adopted by Law no. 227/2015, in force starting 1 January 2016).

The requirements of the ‘simplification measures’ arrangement

From the legal provisions regulating the simplification measures, as amended over time, the following criteria emerge as being mandatory:

- The supply must be specifically listed as subject to the special ‘simplification measures’ arrangement.
- Both the supplier and the customer have to be registered for VAT purposes. Only starting with 1 January 2007, it is expressly specified that the VAT registration has to be made according to Romanian legislation, i.e., the VAT number has to be granted by the Romanian tax authorities. This requirement is linked to the next one, meaning that the existence of a VAT number has to be verified when the VAT is chargeable. The VAT registration has to be a valid one, meaning that if the VAT number of the supplier or/and of the customer is revoked when the chargeability occurs, the special regime is not applicable;
- As an exception to the standard rule, the VAT regime in the case of the ‘simplification measures’ is dictated by the chargeability moment. This exception results from the rules implementing the articles regulating the ‘simplification measures’ over time, being provided expressly within the Tax Code, in the article dedicated to the chargeable event and chargeability, only starting on 1 January 2010. This rule generated various complications, because the list of the transactions subject to the ‘simplification measures’ was constantly amended and because the VAT registration status of the parties can change until the completion of the transaction. In summary, if the supply is made before the issue of the invoice or the advance payment, the VAT regime is determined according to the rules in force when the supply is made, irrespective of when the invoice is issued. If, however, before the supply is made, partial or total invoices are issued, or advance payments are made, the chargeability occurs at these moments, but only regarding the amounts of the invoices/advance payments and irrespective of the date of the supply. By applying this rule, there might be situations in which a partial invoice/advance payment is subject to the simplification measure and the remaining price is not, or vice versa, due to the amendment of the material scope or to a change in the VAT registration status of the parties between those moments.
- The ‘simplification measures’ apply only to supplies made within the Romanian territory. This requirement is rather vague and was regulated for the first time on 1 January 2007 within the Implementing Rules. Since 1 January 2010, it has been provided within the Romanian Tax Code. However, only between 1 January 2010 and 31 December 2015, did the Implementing Rules contain a specification, according to which supplies made on the Romanian territory should be understood to be the supplies made by persons registered for VAT purposes according to the Romanian legislation, which have the place of supply of goods and/or services in Romania (before 1 January 2010, to determine the Romanian territory, the Implementing Rules referred to the corresponding article from the Romanian Tax Code implementing the provisions of the VAT Directive regulating the territorial scope. As of 1 January 2016, no additional references have been made to define the expression `supplies of goods/services made within the territory of the country’).

If the requirements mentioned above are fulfilled on a cumulative basis, the application of the ‘simplification measures’ regime is mandatory. In such a case, the supplier has to issue an invoice without VAT (excepting the arrangement before 1 January 2007) and mention ‘reverse charge’ within it. The customer has to determine the VAT and apply the reverse charge mechanism. The responsibility of applying the ‘simplification measures’ belongs both to the supplier and to the customer. However, the tax provisions address the consequences at the level of the customer in the

case of non-compliance, i.e., the customer will be denied the right to deduct the input VAT, wrongfully invoiced by the supplier, and will have to apply the reverse charge mechanism.

The requirement of VAT registration

The judgment delivered by the CJ in the case at hand did not come as a surprise. The outcome of the judgment has already been prefigured, to some extent, by the judgment delivered by CJ in the cases *Fatorie*(CJ 6 February 2014, C-424/12 *Fatorie,* ECLI:EU:C:2014:5) and *Farkas* (CJ 26 April 2017, C-564/15 *Farkas,*ECLI:EU:C:2017:302).

In these two cases, the CJ addressed the issue of the customer's right to deduct the VAT wrongfully invoiced by the supplier for transactions subject to the reverse charge mechanism under a special arrangement. The CJ stressed the substantial nature of the requirement under which the customer is the person liable to pay the VAT, by applying the reverse charge mechanism, irrespective of the existence of any loss of income for the State budget. In *Farkas,* it did not matter that the supplier had collected the VAT on the sale and paid it to the State budget, as opposed to *Fatorie,* where the VAT paid by the customer was not paid to the State budget by the seller because it was declared insolvent.

Indeed, the CJ did not address the requirement of VAT registration in these cases. However, the conclusion after reading these two mentioned decisions is that, in comparison with the standard VAT regime, the CJ addresses derogations more strictly, even in situations implying a cornerstone VAT principle such as the right to deduct. Moreover, it seems that, within this specific derogation arrangement, the Member States are granted a more significant margin of discretion in establishing the formal and substantive requirements. The explanation resides probably in the reasons underlying this derogation, consisting of the prevention of VAT fraud and evasion, correlated with a better understanding of these phenomena at the domestic level by each Member State.

As to the justification underlying this special derogation arrangement, it should be noted that only a specific category of fraudulent transactions is targeted, namely, the one implying a missing trader. It is the case in which a supplier, registered for VAT purposes, issues the invoice with VAT but does not pay it to the State budget and disappears after the transaction is made. On the other hand, the customer registered for VAT purposes holds a valid invoice and is entitled to deduct the VAT. In such cases, the State budget loses revenue in terms of VAT. The application of the reverse charge counteracts such an outcome with a double result: the State does not lose any revenue, and the customer is entitled to exercise its right of deduction. However, because, even under this arrangement, the practice of the tax inspections was to deny the deduction right of the customer in cases which involved suppliers with an 'inappropriate tax behaviour' (suppliers which did not submit the tax statements, did not pay the tax obligations to the State budget etc.), the Romanian Ministry of Finance had to issue a Circular stating that the reverse charge excludes any loss to the State budget, from the VAT perspective, and, therefore, the right of deduction cannot be denied (Circular no. 693567/2016).

Therefore, this special arrangement does not address the fraudulent/tax evasion situations in which the supplier does not hold a valid VAT number, either because it fails to register for VAT purposes when the special threshold established by the 'special exemption scheme' is exceeded or when its VAT number is revoked *ex officio* by the tax authorities. In the latter scenario, under the Romanian legislation, questioned over the time (See CJ 19 October 2017, C-101/16 *Paper Consult,* ECLI:EU:C:2017:775; CJ 12 September 2018, C-69/17 *Gamesa Wind*

România,ECLI:EU:C:2018:703; CJ 7 March 2018, C-159/17 *Dobre*, ECLI:EU:C:2018:161; CJ 18 November 2021, C-358/20 *Promexor Trade*, ECLI:EU:C:2021:936; and CJ 2 May 2022, C-627/21 *Administra?ia Jude?ean? a Finan?elor Publice Sibiu and Direc?ia General? Regional? a Finan?elor Publice Bra?ov* ECLI:EU:C:2022:344. See also: CJ 3 June 2022, C-188/21 *Megatherm-Csillaghegy*, ECLI:EU:C:2022:444), the supplier must collect and pay the VAT to the State budget and comply with special declaration obligations, but it cannot deduct the VAT related to its acquisitions. On the other hand, the customer is not entitled, with few exceptions, to deduct the VAT related to the purchases made from a supplier with a revoked VAT number.

In my opinion, the interpretation of the CJ in the case at hand has an impact not only in situations in which the supplier is registered retroactively by the tax authorities for exceeding the threshold provided for the 'special exemption scheme', but also in cases in which the VAT number of the supplier is revoked, with subsequent re-activation or even irrespective of such a re-activation. Therefore, an interpretation of the CJ in favour of the claimant would have had a significant impact at many levels and would also affect the interpretation delivered by it in Romanian cases concerning the revocation of the VAT number. Moreover, if the CJ had ruled in favour of the claimant, the administrative burden, i.e., the application of the reverse charge, the submission of the VAT returns etc., would have been passed on to the customer, even if it is the supplier who did not comply with legal requirements.

I am unsure if the CJ knew the extent of a contrary interpretation. However, one cannot fail to notice that the Court relied on a literal interpretation of Articles 193, 199(2) and 395 of the VAT Directive to decide on the substantive nature of the (valid) VAT number requirement. If the EU Court had applied a teleological method of interpretation, the outcome would probably not have been the same because, as mentioned, the simplification measures address only a specific category of evasion.

A vital clarification made by the CJ in the case at hand is the conclusion from paragraph 43 of the judgment, namely, that the right of the customer to deduct the VAT is secured when the supplier is not registered for the purpose of VAT at the time of the chargeability. This specification is important because there are cases in which Romanian tax inspectors have a different approach when the person subject to tax inspection is the customer. Only recently, in a specific case implying a supply from the scope of the 'simplification measures', the tax inspection denied the deduction of the VAT invoiced by a bailiff in the name and in the account of the debtor who had the VAT number revoked, on the ground that the customer should have applied the reverse charge mechanism.

Of course, the effective exercise and the moment of the deduction will have to be analysed case-by-case because different scenarios can be imagined.

Questions, however, arise regarding the right of deduction in the specific case referred to the CJ. It is mentioned in paragraph 21 of the judgment that the VAT was calculated by applying the 'per cent increase' method, i.e., the price included the VAT. This method of calculating the VAT was provided within the Implementing Rules after the CJ delivered the judgment in *Tulic? and Plavo?in* (CJ 7 November 2013, C-249/12 and C-250/12 *Tulic? and Plavo?in*, ECLI:EU:C:2013:722) and is usually employed by the tax inspections when the supplier cannot recover the VAT that has to be collected from the customer, particularly in cases in which the customer is an individual or a non-taxable person. This method ensures that the supplier is not

treated as the final consumer. However, when a customer is a taxable person registered for VAT purposes, the VAT is added usually by the tax authorities to the price, and it is considered recoverable through the correction invoice the supplier has to issue following the tax inspection for the customer to be able to deduct the VAT. Considering this, it is questionable if it is correct in this specific case for the customer to deduct the VAT included in the price, especially if the entire paid amount was deducted as cost. If, however, the tax authorities appreciated that the supplier has indeed no possibility to recover the VAT from the customer because, for example, it no longer exists or is in bankruptcy, then the claimant's arguments regarding the application of the reverse charge by the customer are unfounded.

In general, considering the entire VAT system in Romania, the interpretation provided by the CJ in the case at hand prevented a snowball effect with a significant adverse impact on the principle of legal certainty. Moreover, by ruling in favour of the claimant/supplier, the supplier's fault would have burdened the customer without any justification.

Kluwer International Tax Law

This entry was posted on Tuesday, August 30th, 2022 at 10:55 am and is filed under Customs and Excise, Direct taxation, EU law, Indirect taxation
You can follow any responses to this entry through the Comments (RSS) feed. You can leave a response, or trackback from your own site.