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Highlights & Insights on European Taxation

Please find below a selection of articles published this month (May 2024) in Highlights & Insights on European Taxation, plus one freely accessible article.

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– ***Dyrektor Izby Administracji Skarbowej w Bydgoszczy*** **(C-606/22)**. EU law precludes refusal of VAT refund after error in tax rate and absence of invoice. Court of Justice

(comments by **Emilia Sroka**) (*H&I* 2024/117)

The issue concerning the entitlement to seek return of excessively charged VAT, as evidenced by a cash register receipt, has attracted significant attention and debate. In this particular case, it is undisputed that the taxable person, acting in good faith, remitted an incorrect, overstated amount of VAT to the State Treasury. However, the tax authorities deemed a VAT return impossible, citing two factors: (i) the lack of a domestic legal basis for such adjustment, and (ii) the belief that refunding the taxable person would lead to unjust enrichment of Company B.

The preliminary question revolved around determining whether EU VAT regulations and the principles of neutrality, proportionality, and equal treatment permit Polish tax authorities to refuse the taxable person's request for adjustment of the VAT taxable amount and output tax based on this argumentation.

Regarding the first argument, the Court of Justice of the European Union (hereinafter: 'CJ') unequivocally indicated that it is possible for the taxable person to adjust the VAT due in the case of sales to consumers where cash register receipts were issued instead of invoices. The CJ noted that even in such circumstances, a taxable person who erred in applying a VAT rate that is too high is entitled to seek a refund from the tax authorities of the Member State concerned.

In this instance, the Court fully endorsed the Advocate General's position (hereinafter: 'AG'), who suggested such a response to the preliminary question in this regard (AG Kokott 16 November 2023, C-606/22 *Dyrektor Izby Administracji Skarbowej w Bydgoszczy*, ECLI:EU:C:2023:893, paragraph 73].

The CJ did not share the stance of the Polish authorities, who argued that since the EU VAT law does not regulate the matter of sales registration via cash registers at all, the possibility of adjusting receipts depends on the decision of each individual Member State (Written Comments of the Republic of Poland (RP) in case C-606/22, 6 January 2023, ref. DPUE.9323.408.2022(2)(AKS), obtained under the access to public information procedure, paragraph 9). Therefore, if a particular Member State has not opted to introduce such a provision into its legislation, demanding the taxable person's right to adjust the VAT due should be considered unjustified (RP's Written Comments, paragraph 10).

It should be noted that it is undisputed that in the absence of relevant EU regulations, the applicable procedural provisions are, in accordance with the principle of procedural autonomy of the Member States, the internal regulations of each Member State. However, the autonomy of Member States in this regard is limited by the requirement to respect the principles of effectiveness and equivalence (for example, CJ 19 September 2006, in joined cases C-392/04 and C-422/04, *i-21 Germany GmbH and Arcor AG & Co. KG v Bundesrepublik Deutschland*, ECLI:EU:C:2006:586, paragraph 57).

As the AG rightly observed, in VAT law, the entrepreneur is merely the tax collector acting in the interest of the State and, therefore, is obligated to pay only the tax that is legally owed (and not the tax that was calculated incorrectly). The principle of effectiveness thus requires, in principle, the ability to adjust inaccurately declared VAT liabilities to the VAT actually owed (Opinion AG, paragraph 48). The AG also emphasized that the CJ has consistently held in its established case law that taxes levied in breach of EU law must be refunded (for example, CJ 10 April 2008, C-309/06 *Marks & Spencer plc v Commissioners of Customs & Excise*, ECLI:EU:C:2008:21, paragraph 35). Therefore, if national law does not allow for the adjustment of the tax return and the exercise of a corresponding right to a refund, such a right arises from EU law (Opinion AG, paragraph 49).

The CJ shared the AG's position, emphasizing in the judgment that in situations where EU VAT law does not address corrections of taxable persons' tax returns when an incorrect VAT rate was applied, Member States should provide, in their national legal systems, for the possibility of adjusting improperly applied tax in accordance with the principles of effectiveness and equivalence (Judgment, paragraph 30). By making that correction impossible where the taxable person's economic activity does not lead to invoicing but merely to the issue of cash register receipts, a practice such as that of the tax authorities of the Member State concerned fails to observe the principle of effectiveness (Judgment, paragraph 31).

The CJ's decision on this matter is significant but not surprising. It is noteworthy that in the Austrian case *P GmbH*, the Court ruled that a taxable person who has supplied a service and who has stated on the invoice an amount VAT calculated on the basis of an incorrect rate is not liable for the part of the VAT invoiced incorrectly if there is no risk of loss of tax revenue on the ground that the recipients of that service are exclusively final consumers who do not have a right to deduct input VAT (CJ 8 December 2022, C-378/21 *P GmbH v Finanzamt Österreich*, ECLI:EU:C:2022:968).

However, in this case, the CJ limited its interpretation to Article 203 of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (hereinafter: 'VAT Directive'), which regulates the issue of any VAT liability based on an invoice.

The approach, according to which the taxable person always has the right to adjust their tax return, regardless of whether the recipient of the service was a consumer and how the transaction was documented, either by a receipt or an invoice, deserves full approval. It should be noted that every established gross price always includes VAT at the legally prescribed rate – VAT is always automatically included in the agreed price, even if the taxable person errs in determining the applicable rate (Judgment, paragraph 27). It follows that if the taxable person did not remit the due VAT, it must be presumed that what they received from the transaction includes this tax, and therefore, they are obliged to make an adjustment. By symmetry, the above principles must apply in cases where the amount of VAT was inflated by applying a higher rate than required by law. In such a situation, the right to correction cannot be denied to the taxable person.

In the case of the second argument concerning the potential unjust enrichment of the taxable person, the CJ transferred this assessment to the national courts. The CJ held that the tax authority can rely on unjust enrichment on the part of that taxable person only if they have established, following an economic analysis which takes account of all the relevant circumstances, that the economic burden that the tax levied, though not due imposed on that taxable person has been completely neutralised.

In this instance, the CJ did not fully follow the AG's suggestion, who proposed considering that the taxable person is not unjustly enriched in any event in the case of a fixed amount agreed with a final consumer (Opinion AG, paragraph 73). The AG also proposed this decision in the case of *P GmbH* (Opinion AG Kokott, *P GmbH*, paragraph 76).

From the established case law of the CJ, it follows that EU law allows national legal systems to refuse the refund of unduly collected taxes if it leads to unjust enrichment. However, EU law supports the view that defence against unjust enrichment should be narrowly applied, primarily meaning that the burden of proof in this regard lies with the State (for example, *Marks & Spencer* (C-309/06, paragraphs 41-43) and CJ 2 October 2003, C-147/01 *Weber's Wine World and Others*, ECLI:EU:C:2003:533, paragraphs 94 to 100).

Considering the issue of unjust enrichment, one must take into account the broader context of the logic of VAT taxation. Undoubtedly, the economic burden of VAT, due to its incorporation into the prices of services offered by the taxable person, is borne solely by the purchasers of these services, who are end consumers.

The European Commission, referring to this logic, has recognized that in the case of wrongly paid VAT, the refund of this tax should, as a rule, be made to the recipient of the services, rather than the taxable person who merely collects the tax (Written Comments of the European Commission in case C-606/22, 20 December 2022, ref. sj.d(2022)9915860, obtained under the access to public information procedure, paragraph 59). The European Commission acknowledged that EU law

allows for VAT refunds to be obtained by the taxable person, but on the condition that the final recipient, who actually bore the burden of the tax, is not deprived of the possibility of recovering the unduly paid amount (EC's Written Comments, paragraph 60). The European Commission also pointed out that in the present case, it cannot be absolutely ruled out that consumers, for example, those who had a subscription to the fitness club operated by Company B, could be identified, which would practically enable the Company to refund these amounts to those customers if recovered from the State Treasury (EC's Written Comments, paragraph 65).

Similar arguments were invoked by the Polish authorities. In their view, the inability to refund VAT to the taxable person in the present case is intended to prevent a situation where a taxable person, who did not actually bear the burden of VAT, receives unjust enrichment (RP's Written Comments, paragraph 18). The authorities emphasized that in the case of providing access to a fitness club's premises, Company B did not bear the economic burden of VAT. The burden of this tax was, in fact, passed on by Company B to the consumers who purchased services from it. Consequently, only such purchasers (and not Company B) should be able to potentially claim a refund of the overpaid VAT due to the application of an overstated rate (RP's Written Comments, paragraph 11). In this scenario, any VAT refund to the taxable person would only be possible after the end consumers received a refund of the overpaid tax (RP's Written Comments, paragraph 14).

The AG disagreed with the approach presented by the EC and the Polish authorities. In her view, which fully deserves approval, in the case of fixed amounts (that is, gross prices) in relation to the end consumer, unjust enrichment of the taxable person should be excluded per se because, at the time of the transaction, the taxable person must either accept a lower profit margin or lower competitiveness than its competitors (Opinion AG, paragraph 63). In the AG's Opinion, an undertaking competing with Company B and applying the correct tax rate would have been in a significantly better position on the market since the competitor could offer a lower price. This argument speaks against the possibility of unjust enrichment of Company B in the present case (Opinion AG, paragraph 58).

Similar views are expressed in legal doctrine. It is pointed out that, for instance, even if the claimant is able to raise prices in a global economy full of substitutes and pass on the rise in prices to consumers, it could certainly be the case that in the absence of the tax, the claimant's profits would have been higher at the new price. In such a case, the State has deprived the taxable entity of the potential profits they would have made (T. Capriles, *Shortcomings of the EU Passing on Defence*, 1 World Journal of VAT/GST Law 47 (2012), p. 58).

In its judgment, the CJ also highlighted that a taxable person who, in accordance with the initially recommended interpretation by the tax authority of a Member State, applied a standard VAT rate, undoubtedly found themselves in a less favourable situation than their direct competitors who applied the reduced VAT rate (Judgment, paragraph 33).

The AG rightly observed that in the case under consideration, the enrichment inevitably accrues to the State or the taxable person. Of those two parties, however, it was the Polish State which, by 'specifying' an incorrect rate, caused the collection of an excessively high tax and thus enriched the Polish State (Opinion AG, paragraph 70). The AG acknowledged, and it is worth endorsing this argument, that accepting a situation where the State that caused the incorrect VAT calculation in respect of the taxable person is unjustly enriched by retaining the tax seems contrary to the principles for a State governed by the rule of law. Refusing to return the unlawfully obtained tax would leave Poland with the economic advantages that its own unlawful behaviour had caused in the first place (Opinion AG, paragraphs 67-68).

The discussed position is consistent with AG Tesauro's view in *Comateb and Others* (C-192/95 to C-218/95), who pointed out that the reimbursement of the sum unduly paid offsets the unjust impoverishment of the trader who paid charges to the authorities that were not properly due. It is irrelevant that these charges were passed on to the purchaser, as the trader probably had to adjust their profit margin or accept a reduction in sales volume to comply with domestic legislation. If a choice must be made between penalizing a taxable person who paid charges not properly due to authorities that has violated Community law for years, it should not be the taxable person who is penalized (Opinion AG Tesauro 27 June 1996, C-192/95 to C-218/95 *Comateb and Others*, ECLI:EU:C:1997:12, paragraph 22]. In addition, doctrinal sources argue that relying on the unjust enrichment doctrine to justify the unjust enrichment of a law-breaking State is inappropriate (see Capriles 2012, op. cit., p. 60). It is regrettable that in the discussed case, the CJ did not take the opportunity to address whether the issue of unjust enrichment is influenced by factors such as the 'culpability' of the State, which not only misled the taxable person but also unjustly enriched itself.

In summary, in the case of the second argument, the ruling of the CJ cannot also be considered surprising. In previous judgments (for example, CJ C-147/01 *Weber's Wine World and Others*, paragraphs 96, 100 and CJ 16 May 2013, C-191/12 *Alakor Gabonatermel? és Forgalmazó Kft. v Nemzeti Adó- és Vámhivatal Észak-alföldi Regionális Adó F?igazgatósága*, ECLI:EU:C:2013:315, paragraph 30), the CJ has indicated that the question of whether the repayment claimed in the dispute in the main proceedings seeks only to neutralize the economic burden of the tax unduly paid or, conversely, could lead to unjust enrichment for the benefit of the taxable person, is a question of fact to be determined by the national court, which is free to assess the evidence adduced before following an economic analysis in which all the relevant circumstances are taken into account.

As the doctrine rightly points out, the problem with this stance is that it is vague, and results in legal uncertainty. In practice, it is likely to mean that each Member State interprets on a case-by-case basis, and, without a common formula, the burden of proving passing on (see Capriles 2012, op. cit., p. 57). Regrettably, the CJ did not seize the opportunity to provide explicit economic or legal principles for guidance in the course of delivering the discussed judgment.

Dr. Emilia Sroka

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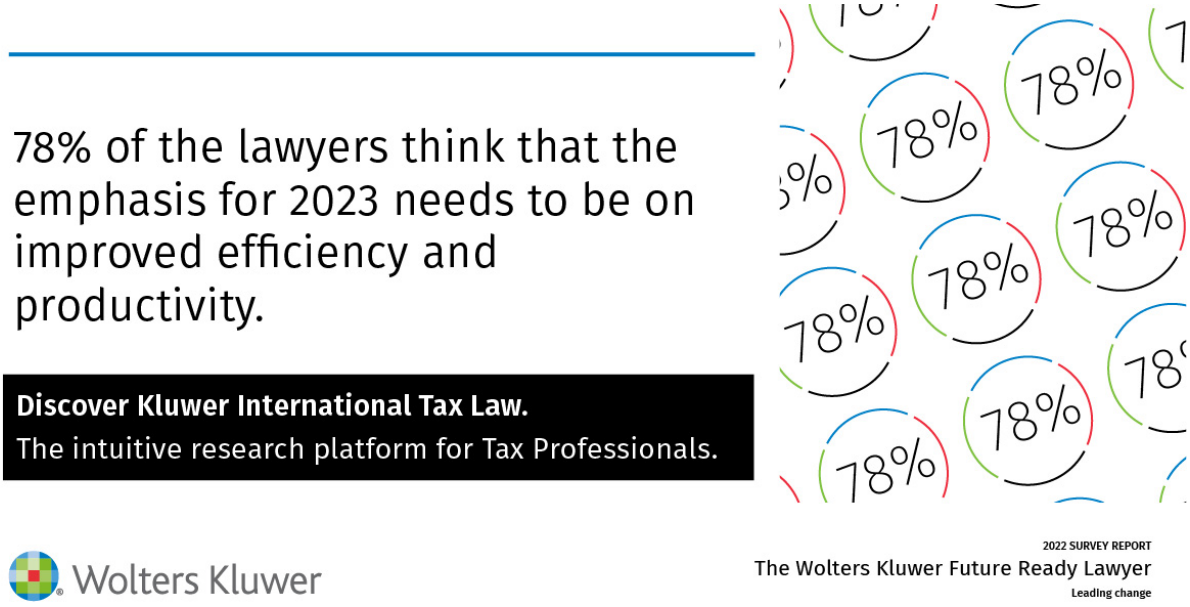

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