



International Fiscal Association

HOW CAN HONEST TAXABLE PERSONS PROTECT THEMSELVES AGAINST VAT FRAUD?

Guidelines from the Jurisprudence of the ECJ

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- Settled Case Law:
 - The common system of VAT ensures **neutrality** of taxation of all economic activities.
 - The **right to deduct** is an **integral part** of the VAT system.
 - **In principle** it may **not** be **limited**.
 - **Whether the VAT** payable on prior or subsequent sales of the goods concerned **has or has not been paid is irrelevant**.



- However: The **objective criteria** which form the basis of the concepts of “supply of goods effected by a taxable person acting as such” and “economic activity” **are not met where tax is evaded** by the taxable person himself.
- In the same way, a **taxable person who knew or should have known** that he was taking part in a transaction connected with fraudulent evasion of VAT **must be regarded as a participant in that fraud**, irrespective of whether or not he profited by the resale of the goods.



- Examples from the Case Law:
 - *Optigen* (Case C-354/03):
 - Case: *Optigen* purchased CPUs; deduction of input VAT refused as supplier did not pay VAT
 - ECJ [p. 52]: “**Nor can the right to deduct input VAT** of a taxable person who carries out such transactions **be affected** by the fact that in the chain of supply of which those transactions form part another prior or subsequent transaction is vitiated by VAT fraud, **without that taxable person knowing or having any means of knowing.**”



- Examples from the Case Law:
 - *Kittel and Recolta* (Case C-439/04, C-440/04):
 - Case: *Kittel* purchased computer components, *Recolta* purchased luxury vehicles; deduction of input VAT refused as suppliers did not pay VAT
 - ECJ, [p. 61]: “By contrast, where it is ascertained, **having regard to objective factors**, that the supply is to a taxable **person who knew or should have known** [...].”



- Examples from the Case Law:
 - *Mahagebén and Dávid* (Case C-80/11, C-142/11):
 - Case: *Dávid* undertook to perform various construction works; as he did not have own employees he used a subcontractor; this subcontractor neither had employees and used another subcontractor; deduction of input VAT was refused as the second subcontractor did not pay VAT
 - ECJ, [p. 50]: “[...] without that **authority establishing, on the basis of objective evidence**, that the taxable person concerned knew, or ought to have known, that [...].”



- Examples from the Case Law:
 - *Mahagebén and Dávid* (Case C-80/11, C-142/11):
 - ECJ, p. 66: “[The right to deduct cannot be refused] on the ground that the taxable person **did not satisfy himself** that the issuer of the invoice [...] **had the status of a taxable person**, that **he was in possession of the goods** [...] and **was in a position to supply them**, and that **he had satisfied his obligations as regards declaration and payment of VAT** [...] and the **taxable person is not in possession of any material justifying the suspicion** that irregularities or fraud have been committed [...].”



- Examples from the Case Law:
 - *Tóth* (Case C-324/11):
 - Case: *Tóth* undertook building works using a subcontractor who did not declare his employees to the tax authority and whose license was finally revoked; deduction of input VAT was refused as the subcontractor ceased to be a taxable person



- Examples from the Case Law:
 - *Tóth* (Case C-324/11):
 - ECJ, [p. 45]: “[The] fact that a taxable person **did not verify** either **whether a legal relationship existed between the workers employed on a work site and the issuer of the invoice** or **whether the latter had declared those workers does not constitute an objective factor** which demonstrates that the addressee of the invoice knew or ought to have known [...], **where the addressee was not in possession of any material justifying the suspicion** that irregularities or fraud had been committed within that invoice issuer’s sphere of activity.”



- Conclusions:
 - No definition of „knew or should have known”
 - Objective evidence necessary
 - Investigative requirements depending on circumstances
 - Test question: Is the addressee of the invoice in possession of any material justifying the suspicion that fraud have been committed?



- Burden of proof?
 - *Bonik EOOD* (C-285/11), p. 43: “[S]ince the refusal of the right of deduction is an exception to the application of the fundamental principle constituted by that right, it is incumbent upon the competent tax authorities to establish, to the requisite legal standard, the objective evidence needed to substantiate the conclusion that the taxable person knew, or should have known, that [...]”



- Risk management depending on
 - Type of business
 - Duration of business relationship

