VAT ON PURCHASES IN CASE OF VAT CODE CANCELLATION: TO BE OR NOT TO BE DEDUCTIBLE?

Lavinia Lazăr*
Viboal FindEx

Abstract

The right of taxable persons registered for VAT purposes to deduct the VAT they owe or pay for goods and services purchased in their current activity is a fundamental principle of the VAT system established by European Union law. Moreover, another essential principle, the principle of tax neutrality, requires that the right to deduct VAT to be granted even if the formal requirements have not been met by the taxable persons involved in a transaction, as long as the substantive requirements are properly fulfilled. In this context, can the revocation of the VAT registration of a taxable person be a sufficiently grounded reason for limiting the right to deduct the tax? In the framework of this article, we will try to analyze this question at the level of national legislation and practices in relation to several Romanian cases relevant to this issue, solved by the Court of Justice of the European Union (hereinafter CJEU).

Keywords: value added tax, registration for VAT purposes, right of deduction, cancellation, VAT code

JEL classification: H87, K34

1. The national legislative framework

Until recently, more precisely by the end of 2016, Romanian tax legislation established that taxable persons who made purchases from suppliers that had their VAT code revoked were not entitled, without any exception, to deduct their tax on transactions made in relation with that partner. Moreover, in case of taxable persons who themselves were in the situation of cancellation of their own VAT code, they could not exercise their right to deduct VAT on

* Corresponding author, Lavinia Lazar - lavinia.lazar@viboal-findex.ro

any acquisition made during this period in their current activity, without exception. Practically, the applicable national legislation at that time established a systematic and definitive denial of the right to deduct VAT on the ground of revocation of the VAT code, irrespective of any other considerations such as the fulfilment of the substantive conditions of the transaction.

Subsequently, as of 1 January 2017, the Fiscal Code was amended in sense that it allows that VAT due or paid by persons who have the VAT registration canceled or to persons in this situation to be able be deducted only once the VAT code has been reactivated. Thus, only after the situation which led to cancelation of VAT code ceases and re-registration for VAT purposes takes place, both the taxpayer concerned and his trading partners may exercise their right to deduct VAT on transactions carried out during the period in which the registration for VAT purposes has been canceled. More specifically, tax regulations have been modified from a clear denial of the right to deduct in such cases, to a postponement of the right until re-registration for VAT purposes.

But, what are the situations where the registration for VAT purposes of a taxable person is canceled by tax authorities? Are these situations difficult to achieve in practice by a taxpayer if he/she shows adequate fiscal behavior? Considering the legal provisions in this respect, we observe that the VAT code is revoked by the tax authorities according to art. 316 par. (11) of the Fiscal Code in the following cases:

- if the taxable person concerned is declared inactive according to the provisions of the Fiscal Procedure Code;
- if the associates or administrators of the taxable person or the taxable person himself have entered in the criminal record the offenses and/or the acts stipulated in art. 4 par. (4) lit. a) of the Government Ordinance no. 39/2015 on the criminal record.
- if the taxable person has not filed any tax return for 6 consecutive months for the tax period the calendar month, respectively for 2 consecutive quarters for the tax period the calendar quarter.
- if in the last 6 consecutive tax returns submitted for the tax period the calendar month or the last 2 consecutive tax returns for the fiscal period the calendar quarter did not exist any purchase of goods or services or any deliveries of goods or services performed during the reporting period for which the tax return is submitted.
- if the taxable person presents a high fiscal risk in accordance with the criteria established by a tax administration order.

Therefore, we consider that among these conditions, on the basis of which the tax authorities cancel the VAT code of a taxpayer, we also find common situations, which do not definitely prove fraudulent behavior, situations in which an ordinary taxpayer proving an adequate tax compliance can be from a simple human error. The most eloquent example in this respect is a situation that is quite common in our opinion, in which, due to expiration of the duration of registered office (for example by omitting the extension of the rental agreement for the registered office space), a taxable person is declared as inactive taxpayer and as a result VAT registration si also revoked. Such a situation can be quickly remedied by extending the duration of registered office to the Trade Registry, the taxpayer being then fiscally reactivated and re-registered for VAT purposes.

Coming back to the rules relating to the right to deduct VAT in situations of VAT code cancellation presented at the beginning of this article, essentially to be analyzed in this issue we consider the following: the primary condition underlying the justification of the right to

deduct VAT should be, according to the current provisions of national law, that the taxable person has reactivated his VAT code or that the substantive requirements of Directive 112/2006 / EC on the Common System of VAT and that the proof of a fraudulent intention is missing? In this respect, we will present some of the Romanian VAT cases solved by the CJEU relevant to the situation under discussion.

2. Romanian cases at the CJEU

Tax administration's practice of refusing VAT deduction on the basis of the provisions of National Tax Code is quite common, as confirmed by the numerous disputes between the Romanian taxpayers and the tax administrations reached at the CJEU on this issue.

2.1. C101/2016- Paper Consult SRL

Description of the dispute:

Rom Packaging SRL was declared as inactive taxpayer on October 7, 2010 for failing to submit tax returns and revoked from the Register of taxable persons registered for VAT purposes as of 1 November 2010. Based on a contract concluded on January 3, 2011 Rom Packaging has provided services to Paper Consult SRL. The latter deducted the VAT for the purchased services, and Rom Packaging paid the tax collected to the state budget. The tax administration considered that Paper Consult would not have been entitled to deduct VAT on the services provided by Rom Packaging, given that at the date of conclusion of the service contract, the latter appeared in the Inactive Taxpayers Register. Paper Consult challenged the decision issued by the tax administration in this regard, considering that the exercise of the right to deduct VAT depends exclusively on compliance with the conditions of Art. 178 of Directive 112/2006 / EC on the Common System of VAT.

Questions to the Court for a preliminary ruling:

„(1) Does Directive 2006/112/EC preclude national rules under which a taxable person is denied the right to deduct VAT on the ground that the person upstream, who issued the invoice in which the expenditure and the VAT are indicated separately, has been declared inactive by the tax authorities?

(2) If the answer to the first question is in the negative, does Directive 2006/112/EC preclude national rules under which it is sufficient to display the list of registered inactive taxpayers at the headquarters of the NAFA and to publish that list on the website of that agency, in the section "Public information — Information relating to economic operators" in order that the right to deduct VAT in the circumstances described in the first question may be refused?"

Judgement of the Court:

„Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax must be interpreted as precluding national rules, such as those at issue in the main proceedings, under which the right to deduct value added tax is refused to a taxable person on the ground that the trader which supplied a service to that taxable person and issued a corresponding invoice, on which the expenditure and the value added tax are indicated separately, has been declared inactive by the tax authorities of a Member State, that

declaration of inactivity being public and accessible on the internet to any taxable person in that State, in the case where that refusal of the right to deduct is systematic and final, making it impossible to adduce evidence that there was no tax evasion or loss of tax revenue."

In this case, the CJEU has established that European Union law prohibits national legislation under which a taxable person would not be entitled to deduct VAT on an acquisition from a supplier with the VAT code cancelled due to the fact that he was declared inactive taxpayer, when the cancellation of the right to deduct the tax for this reason is systematic and definitive without the possibility of proving the absence of tax fraud or a loss of budgetary revenues. It is important to note that in this case the applicable law is the one before 2017, in which, according to the National Tax Code, the deduction right was categorically cancelled in the context of one of the transaction partners having the VAT code cancelled.

2.2. C69/17- Gamesa

Description of the dispute:

Siemens Gamesa Renewable Energy Romania SRL, formerly Gamesa Wind Romania SRL, is a Romanian law company whose main activity is the installation and maintenance of wind farms. It was declared as inactive taxpayer during the period October 7, 2010 - May 24, 2011, due to the fact that it did not fulfill any declaratory obligation stipulated by legislation during a calendar semester. Following a tax audit during which the period from May 15, 2009 to December 31, 2013 was checked for VAT and corporate income tax, Gamesa received a tax decision issued by the tax administration which denied the right to deduct VAT on purchases incurred in the period of inactivity, a right of deduction exercised by the company after re-registration for VAT purposes, and set up payment obligations for the amount of that VAT. In his application, Gamesa repaid to the tax administration mainly the failure to comply with the principle of proportionality and the principle of VAT neutrality, since all the obligations requested to reactivate the VAT code were fullfiled and requested the annulment of that tax decision. In his defense, the tax administration invoked the need to collect VAT correctly and prevent tax evasion.

Questions to the Court for a preliminary ruling:

„(1) Does [Directive 2006/112] (in particular, Articles 213, 214 and 273) preclude, in circumstances such as those of the main proceedings, national legislation or a tax practice under which a taxpayer does not have the right to deduct VAT claimed in several returns after the reactivation of the taxpayer's VAT identification number, on the basis that the VAT in question relates to purchases made during a period in which the taxpayer's VAT identification number was inoperative?

(2) Does [Directive 2006/112] (in particular, Articles 213, 214 and 273) preclude, in circumstances such as those of the main proceedings, national legislation or a tax practice under which a taxpayer does not have the right to deduct VAT claimed in several returns after the reactivation of the taxpayer's VAT identification number, on the basis that, although the VAT in question relates to invoices issued after the reactivation of the taxpayer's VAT identification number, it concerns purchases made during a period in which the VAT identification number was inoperative?"

Judgement of the Court:

„Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax, as amended by Council Directive 2010/45/EU of 13 July 2010, in particular Articles 213, 214 and 273 thereof, must be interpreted as precluding national legislation, such as that at issue in the main proceedings, under which it is permissible for the tax authorities to refuse,on account of a failure to submit tax returns, a taxable person which has made acquisitions in the period during which its value added tax identification number was revoked the right to deduct value added tax on those acquisitions using value added tax returns filed — or invoices issued — after the reactivation of its identification number, on the sole ground that those acquisitions took place in the period during which its value added tax identification number was de-activated and where the substantive requirements have been satisfied and the right of deduction is not being invoked fraudulently or abusively."

In this case, the CJEU decided to reject the tax administration's decision to refuse the right of deduction in the case of a taxable person who was in the situation of VAT code being cancelled simply because the deduction was related to acquisitions made by the taxpayer during the period in which VAT code was inactive, in the context in wich the substantive requirements were met and the right to deduct was not fraudulently or abusively invoked. We consider that in this case it should be pointed out that the taxable person exercised his right of deduction for purchases during the inactivity of the VAT code only after he had been re-registered for VAT purposes in accordance with the legal provisions in force.

2.3. C159/17- Dobre

Description of the dispute:

The Individual Enterprise Dobre M. Marius was registered for VAT purposes in Romania from July 13, 2011 to July 31, 2012. Since it did not submit any tax return for two consecutive calendar quarters (namely, the last quarter of 2011 and the first quarter of 2012), tax administration canceled its VAT registration as of 1 August 2012. After the VAT code was canceled, the individual company continued to collect the tax by issuing invoices containing VAT, but he did not submitted the tax returns required. Following a tax audit in the 2015, tax administration issued a tax decision ordering the company to pay the VAT it had collected in the period in which the registration for VAT purposes was canceled. As a result, the company also claimed a VAT deduction for the goods and services purchased for the provision of services to legal persons corresponding to its object of activity during the period in which it was not registered for VAT purposes, right of deduction refused by the tax adminstrartion.

Questions to the Court for a preliminary ruling:

„Must Articles 167, 168, 169 and 179, Article 213(1), Article 214(1)(a) and Article 273 of Directive [2006/112] be interpreted as precluding national legislation which, in circumstances such as those of the main proceedings, requires a taxpayer, whose identification for VAT purposes has been revoked, to pay to the State the VAT collected during the period in which the VAT reference number was revoked, without, however, recognising his right to deduct the VAT relating to purchases made during that period?"

Judgement of the Court:

„Articles 167 to 169 and 179, Articles 213(1) and 214(1), and Article 273 of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax must

be interpreted as not precluding national legislation, such as that at issue in the main proceedings, which allows tax authorities to refuse a taxable person the right to deduct value added tax when it is established that, on account of the alleged infringements committed by that person, the tax authorities could not have access to the information necessary to establish that the substantive requirements giving rise to the right to deduct input value added tax paid by that taxable person have been satisfied or that that person acted fraudulently in order to enjoy that right, a matter which it is for the referring court to ascertain."

Following this decision of the CJEU, we note that in a situation quite similar to that of Gamesa, the Court allowed the national tax administration to refuse the right to deduct VAT in the case of a taxable person for purchases made during the period in which it had the VAT code revoked, the particulars of the case which led to this decision being that the failure of taxpayer to comply with formal requirements led to the impossibility of the tax authorities to determine whether the substantive requirements of the right to deduct are met. European Union law therefore does not prevent Member States from considering that such failure of a taxpayer to comply with tax obligations is evidence of fraudulent behavior and refusing to grant the right to deduct.

3. Conclusions

After examining these cases and the CJEU's decisions, we conclude that the determining factor in granting the right to deduct VAT is that substantive requirements are met and that the right to deduct is not fraudulently or abusively invoked by the taxpayer. The cancellation of the VAT code can not be a self-evident reason that may lead to the refusal to deduct the tax, just as re-registration for VAT purposes should not be a vital condition for the exercise of this right. However, as regards formal requirements, even if their non-fulfillment does not prevent the fact that the substantive requirements are met, such taxpayer's behavior in relation to tax obligations may lead to the possibility of proving an intention of tax fraud, in which case the right to deduct the tax is automatically canceled.

Refernces

[1] Legea nr. 207/2015 privind Codul de procedură fiscală, publicată în Monitorul Oficial nr. 547/23.07.2015, cu modificările și completările ulterioare.

[2] Legea nr. 227/2015 privind Codul fiscal, publicată în Monitorul Oficial nr. 688/10.09.2015, cu modificările și completările ulterioare.

[3] Cauza C-101/16 – SC Paper Consult SRL împotriva Direcției Regionale a Finanțelor Publice Cluj-Napoca și a Administrației Județene a Finanțelor Publice Bistrița-Năsăud.

[4] Cauza C-69/17- Siemens Gamesa Renewable Energy România SRL, fostă Gamesa Wind România SRL împotriva Agenției Naționale de Administrare Fiscală – Direcția Generală de Soluționare a Contestațiilor, Agenției Naționale de Administrare Fiscală – Direcția Generală de Administrare a Marilor Contribuabili.

[5] Cauza C-159/17 - Întreprinderea Individuală Dobre M. Marius împotriva Ministerului Finanțelor Publice – A.N.A.F. – D.G.R.F.P. Galați – Serviciul Soluționare Contestații, A.N.A.F – D.G.R.F.P. Galați – A.J.F.P. Constanța – Serviciul Inspecție Fiscală Persoane Fizice 2 Constanța.

[6] Directiva 2006/112/CE a Consiliului din 28 noiembrie 2006 privind sistemul comun al taxei pe valoarea adăugată, publicată în Jurnalul Oficial L 347/11.12.2006, cu modificările și completările ulterioare.