Case C-528/19

Summary of the request for a preliminary ruling pursuant to Article 98(1) of the Rules of Procedure of the Court of Justice

Date lodged:

10 July 2019

Referring court:

Bundesfinanzhof (Federal Finance Court, Germany)

Date of the decision to refer:

13 March 2019

Applicant, and Appellant in the appeal on a point of law:

F-AG

Defendant, and Respondent in the appeal on a point of law:

Tax Office Y

Subject-matter of the main proceedings

Turnover tax treatment of an upgrading of a public municipal road, right to deduction of input tax, supply of goods for consideration

Subject matter and legal basis of the reference

Interpretation of EU law, Article 267 TFEU

Questions referred

1. In circumstances such as those of the main proceedings, in which a taxable person carries out construction works on a municipal road on behalf of a city, is that taxable person, which has procured from other taxable persons services relating to the construction of the road that has been transferred to the municipality, entitled to deduct input tax in respect thereof pursuant to Article 17(2)(a) of the Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes?

2. If the answer to Question 1 is in the affirmative: In circumstances such as those of the main proceedings, in which a taxable person carries out construction works on a municipal road on behalf of a city, does a supply of goods for consideration exist when the authorisation to operate a quarry is the consideration for the supply of a road?

3. If the answer to question 2 is in the negative: In circumstances such as those of the main proceedings, in which a taxable person carries out construction works on a municipal road on behalf of a city, is the free-of-charge transfer of the public road to the municipality treated, in accordance with Article 5(6) of Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes, as a supply of goods free of charge even though the transfer serves commercial purposes, in order to prevent an untaxed final consumption by the municipality?

Provisions of EU law cited

Sixth Council Directive of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of tax assessment, in particular Article 17(2)(a) and Article 5(6)

Provisions of national law cited

Umsatzsteuergesetz (Law on Turnover Tax, hereinafter the 'UStG'), specifically Paragraphs 1, 3 and 15

Brief summary of the facts and procedure

1 The applicant and appellant in the appeal on a point of law ('the applicant'), a public limited company, is a managing holding company. Its subsidiaries include A-GmbH. A tax group arrangement for turnover tax purposes existed between the applicant and A-GmbH.

2 In the year in dispute (2006), A-GmbH operated inter alia a limestone quarry in X. By way of a notice of approval of 16 February 2001, the Regional Council of Z approved the new excavation and operation of the quarry, subject to the condition that the quarry be developed via a public municipal road owned by the city of X (hereinafter the 'City'):

3 The upgrading of the municipal road in question was necessary for the purposes of carrying away the limestone extracted. The legal predecessor of A-GmbH had therefore already entered into an agreement relating to the upgrading of the road with the City on 11 December 1997 during the authorisation procedure. In that agreement, the City undertook to plan and implement the upgrading of the relevant section of road. In addition, the City undertook, if the upgraded section of

road continued to be dedicated to the public, to make it available to the legal predecessor of A-GmbH without restriction for the purposes of the development and in the event of any expansions of the quarry. The legal predecessor of A-GmbH undertook to bear all of the costs associated with the upgrading of the section of road. The agreement was also to apply to all legal successors of the parties to the agreement. In an amending notice of 25 April 2005 pertaining to the authorisation notice of 16 February 2001, it was specified that the authorisation would expire if the upgrading of the road in question was not completed by 31 December 2006.

4 In 2006, A-GmbH commissioned its sister company B-GmbH, which is also a company controlled by the applicant, to upgrade the relevant section of road in accordance with the agreement with the City. The upgrade was completed in November 2006 and the construction works were accepted in December 2006. From December 2006 onwards, the section of road was used by the heavy goods traffic of A-GmbH and, to a limited extent, by passenger vehicles.

5 While the applicant did not account for A-GmbH's expenditure on the construction works in the tax declarations for turnover tax in 2006, it deducted the turnover tax amounts included in the inputs of B-GmbH as input tax in the 2006 turnover tax declaration.

6 On the basis of an external audit, the defendant and respondent in the appeal on a point of law ('the Tax Office') took the view that, in upgrading the road, the applicant had provided the City with a free-of-charge supply of services that was liable to turnover tax pursuant to number 3 of the first sentence of Paragraph 3(1b) of the UStG. No taxable intercompany transactions existed between A-GmbH and B-GmbH since both belonged to the applicant's tax group arrangement.

7 On 1 March 2012, the Tax Office issued an amended turnover tax notice for 2006.

8 The applicant's complaint was unsuccessful.

9 The Finance Court of Hesse ('the FC') upheld in part the action brought by the applicant.

10 In support of its appeal on a point of law which was lodged with the referring court, the applicant contends that, on an interpretation of Paragraph 15(1) of the UStG in conformity with EU law, the deduction of input tax should be permitted because the expenditure on the upgrading of the road formed part of the general expenditure of its business and, as such, constituted components of the price of its output transactions that were liable to turnover tax. Nor was there any disposal free of charge within the meaning of number 3 of the first sentence of Paragraph 3(1b) of the UStG.

Brief summary of the basis for the reference

11 It is doubtful whether the assessment based on national law is compatible with EU law in a number of respects for the purposes of Article 267(3) TFEU.

Assessment on the basis of national law

12 On the basis of the Federal Finance Court's case-law to date, the deduction of input tax is ruled out because the applicant has procured the inputs procured from B-GmbH for the purposes of carrying out a free-of-charge supply to the City.

13 A trader is entitled to deduct input tax when it procures inputs for the purposes of its business and thus for its economic activity. Under number 1 of the first sentence of Paragraph 15(1) of the UStG, a trader may deduct as input tax the tax statutorily owed in respect of supplies effected by another trader for the purposes of its business. Under number 1 of the first sentence of Paragraph 15(2) of the UStG, it is not possible to deduct input tax in respect of supplies which a trader uses for exempt transactions.

14 According to settled case-law of the Court of Justice and of the Federal Finance Court, the existence of a direct and immediate link between a particular input transaction and a particular output transaction or transactions giving rise to entitlement to deduct is, in principle, necessary before the taxable person is entitled to deduct input tax and in order to determine the extent of such entitlement (see, for example, judgments of the Court of Justice of 29 October 2009, *SKF*, C-29/08, EU:C:2009:665, paragraph 57, of 18 July 2013, *AES-3C Maritza East 1*, C-124/12, EU:C:2013:488, paragraph 27, of 22 October 2015, *Sveda*, C-126/14, EU:C:2015:712, paragraph 27; of 14 September 2017, *Iberdrola Inmobiliaria Real Estate Investments*, C-132/16, EU:C:2017:683, paragraph 28).

15 However, a taxable person also has a right to deduct even where there is no direct and immediate link between a particular input transaction and an output transaction or transactions giving rise to the right to deduct where the costs of the services in question are part of his general costs and are components of the price of the goods or services which he supplies. Such costs do have a direct and immediate link with the taxable person's economic activity as a whole (settled case-law, see in that regard, for example, judgments *SKF*, EU:C:2009:665, paragraph 58, and the case-law cited therein; *AES-3C Maritza East 1*, EU:C:2013:488, paragraph 28; *Iberdrola Inmobiliaria Real Estate Investments*, EU:C:2017:683, paragraph 29, of 17 October 2018, *Ryanair*, C-249/17, EU:C:2018:834, paragraph 27).

16 A trader is therefore entitled to deduct input tax if he intends to use services for the purposes of his business (Paragraph 2(1) of the UStG, Article 4 of Directive 77/388/EEC) and thus for his economic activities for the purpose of the provision of services for consideration (economic activities) (judgment of 13 March 2008, *Securenta*, C-437/06, EU:C:2008:166, headnote 1). However, no entitlement to

deduct input tax exists where the trader, when procuring services, intends to use them for a free-of-charge transaction and thus for a non-economic activity which does not fall within the scope of application of value added tax (cf. judgments of 12 February 2009, C-515/07, *Vereniging Noordelijke Land- en Tuinbouw Organisatie*, EU:C:2009:88, paragraph 34; of 13 March 2014, *Malburg*, C-204/13, EU:C:2014:147, paragraphs 36 and 37).

17 On the basis of these principles, the inputs in dispute of B-GmbH, which are to be imputed to the applicant in the context of the tax group arrangement, do not give rise to an entitlement to deduct input tax because the inputs were procured with the intention that they would be used for a non-economic activity (supply free of charge to the City).

18 The construction works on the road constitute disposals of goods. When — as in the case in dispute — a trader establishes development facilities on third-party land in return for consideration on the basis of a development agreement entered into with a city, it provides a supply of services to the municipality (supply of development facilities) within the meaning of Paragraph 3(4) of the UStG.

19 The disposals were also — on the basis of the view taken to date by the Federal Finance Court — undertaken free of charge. The development agreement entered into between the legal predecessor of A-GmbH and the City did not provide that the municipality was under any obligation to pay an amount of consideration. There is insufficient evidence to suggest that the Regional Council's authorisation notice constitutes consideration for the upgrading of the road by the applicant. The intentional transfer of goods in the nature of a benefit that is required by number 3 of the first sentence of Paragraph 3(1b) of the UStG arises from the fact that the intention was for the City to acquire legal ownership of construction works relating to the municipal road without consideration. There is no evidence to suggest that the applicant, at least economically, wished to retain ownership of the municipal road, or even merely rights of use over it, which would preclude the assumption of a subsequent disposal of such a nature.

20 Under national law, the applicant would therefore have no right to the deduction of input tax.

Assessment on the basis of EU law

The first question referred

21 On the basis of the decisions of the Court of Justice in the *Sveda* (EU:C:2015:712) and *Iberdrola Inmobiliaria Real Estate Investments* (EU:C:2017:683) cases and in the Opinion of Advocate General Kokott of 6 April 2017 that was given in relation to the *Iberdrola Inmobiliaria Real Estate Investments* case, C-132/16 (EU:C:2017:283), there are doubts as to whether the previous assessment under national law is valid. On the contrary, it could be conceivable that the applicant would be able to deduct input tax for the inputs.

22 In these decisions, the Court of Justice found that a right to deduct input tax did exist in respect of the creation of a public road and a pumping station because the costs of the services procured were part of the general costs of the taxable person and are, as such, components of the price of the goods or services which he supplied. It either did not examine any link with the free-of-charge service within the meaning of Article 26 of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (Directive 2006/112/EC — in the year in dispute still Article 6(2) of Directive 77/388/EEC) (*Iberdrola Inmobiliaria Real Estate Investments* judgment, EU:C:2017:683, paragraph 23), or it held that the immediate use free of charge does not affect the existence of the direct and immediate link between the input transactions and the output transactions which give rise to the right to deduct input tax or with the taxable person's economic activities as a whole (*Sveda* judgment, EU:C:2015:712, paragraph 34). The free-of-charge use therefore does not appear to preclude the right to deduct input tax even though, in the view of the referring Chamber, that constitutes a non-economic activity.

The second question referred

23 Furthermore, assuming that the applicant does have a right to deduct input tax, the question arises for the referring Chamber as to whether the entitlement to deduct input tax should be offset against a turnover tax receivable arising from a supply for consideration or from a free-of-charge disposal within the meaning of Article 5(6) of Directive 77/388/EEC (now Article 16 of Directive 2006/112/EC). That must be assessed on the basis of national procedural law in the context of the case in dispute.

24 It is not completely beyond doubt under EU law whether the applicant supplied the road to the City in return for consideration.

25 A supply of goods or services 'for consideration' requires the existence of a direct link between the supply of goods or services and consideration actually received by the taxable person. Such a direct link is established if there is a legal relationship between the provider of the service and the recipient pursuant to which there is reciprocal performance, the remuneration received by the provider of the service constituting the value actually given in return for the service supplied to the recipient (see, to that effect, judgments of 26 September 2013, *Serebryannay vek*, C-283/12, EU:C:2013:599, paragraph 37, and of 22 November 2018, *Meo — Serviços de Comunicações e Multimedia*, C-295/17, EU:C:2018:942, paragraph 39). The consideration for a supply of services may also consist of a supply of goods, provided, however, that there is a direct link between the supply of services and the supply of goods and that the value of the latter can be expressed in monetary terms (see judgment of 10 January 2019, *A*, C-410/17, EU:C:2019:12, paragraphs 35 and 36).

26 The Chamber is inclined, in accordance with the prevailing national view in that regard, to proceed on the basis that the road was the subject of a free-of-charge

supply to the City. There is a supply of goods and not of services here because the applicant has granted the City a power of disposal over the road.

27 However, in circumstances such as those of the main proceedings, which are very similar to those of the *Iberdrola Inmobiliaria Real Estate Investments* case, the existence of a free-of-charge supply is not beyond doubt under EU law since Advocate General Kokott, in point 50 of her Opinion in *Iberdrola Inmobiliaria Real Estate Investments* (EU:C:2017:283), took the view that an undertaking rarely gives an external third party something unless it expects a corresponding advantage from that third party. If that were the case, in the case in dispute that advantage would be the authorisation for the new excavation and operation of the quarry, which the Regional Council granted only on the condition that the (legal predecessor of the) applicant upgraded the road in question. The authorisation for the mining of limestone would have expired if the upgrading of the municipal road had not been completed by 31 December 2006. Considered from that point of view, according to Advocate General Kokott, there would be a supply for consideration, which does give entitlement to deduct input tax, but also gives rise to tax liability in the same amount in respect of the renovation carried out for consideration.

The third question referred

28 If, on the other hand, it is assumed — as the referring Chamber has done to date — that that was a free-of-charge supply, then it is still doubtful whether that free-of-charge supply of goods is taxable pursuant to Article 5(6) of Directive 77/388/EEC (now Article 16 of Directive 2006/112/EC).

29 The referring Chamber has so far assumed that that is the case. According to the case-law of the Court of Justice, the fact that the supply is made for business purposes does not preclude taxation under Article 5(6) of Directive 77/388/EEC, since it is clear from the very wording of that provision that Directive 77/388/EEC regards the application by a taxable person of goods forming part of his business assets which are passed on by the latter free of charge as supply made for consideration where input tax was deductible on those goods, it being in principle immaterial whether that application was for business purposes (cf. judgment of 27 April 1999, *Kuwait Petroleum*, C-48/97, EU:C:1999:203, paragraph 22). Even if applications are effected for the purposes of the business, they must be regarded as taxable supplies unless they relate to samples (judgment of 30 September 2010, *EMI Group*, C-581/08, EU:C:2010:559, paragraphs 18, 23) or gifts of small value (cf. *Kuwait Petroleum* judgment, EU:C:1999:203, paragraph 23). It is clear that neither exception applies in the present case.

30 However, that argument could be precluded by the fact that the municipal road is used by the City not for ‘private’ purposes but rather (on account of the road’s dedication) for public road traffic (cf., in a different context, Opinion of Advocate General Kokott in the *Iberdrola Inmobiliaria Real Estate Investments* case,

EU:C:2017:283, point 51; *Vereniging Noordelijke Land- en Tuinbouw Organisatie* judgment, EU:C:2009:88, paragraph 35 et seq.).

31 In addition, the liability for tax under Article 5(6) of Directive 77/388/EC is questionable for the further reason that a judgment to the contrary has been delivered by a national court within the European Union. In a case that was comparable in that regard, the Austrian Verwaltungsgerichtshof (Supreme Administrative Court) found that no taxable private consumption involving extra expense existed because the expenditure concerned was expenditure for business purposes which, as auxiliary transactions or ancillary transactions, belonged to the services within the scope of the business.

32 That potentially fundamentally different approach adopted by another court of a Member State means that the Chamber is obliged, pursuant to Article 267(3) TFEU, to refer the question of law to the Court of Justice (cf. judgment of 5 July 2018, *Marcandi*, C-544/16, EU:C:2018:540, paragraph 64; cf. also judgment of 15. September 2005, *Intermodal Transports*, C-495/03, EU:C:2005:552, paragraph 39).

33 Moreover, the taxation of the free-of-charge disposal is questionable for the further reason that it impinges on the principle of the neutrality of value added tax. The applicant is being charged turnover tax on general costs of the business. The justification which is cited for the rule in Article 5(6) of Directive 77/388/EEC (now Article 16 of Directive 2006/112/EC), of preventing an ‘untaxed final consumption’ (cf., for example, judgments *EMI Group*, EU:C:2010:559, paragraph 17, in relation to Article 5(6) of Directive 77/388/EEC; of 17 July 2014, *BCR Leasing IFN*, C-438/13, EU:C:2014:2093, paragraph 23, in relation to Article 16 of Directive 2006/112/EC), is not relevant to cases such as the case in dispute because the costs in dispute have been incorporated in the calculation of the prices of the regular output transactions.