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Judgments of the Court of Justice in Cases C-255/02, C-419/02 and C-223/03

Halifax PLC and Others, BUPA Hospitals Ltd and Others, and University of Huddersfield v Commissioners of Customs & Excise

THE SIXTH VAT DIRECTIVE DOES NOT GRANT A TAXABLE PERSON ANY RIGHT TO DEDUCT INPUT VAT WHERE THE TRANSACTIONS FROM WHICH THAT RIGHT DERIVES CONSTITUTE AN ABUSIVE PRACTICE

In addition, where payments are made on account, in order for VAT to become chargeable without the supply having taken place, it is necessary, in particular, for the goods or services to have been precisely identified.

In these three cases, English courts submitted questions on the interpretation of the Sixth VAT Directive[1], which establishes a common system of VAT, in connection with proceedings concerning schemes drawn up by certain economic operators in order to reduce their VAT liability.

Halifax (Case C-255/02), a banking establishment, and the University of Huddersfield (Case C-223/03), a university, wished to carry out construction works. Since most of their services were exempt from VAT, they would have been able to recover only a small proportion of VAT. However, both Halifax and the University of Huddersfield prepared schemes enabling them, through a series of transactions involving different companies or organisations, to recover in practice all the input VAT paid in respect of the construction works.

In the BUPA case (Case C-419/02), a United Kingdom company which manages a large number of private hospitals concluded contracts with other companies in the same group for the future supply of drugs and prostheses. In order to benefit from a much more favourable VAT system,

[1] Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment (OJ 1977 L 145, p. 1).

they arranged for the payments under those contracts to be made before delivery of the goods and before the entry into force of legislation amending that system.

BUPA, Halifax and the University of Huddersfield applied for repayment of or relief from input VAT on their transactions. The applications were rejected by the Commissioners of Customs & Excise. The latter concluded that a transaction, of whatever nature, carried out with the sole aim of avoiding VAT, is not in itself either a 'supply of goods' or a 'supply of services', nor a measure adopted in the context of an 'economic activity' for VAT purposes.

The applicants challenged the Commissioners' refusal before the English courts, which have asked the Court of Justice of the European Communities to interpret certain provisions of the Sixth VAT Directive. The English courts seek to ascertain whether transactions of the kind at issue constitute supplies of goods or services and an economic activity within the meaning of the Sixth Directive where they are carried out for the sole purpose of obtaining a tax advantage, without any other economic aim. They also wish to know whether the Sixth VAT Directive withholds from taxable persons the right to deduct input VAT where the transactions on which that right is based constitute an abusive practice and, finally, under what circumstances VAT may be recovered where an abusive practice has been found to exist.

In the **Halifax** and **University of Huddersfield** judgments, the Court of Justice pointed out that the system established by the Sixth VAT Directive is based, in particular, on a uniform definition of taxable transactions. An analysis of the terms 'supply of goods' and 'supply of services', and of 'taxable person' and 'economic activity', shows that those terms, which define taxable transactions under the Sixth VAT Directive, are all objective in character and apply regardless of the aims and results of the transactions concerned. The question whether the transaction concerned is carried out for the sole purpose of obtaining a tax advantage is therefore irrelevant in determining whether it constitutes a supply of goods or services and an economic activity. It follows that **transactions of the kind at issue in this case constitute supplies of goods or services and an economic activity** within the meaning of the Sixth VAT Directive, **provided that they satisfy the objective criteria on which those concepts are based, even where they are carried out with the sole aim of obtaining a tax advantage, without any other economic objective**.

Next, the Court emphasised that no-one is entitled to exploit Community provisions fraudulently or abusively. **That principle of the prohibition of abusive practices extends to the sphere of VAT**. The Court observed that the Sixth VAT Directive precludes any entitlement on the part of a taxable person to deduct input VAT where the transactions on which that right is based constitute an abusive practice. For the existence of such a practice to be established, it is necessary, first, for the transactions in question, notwithstanding formal application of the conditions laid down by the relevant provisions of the Sixth VAT Directive and the national legislation transposing that directive, to result in the accrual of a tax advantage the granting of which would be contrary to the purpose of those provisions. Second, it must also be apparent from a number of objective factors that the essential aim of the transactions in question is to obtain a tax advantage.

Finally, the Court held that, since no provision of the Sixth VAT Directive concerns the recovery of VAT, it is in principle for the Member States to determine the conditions under which VAT

may be recovered after the event by the revenue authorities, provided that they remain within the limits imposed by Community law. **Recalling in particular that measures adopted by Member States may not be used in such a way as to call in question the neutrality of VAT, the Court held that, where an abusive practice has been found to exist, the transactions concerned must be redefined so as to re-establish the situation that would have prevailed in the absence of the transactions constituting that abusive practice**.

In the **BUPA** judgment, the Court referred to the rule whereby VAT becomes chargeable when the goods are delivered or the services are performed. The possibility, in the case of payments on account before the delivery of goods or a supply of services, that VAT might become chargeable on receipt of the payment and on the amount received, constitutes a derogation from the rule and must be interpreted strictly. **For that derogation to be available, it is necessary for all the information concerning the future supply of goods or services to be known already and therefore, in particular, it is necessary for the goods or services to be precisely identified at the time when the payment on account is made**. Consequently, the Court held that prepayments of the kind at issue in the main proceedings whereby lump sums are paid for goods indicated in general terms in a list which may be altered at any time by agreement between the buyer and the seller and from which the buyer may possibly select articles, on the basis of an agreement which he may unilaterally rescind at any time, thereupon recovering the unused balance of the prepayments, do not fall within the scope of that derogation.

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