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The Economic Objective of a Contract as a Criterion for the Assessment of Taxation of a Transaction with Value Added Tax

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The article attempts to examine the impact of the intentions of the parties to a business transaction on the fiscal circumstances within the framework of value added tax. Analysis of the Court's case law allows one to conclude that the economic objective of a contract between the parties to a transaction may be of considerable importance for the determination of the tax effects in VAT. This is because the economic and commercial reality is a fundamental criterion for the operation of the common VAT system, and it should be taken into account. In this respect, significant contractual terms may be important. In addition to the stipulations of the contract between the parties, objective interests of the parties, such as pricing and invoicing, may also be relevant. It is also possible to refer to the economic purpose of supply and the conventional rules and standards applicable in a given field as well as the economic practice.

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Introduction

The article attempts to examine the impact of the intentions of the parties to a business transaction on the fiscal circumstances within the framework of value added tax.

The shaping of fiscal circumstances through civil law acts is limited for the purpose of prevention of tax avoidance, abuse, and tax fraud. Within the framework of value added tax, this restriction is also concerned with a very important principle that shapes the structural elements of this tax – the principle of neutrality. According to the Court of Justice of the EU (hereinafter: The Court or the CJEU), the principle of tax neutrality "precludes economic operators carrying out the same transactions being treated differently in relation to the levying of VAT". Within the framework of value added tax, it is forbidden to exercise different treatment of goods and services which are competitive due to similarity between them.[1] On the

[1] See judgments of the CJEU: of 7 March 2013 in Case C424/11 Wheels Common Investment Fund Trustees and others, ECLI:EU:C:2013:144, paragraphs 20, 21; in Case C363/05 JP Morgan Fleming Cloverhouse Investment Trust and the Association of Investment Trust Com-

other hand, it is not possible to ignore the fact that value added tax is tax on economic events (Bartosiewicz, 2013, pp. 276–277).

The Court points out that value added tax has an economic character as the CJEU has frequently stressed that the VAT Directive establishes a common VAT system based, in particular, on a uniform definition of taxable transactions.[2] The idea of the economic character of VAT was first raised by the Court when it was examining the importance of the definition of the supply of goods. In accordance with Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ L of 2006, No. 347/1 as amended; hereinafter Directive 112; earlier, the Sixth Directive), supply of goods is understood as "transfer of the right to dispose of tangible property as owner". Therefore, the provision does not refer to the concept of transfer of ownership, which is known under national civil law systems. The Court concluded that supply of goods within the meaning of the Directive is not limited to transfer of ownership such as under the civil law. The economic right to use an item as the owner is of major importance, provided that it gives the buyer analogous rights in practice as transfer of ownership.[3] The Court has also repeatedly stressed later that the term "supply of goods" provided for in Article 5(1) of the Sixth Directive and in Article 14(1) of Directive 112 does not refer to transfer of ownership as stipulated in the relevant national legislation but covers any transfer of tangible property by a party that authorises the other party to dispose of them as the owner.[4]

The Court has already concluded that the concept of supply "is objective in nature and that it applies without regard to the purpose or results of the transactions concerned and without its being necessary for the tax authorities to carry out inquiries to determine the intention of the taxable person in question or for them to take account of the intention of a trader other than that taxable person involved in the same chain of supply".[5] However, the above Court's view does not preclude the relevance of objective evaluation of an operation made by the parties, which takes into consideration the economic sense of that operation, for the assessment of its tax consequences. Because the Court has consistently held that when classifying a transaction as a 'taxable transaction' within the meaning of the VAT Directive 112,[6] the economic and commercial reality is a fundamental criterion for the operation of the common VAT system, which should be taken into account.[7]

panies, ECLI:EU:C:2007:391, paragraph 46; of 23 October 2003 in Case C:109/02 Commission v Germany; ECLI:EU:C:2003:586, paragraph 20; of 16 September 2004 in Case C382/02 Cimber Air, ECLI:EU:C:2004:534, paragraph 24; of 17 February 2005 in joined cases C453/02 and C462/02 Linneweber and Akritidis, ECLI:EU:C:2005:92, paragraph 24; of 8 June 2006 in Case C106/05 L.u.P., ECLI:EU:C:2006:32:380, paragraph 32.

[2] Judgment of the Court of Justice of the EU of 12 January 2006 in joined cases C-354/03, C-355/03 and C-484/03 Optigen and others, ECLI:EU:C:2006:16, paragraph 36; of 21 February 2006 in Case C-255/02 Halifax and others, ECLI:EU:C:2006:121, paragraph 48; and in Case C-653/11 Paul Newey, paragraph 39.

[3] Judgment of the Court of 8 February 1998, in Case C-320/88 Shipping and Forwarding Enterprise Safe, ECLI:EU:C:1990:61.

[4] Judgment of 14 July 2005 in Case C-435/03 British American Tobacco and Newman Shipping, ECLI:EU:C:2005:464, paragraph 35; the above mentioned judgments in joined cases C-354/03, C-355/03 and C-484/03 Optigen and others, paragraph 39; in Case C-255/02 Halifax and others, paragraph 51; judgments: of 3 June 2010 in Case C-237/09 de Fruytier, ECLI:EU:C:2010:316, paragraph 24; of 18 July 2013 in Case C-78/12 Evita-K, ECLI:EU:C:2013:486, paragraph 33; of 21 November 2013 in Case C-494/12 Dixons Retail, ECLI:EU:C:2013:758, paragraph 20.

[5] Judgments: in joined cases C-354/03, C-355/03 and C-484/03 Optigen and others, paragraphs 44-46, and paragraphs 51, 55; in Case C-255/02 Halifax and others, paragraphs 56, 57; judgment of 6 July 2006 in joined cases C-439/04 and 440/04 Kittel and Recolta Rececling, ECLI:EU:C:2006:446, paragraphs 41-44; as well as the above-mentioned judgment in Case C-653/11 Paul Newey, paragraph 41; of 21 November 2013 in Case C-494/12 Dixons Retail, paragraph 21.

[6] Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ EU L 347, hereinafter Directive 112).

[7] Judgment of the CJEU in Case C-653/11 Paul Newey, paragraph 42 and the case law cited therein; judgment of

Important contractual conditions and the economic and commercial reality

Citing economic and commercial reality as the rationale behind classifying a transaction for the purposes of taxation with value added tax requires clarification of what these terms mean precisely. In particular, the question is whether this should also include significant contractual terms. Significant contractual terms are a factor to be taken into account when the contractual situation reflects the actual economic and commercial events within the framework of a transaction – and in order to meet the requirements of legal certainty.[8] In this respect, the Court has established that the significant contractual terms should not be taken into account when they do not fully reflect the actual economic and commercial events within the framework of a transaction. This would be the case, in particular, if it turned out that the contractual terms in question are an entirely artificial structure that do not adequately reflect the actual economic and commercial events within the framework of a transaction.[9] This is because in a number of cases the Court has found that countering possible tax fraud, tax evasion, or abuse is an objective recognised and supported by the Sixth Directive[10] and that the principle of prohibition of abuse of the law forbids devising completely artificial structures deviating from the actual economic events, which have been created solely for the purpose of obtaining tax advantages.[11] Hence it is not possible to extend the scope of the EU regulations to cover abuse committed by economic entities, that is, transactions that are not carried out as ordinary commercial transactions but solely for the purpose of abusing the advantages provided for in the EU law, and that this principle of prohibition of abusive practices also applies to VAT.[12] The national court is responsible for such an assessment.[13] The national court should examine the terms and conditions of a contract in order to check, in particular, whether they are contrary to the provisions of the Directive or the national legislation transposing the Directive. This would be the case especially if the amount of lease payments were to be determined and it turned out to be grossly low and not pertaining to the economic reality in any way.[14]

The examination of the stipulations of a contract as an element of the economic and commercial reality is an important aspect to be taken into account, among other things, to determine the scope of the right of deduction.[15]

As it will be indicated below, the Court does not always refer explicitly to significant contractual terms. In particular, the Court has referred to the interests of the parties to a contract, such as the manner of pricing and invoicing.[16] The Court has also referred to the economic purpose of supply[17] and the standards applicable in a given field[18] and economic practice.[19]

22 November 2018, C295/17 MEO — Serviços de Comunicações e Multimédia, EU:C:2018:942, paragraph 43.

[8] Judgment of the CJEU in Case C653/11 Paul Newey, paragraph 43.

[9] Judgment of the CJEU in Case C653/11 Paul Newey, paragraphs 44 and 45.

[10] Judgment of the CJEU in Case C255/02, Halifax and others, paragraph 71, and the case law cited therein.

[11] Judgments of the CJEU: of 22 May 2008 in Case C162/07 Ampliscientifica et Amplifin, ECLI:EU:C:2008:301, paragraph 28; of 27 October 2011in Case C504/10 Tanoarch, ECLI:EU:C:2011:707, paragraph 51; of 12 July 2012 in Case C326/11 J.J. Komen en Zonen Beheer Heerhugowaard, EU:C:2012:461, paragraph 35.

[12] Judgment of the CJEU of 22 December 2010, C-103/09 Weald leasing Ltd, ECLI:EU:C:2010:804, paragraph 26 and the case law cited therein.

[13] Judgment of the CJEU of 20 June 2013 in Case C653/11 Paul Newey, paragraph 52.

[14] Judgment of the CJEU of 22 December 2010 in Case C-103/09 Weald Leasing Ltd, paragraph 39.

[15] Judgment of the CJEU of 1 October 2020 in Case C-405/09 Vos Aannemingen, ECLI:EU:C:2020:785, paragraphs 40 and 42.

[16] Judgment of the CJEU of 17 January 2013 in Case C-224/11 BGŻ Leasing, EU:C:2013:15, paragraphs 44 and 45.

[17] For example, judgment of the CJEU of 19 November 2009 in Case C-461/08 Don Bosco Onroerend Goed, EU:C:2009:722, paragraph 39.

[18] Judgment of the CJEU of 2 May 2019 in Case C-224/18 Budimex, ECLI:EU:C:2019:347, paragraph 35.

[19] Judgment of the CJEU of 18 June 2020 in Case C-276/18 KrakVet Marek Batko, ECLI:EU:C:2020:485, paragraph 69.

The conditions for taking into account contractual terms when determining the supplier and the recipient in a 'supply of services' transaction within the meaning of the VAT Directive

In the Newey case,[20] the Court considered "whether contractual terms are decisive for the purposes of identifying the supplier and the recipient in a 'supply of services' transaction within the meaning of Articles 2(1) and 6(1) of the Sixth Directive, and, if the answer is in the negative, under what circumstances those terms may be recharacterised". In that judgment, the Court ruled that significant contractual terms may be taken into account when determining the supplier and the recipient in a 'supply of services' transaction within the meaning of the VAT Directive.[21] The Courts' view that the relevant contractual terms are a factor that should be taken into account was limited by the requirement that the contractual situation must reflect the actual economic and commercial events.[22] Consequently, the Court has taken the view that "contractual terms, even though they constitute a factor to be taken into consideration, are not decisive for the purposes of identifying the supplier and the recipient of a 'supply of services' within the meaning of Articles 2(1) and 6(1) of the Sixth Directive. They may in particular be disregarded if it becomes apparent that they do not reflect economic and commercial reality but constitute a wholly artificial arrangement which does not reflect economic reality and was set up with the sole aim of obtaining a tax advantage, which it is for the national court to determine". The Court has left examination of this issue to the national courts.

It follows from the above judgment that the relevant contractual terms are circumstances that should be taken into account when determining who the supplier is and who the recipient is for the purposes of VAT. However, they should be disregarded if they deviate completely from the real economic events.

The significance of contractual terms to determine the character of a transaction for VAT purposes

Significant contractual terms should not always be taken into account, even if a transaction reflects actual economic events. This is because contractual terms cannot freely shape taxpayers' tax liabilities, but such obligations may be determined taking into account the stipulations of the contract. This may be the case especially if it is necessary to examine the character of a transaction in regard of its manner of taxation with VAT, in particular whether it is a supply transaction or a financial service. In the judgment Auto Lease Holland,[23] the Court assessed the facts where the applicant, a leasing company, offered the lessee a fuel management agreement in addition to a vehicle leasing contract. As a result of this agreement, the lessee had the right to refuel and occasionally purchase petroleum products on behalf of and for the account of the applicant. To this end, the lessee received the so-called 'ALH-Pass' and a credit card intended for refuelling from the credit card company D. The card indicated the applicant as client D. The Court, therefore, concluded that in order to answer the question raised, it was necessary to determine within the framework of the main proceedings to whom petrochemical companies transferred the right to dispose of the fuel as the owner – the lessor or the lessee. In the Court's view, the fact that the lessee was entitled to dispose of the fuel as the owner was beyond dispute. They purchased fuel directly at petrol stations and Auto Lease (i.e., the lessor) had no

[20] Judgment of the CJEU in Case C653/11 Paul Newey.

[21] Judgment of the CJEU in Case C653/11 Paul Newey, paragraph 43.

[22] Judgment of the CJEU in Case C653/11 Paul Newey, paragraph 43.

[23] Judgment of the CJEU of 6 February 2003 in Case C185/01 Auto Lease Holland, EU:C:2003:73.

right to decide how and for what purpose the fuel would be used. The Court took into account that under the contract concluded in this case, "the lessee of the leased vehicle himself purchases the fuel from filling stations and has a free choice as to its quality and quantity, as well as when to purchase". As a consequence, the Court decided that "the fuel management agreement between the lessor of the leased vehicle and the lessee of that vehicle is not a contract for the supply of fuel, but rather a contract to finance its purchase".[24]

Hence the Court assessed the agreement between the parties to be financing of fuel rather than fuel supply.

The fact that the stipulations of the agreement between the parties were taken into account was justified by the CJEU with the economic character of value added tax. The Court referred to the Case regarding *Shipping and Forwarding Enterprise Safe*,[25] where it was concluded that supply of goods does not constitute transfer of ownership in accordance with the procedure laid down in the national law but covers any transfer of movable property by a party, which entitles the other party to dispose of the property as the owner. In the opinion of the CJEU, the objective of the Directive could be jeopardised if the reasons for the supply of goods – which is one of the three types of taxable transactions – differed in individual Member States as regards the conditions for transfer of ownership provided for in the civil law.[26]

The importance of the economic objective of a contract for classifying events as composite or distinct services

For the purposes of VAT, each service should normally be considered separate and independent, as indicated in Article 1(2) of the VAT Directive.[27] However, the case law of the Court indicates that under some circumstances, formally separate services that may be effectuated separately and so may separately lead to taxation or exemption should be considered a single transaction, if they are not independent from one another. "There is a single supply where two or more elements or acts supplied by the taxable person to the customer are so closely linked that they form, objectively, a single, indivisible economic supply, which it would be artificial to split." This is also the case where one or more services constitute the main service, while other service(s) constitute(s) one or more ancillary services that are treated in terms of taxation in the same way as the main service.[28] In particular, the service should be considered ancillary to the main service, if using it is not the customer's goal, but serves to make the best use of the main service offered by the service provider.[29]

In order to determine whether services constitute several independent services or a single service, one should seek elements that are specific for a transaction.[30]

Composite insurance services were discussed in, among others, the judgement in Case C-224/11 BGŻ Leasing.[31] In that judgment, the CJEU ruled that "the supply of insurance services for a leased item and the supply of the leasing services themselves must, in principal, be regarded as distinct and independent supplies of services for VAT purposes." The Court also held in that judgment that "where the lessor insures the leased item itself

[24] Judgment of the CJEU in Case C185/01 Auto Lease Holland, paragraph 36.

[25] Judgment of the CJEU in Case C-320/88 Shipping and Forwarding Enterprise safe.

[26] Judgment of the CJEU in Case C185/01 Auto Lease Holland, paragraph 32.

[27] Judgements of the CJEU: of 27 September 2012 in Case 392/11 Field Fisher Waterhouse, EU:C:2012:597, paragraph 14; in Case C224/11 BGŻ Leasing, paragraph 29; of 16 April 2015 in Case C-42/14 Wojskowa Agencja Mieszkaniowa, ECLI:EU:C:2015:229, paragraph 30.

[28] Judgment of the CJEU in Case C224/11 BGŻ Leasing , paragraph 30.

[29] Judgments of the CJEU: in Case C392/11 field Fisher Waterhouse, paragraph 17; in Case C-42/14 Wojskowa Agencja Mieszkaniowa, paragraph 31.

[30] Judgment of the CJEU in Case C224/11 BGŻ Leasing, paragraph 32; in Case C-42/14 Wojskowa Agencja Mieszkaniowa, paragraph 32.

[31] Judgment of the CJEU in Case C224/11 BGŻ Leasing.

and re-invoices the exact cost of the insurance to the lessee, such a transaction constitutes, in circumstances such as those at issue in the main proceedings, an insurance transaction within the meaning of Article 135(1)(a) of the VAT Directive." The Court of Justice stressed that "in order to determine whether the services supplied constitute independent services or a single service it is necessary to examine the characteristic elements of the transaction concerned".[32]

In particular, it follows from the BGŻ leasing judgment that "the elements which reflect the interests of the contracting parties, such as the way in which invoicing and pricing are carried out, may be taken into account to determine the characteristic elements of the transaction concerned." The Court noted that "the lessee wishes, above all, to obtain leasing services and the insurance he is required to take by the lessor is of only secondary importance to him. If the lessee also decides to obtain insurance services through the lessor, such a decision is made independently of his decision to conclude a leasing agreement".[33]

The significance of the economic objective of a transaction and the contractual terms in rental agreements

In the Field Fisher Waterhouse Judgment,[34] the Court answered the question as to "whether the VAT Directive must be interpreted as meaning that, in the circumstances of the main proceedings, the leasing of immovable property and the supplies of services linked to that leasing must be regarded as constituting a single supply, entirely exempt from VAT, or several independent supplies, assessed separately as regards whether they are subject to VAT. The court seeks in particular to know what importance should be attached, in those circumstances, to the fact, first, that the lease provides that the tenant must receive the services supplied by the landlord, even though he could in principle be supplied with at least part of the services by a third party, and, secondly, that the tenant's failure to pay the service charges gives the landlord the right to terminate the lease". The Court ruled that the stipulations of the rental agreement may be important. In this case, the CJEU referred to a rental agreement of business premises by a law firm to indicate that according to the information available to the Court, the agreement stipulated that, in addition to the letting of the premises, the landlord was supposed to provide the tenant with a certain number of services resulting in additional rental fees which could lead to termination of the lease. In the Court's view, "the economic reason for concluding that contract was not only to obtain the right to occupy the premises concerned, but also for the tenant to obtain a number of services". As a consequence, the CJEU "concluded that the lease designated a single supply between the landlord and the tenant. In its analysis, the Court placed itself in the shoes of an average tenant of the commercial premises concerned, that is to say offices for law firms". The Court declared that the provision of additional services to the average tenant of the premises "cannot be regarded as constituting an end in itself for an average tenant of premises such as those at issue in the main proceedings but constitutes rather a means of better enjoying the principal supply, namely the leasing of commercial premises".[35]

In the judgment regarding Wojskowa Agencja Mieszkaniowa in Warsaw,[36] the Court responded to the national court's doubts as to "whether the VAT Directive must be interpreted as meaning that the letting of immovable property and the associated provision of water, electricity, heating, and refuse collection must be regarded as constituting

[32] Judgment of the CJEU in Case C224/11 BGŻ Leasing, paragraph 32.

[33] Judgment of the CJEU in Case C224/11 BGŻ Leasing, paragraphs 44 and 45.

[34] Judgment of the CJEU in Case C392/11 Field Fisher Waterhouse.

[35] Judgment of the CJEU in Case C392/11 Field Fisher Waterhouse, paragraph 23.

[36] Judgment of the CJEU in Case C-42/14 Wojskowa Agencja Mieszkaniowa.

a single supply or several distinct and independent supplies which must be assessed separately from the point of view of VAT". In the judgment regarding Wojskowa Agencja Mieszkaniowa, the CJEU indicated explicitly the necessity to take into consideration the contractual terms when classifying operations. The Court stated the following: "it needs to be assessed, in particular, whether, under the contract, the tenant and the landlord seek, above all, to obtain and let immovable property, respectively, and whether the fact that one party obtains other services provided by the other party is of only secondary importance to them, even if they are necessary for the enjoyment of the property".[37]

This is because the Court primarily noted that "if the tenant has the right to choose his suppliers and/or the terms of use of the goods or services at issue, the supplies relating to those goods or services may, in principle, be considered to be separate from the letting. In particular, if the tenant can determine his own consumption of water, electricity or heating, which can be verified by the installation of individual meters and billed according to their consumption, supplies relating to those goods or services may, in principle, be considered to be separate from the letting. As regards services, such as the cleaning of the common parts of a building under joint ownership, such services should be regarded as separate from the letting, if they can be organised by each tenant individually or by the tenants collectively and if, in all cases, the supply of those goods and services is itemised separately from the rent on invoices addressed to the tenant".[38]

The Court ruled that "the mere fact that the non-payment of rental charges allows the landlord to terminate the rental agreement does not prevent the services to which those charges relate from constituting services separate from the letting." Similarly, the fact "that the tenant has the right to obtain those services from the provider of his choice is also not in itself decisive, since the possibility that elements of a single supply may, in other circumstances, be supplied separately is inherent in the concept of a single composite transaction".[39] On the other hand, the CJEU stated that "if an immovable property offered for letting appears objectively, from an economic point of view, to form a whole with the supplies that accompany it, they can be considered to constitute a single supply with the letting. The same may apply to the letting of turnkey offices, ready for use with the provision of utilities and certain other supplies, and the immovable property which is let for short periods, in particular for holidays or for professional reasons, and offered with those supplies, which are not separable from it".[40]

As a consequence of the judgment regarding Wojskowa Agencja Mieszkaniowa, there has been a practice developed that provisions concerning settlement of utility costs separately from rental costs are introduced in rental/lease agreements. If there are no such provisions, however, utility costs are part of the price (Kasprzyk & Verdun, 2019, pp. 14–22).

Therefore, the judgment regarding Wojskowa Agencja Mieszkaniowa in Warsaw, C42/14, is an example of a view of the CJEU whereby referring directly to the stipulations of a contract, the Court has developed a practice that affects the way rental services and associated services are taxed.

The significance of the economic objective of a contract in transactions concerning land that has not been built on

In the judgments that covered composite services, the Court examined, among others, the possibility

[37] Judgment of the CJEU in Case C-42/14 Wojskowa Agencja Mieszkaniowa, paragraph 37.

[38] Judgment of the CJEU in Case C-42/14 Wojskowa Agencja Mieszkaniowa, paragraph 39.

[39] Judgment of the CJEU in Case C-42/14 Wojskowa Agencja Mieszkaniowa, paragraphs 40 and 41.

[40] Judgment of the CJEU in Case C-42/14 Wojskowa Agencja Mieszkaniowa, paragraph 42.

of applying exemptions in connection with supply of land that has not been built on.[41]

When defining areas that should be considered 'building land', Member States are obliged to upkeep the objective pursued by point (k) of Article 135(1) of Directive 112, which consists in only exempting from VAT supply of land that has not been built on and is not intended for such a purpose.[42]

The Member States' discretion in defining the term 'building land' is also limited by the scope of the term 'building', very broadly defined by the EU legislator in the first paragraph of Article 12(2) of Directive 112 as including "any structure fixed to or in the ground".[43]

In its case law, the TS has repeatedly indicated circumstances to be taken into account when sale of the land along with an existing building which is planned to be partially or completely demolished is classified for VAT purposes. "It is clear from the case law of the Court that the relevant objective factors to be taken into consideration for the purposes of classifying a given transaction as regards VAT include the state of advancement, at the date of the supply of a property composed of land and a building, of the demolition or transformation works carried out by the vendor, the use of that immovable property on the same date and the undertaking by the vendor to carry out demolition work in order to enable future construction".[44]

In the judgment regarding Don Bosco Onroerend Goed,[45] the CJEU took into account the economic objective pursued by the vendor and the purchaser of the property, which was to provide land ready for construction. Therefore, the CJEU declared that "the vendor was responsible for the demolition of the existing building on the land in question and that the cost of that demolition had been borne, at least in part, by the purchaser." The Court also pointed out that "at the date of the supply of the immovable property, the demolition of the building had already begun. Therefore, "in the light of those circumstances, the Court classified the supply of the immovable property in question and the demolition of the existing building as a single supply of land which had not been built upon".[46]

In other judgments concerning the character of immovable property subject to sale, the Court has also upheld the view that in order to determine whether a transaction that involves multiple services is a single transaction for the purposes of VAT, its economic purpose must be taken into consideration.[47] However, the purpose of the transaction was not always of paramount importance for assessing the tax effects regarding value added tax in the case of sale of real estate. The purpose of a transaction was not decisive in the judgment of 8 July 1986, Kerrutt 73/85.[48] The Court that was asked "whether the supply of building land and

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[41] Article 135 of Directive 112 states:

"1. Member States shall exempt the following transactions:

...

(j) the supply of a building or parts thereof, and of the land on which it stands, other than the supply referred to in point (a) of Article 12(1);

(k) the supply of land which has not been built on other than the supply of building land as referred to in point (b) of Article 12(1);"

However, Article 12(3) of Directive 112 provides that for the purposes of supply of building land, 'building land' shall mean any unimproved or improved land defined as such by the Member States."

[42] Judgment of the CJEU of 17 January 2013 in Case C-543/11 Woningstichting Maasdriel, EU:C:2013:20, paragraph 30; of 4 September 2019 in Case C-71/18 KPC Herning, ECLI:EU:C:2019:660, paragraph 53 and the case law cited therein.

[43] Judgment of the CJEU in Case C-71/18 KPC Herning, paragraph 54 and the case law cited therein.

[44] Judgments of the CJEU: in Case C-326/11 J.J. Komen en Zonen Beheer Heerhugowaard, paragraph 34; in Case C-543/11 Woningstichting Maasdriel, paragraph 33.

[45] Judgment of the CJEU in Case C-461/08 Don Bosco Onroerend Goed.

[46] Judgment of the CJEU in Case C-461/08 Don Bosco Onroerend Goed, paragraph 39.

[47] See similar judgments of the CJEU: of 28 October 2010, in Case C-175/09 Axa UK, , EU:C:2010:646, paragraph 23; in Case C392/11 Field Fisher Waterhouse, paragraph 23; of 8 December 2016 in Case C-208/15 Stock'94, ECLI:EU:C:2016:936, paragraph 29.

[48] Judgment of the CJEU of 8 July 1986 in Case 73/85 Kerrutt, EU:C:1986:295.

the subsequent construction on that land of a new building, as provided for in a framework contract, were to be classified as a single transaction, took account of the fact that, first, the transaction relating to the land and, second, supplies of property and services constituted legally distinct transactions carried out by different contractors." Under these circumstances, the CJEU decided that "despite the economic links between all the transactions at issue and their common purpose, which consisted of the construction of a building on the land acquired, it was not appropriate, in the circumstances of that case, to classify them as a single transaction"[49]

In KPC Herning Case, C-71/18,[50] the Court examined "whether Article 12(1)(a) and (b), (2) and (3) and Article 135(1)(j) and (k) of Directive 2006/112 must be interpreted as meaning that a supply of land supporting a building at the date of that supply may be classified as a supply of 'building land' where the parties' intention was that the building should be wholly or partly demolished to make room for a new building". In that judgment, the CJEU declared that "Article 12(1)(a) and (b), (2) and (3), and Article 135(1)(j) and (k) of Directive 2006/112 must be interpreted as meaning that a supply of land supporting a building at the date of that supply cannot be classified as a supply of 'building land' where that transaction is economically independent of other services and does not form a single transaction with them, even if the parties' intention was that the building should be wholly or partly demolished to make room for a new building". The Court held that the intention of the parties to a contract itself cannot determine that sale should be considered supply of building land and not supply of an old building and the relevant land, if the object of the supply were a fully operational building that could be used as a warehouse. This is because according to the CJEU, such an interpretation "would undermine the principles of Directive 2006/112 and would be likely to render the exemption provided for in Article 135(1)(j) of that directive meaningless." The Court noted that "the interpretation of the terms used to describe the exemptions envisaged by Article 135(1) of Directive 2006/112 must be consistent with the objectives pursued by those exemptions and comply with the requirements of the principle of fiscal neutrality inherent in the common system of VAT".[51]

It follows from the above that the economic objective of a transaction may be of considerable importance for the classification of transactions such as supply of building land. However, this objective should not be taken into account, if that were contradictory to the provisions of the Directive providing for the tax exemptions.

The importance of contractual provisions for determining when a tax obligation arises in VAT

The issue of the impact of contractual provisions on the moment when tax liability arises was discussed, among others, in relation to construction services. In the Budimex Case, the Court answered the following question of a national court: "In a situation where the parties to a transaction have agreed that payment for construction works or construction/installation works requires express acceptance by the client of their performance in the formal record of acceptance for the works, does the performance of services, for the purposes of Article 63 of [the VAT Directive], in respect of such a transaction occur at the time of actual performance of the construction or construction/installation works, or at the time of acceptance of the performance of the works by the client, expressed in the formal record of acceptance?"[52] In this case, "the parties in the main proceedings disagree as to the time from which the services supplied by

[49] Judgment of the CJEU in Case 73/85 Kerrutt, paragraphs 12 and 15.

[50] Judgment of the CJEU in Case C-71/18 KPC Herning.

[51] Judgment of the CJEU in Case C-71/18 KPC Herning, paragraphs 59, 60, and 62.

[52] Judgment of the CJEU in Case C-224/18 Budimex.

Budimex were performed. Budimex claims that, under the terms of the contract that it uses, that time can run only once the work is accepted by the client, regardless of whether the work was in fact completed at an earlier date". The Court declared that "whilst it is true that construction or installation services are commonly regarded as supplied on the actual date the work is completed, the fact remains that, for a transaction to be regarded as a 'taxable transaction' within the meaning of the VAT Directive, economic and commercial realities form a fundamental criterion for the application of the common system of VAT, which must be taken into account".[53] According to the Court, "it is not inconceivable that, taking account of contractual terms reflecting the economic and commercial realities in the field in which the service is supplied, that service may be regarded as supplied only at a time after the actual completion of the service, following the performance of certain formalities indistinguishably related to the service and conclusive in ensuring its complete performance. In that regard, it must be borne in mind that a supply of services is taxable only 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".[54] Therefore, the CJEU took into account that "it follows from the information provided by the referring court that the terms of contracts concluded by the applicant in the main proceedings provide the client with the right to check the conformity of the completed construction or installation work before accepting it and the supplier with the obligation to carry out the necessary modifications so that the end product does in fact correspond to what was agreed". The Court took into consideration the company's claim that it had frequently been impossible for them to determine the taxable amount and the amount of tax due before the client accepted the works.[55] The Court noted that "whilst the requirement constituted by the drawing up of a formal record of acceptance by the client takes place only after the time given to the client for notifying the supplier of any defects, which would be for the supplier to remedy so that the construction or installation service complies with the terms of the contract, it is not inconceivable that that service is not entirely performed before the time of acceptance".[56] As a consequence, the Court ruled that "in so far as it is not possible to ascertain the consideration due by the customer before the customer has accepted the construction or installation work, the VAT on such services cannot be chargeable before that acceptance".[57] Finally, the Court concluded that "provided that the acceptance of the work has been stipulated in the contract for the supply of services, provided that such a requirement reflects the conventional rules and standards in the field in which the service is supplied, which is for the referring court to ascertain, it must be held that that requirement is itself a part of the service and that it is, therefore, decisive in determining whether that service has in fact been supplied".[58]

Thus, not only have important contractual terms turned out significant, but also the rules and standards in the field in which the service is provided, that is, the economic practice. It is a normal practice that the construction and installation services are performed on the basis of pre-existing contracts defining, among others, the scope of such a service, the conditions for its performance, the deadline, and the manner of financial settlements. In such contracts, the client usually reserves the right to examine the performance of the service before it is accepted, which may give rise to a necessity to carry out additional operations

[53] Judgment of the CJEU in Case C-224/18 Budimex, paragraph 27.

[54] Judgment of the CJEU in Case C-224/18 Budimex, paragraphs 29 and 30.

[55] Judgment of the CJEU in Case C-224/18 Budimex, paragraph 31.

[56] Judgment of the CJEU in Case C-224/18 Budimex, paragraph 32.

[57] Judgment of the CJEU in Case C-224/18 Budimex, paragraph 34.

[58] Judgment of the CJEU in Case C-224/18 Budimex, paragraph 35.

by the service provider to ensure that the ordered service has been performed in accordance with the conditions set out earlier. The above characteristics of the services are expressed, among others, in contractual provisions that define precisely the moment when the works (i.e., the construction service) are 'taken over' by the client (i.e., the purchaser of the service). In accordance with the contracts that are usually concluded, works will be taken over by the client when they are completed in accordance with the contract. In practice, the so-called 'acceptance report' is drawn up (which testifies that the works have been taken over). Then the moment of completion of the works is considered to be the moment of issuance of the 'acceptance report' or the moment when it should be issued. From then on, the responsibility for the works is taken over by the client.

Therefore, for the purposes of value added tax, the acceptance report may give rise to the tax liability. In order for the date of execution of the acceptance report to be considered the moment of provision of the service, it is necessary to provide for the acceptance of the works in the contract concerning construction works and for the acceptance report not only to specify remuneration but also confirm formal completion of the service (Wesołowska, 2019).

A question arises whether the contractual stipulations providing for the need to confirm performance of the service by the purchaser alone should be taken into account, if they do not conform to the conventional rules and standards existing in the field in which the service is supplied. Before the question can be answered, it should be noted that the CJEU has not limited its stance to construction services only. The moment when tax liability arises is linked to contractual provisions if they reflect the conventional rules and standards existing in the field in which the service is provided. These are the contractual provisions that require the purchaser to accept the performance of the service. This may, therefore, also apply to other services where it is necessary – either because of legal regulations or the practice resulting from the need to maintain certain safety, hygiene, and other similar standards – to verify and formally confirm the scope and quality of the services performed.[59] The contractual obligation to confirm the performance of certain services may affect the moment when tax liability arises, only if such an obligation is not only clearly and precisely indicated in the contract but also prevalent in the industry concerned.[60] It seems that this is not concerned with ignoring the substance of legal operations because of their artificial nature. Deviating from the conventional rules and standards prevalent in a given field may be due to reasons other than the mere desire to abuse the law. The parties to an agreement may shape their mutual obligations at will. In this respect, it can also be concluded that in order for specific civil law effects to be produced, the acceptance of the service will take place at a different time than its performance. However, it will not always lead to postponing the tax obligation, but only if it is in line with existing practice in the field in question, which the Court refers to as maintaining the conventional rules and standards.

The judgment of the CJEU in the Budimex case upholds the view taken in the case regarding Wojskowa Agencja Mieszkaniowa, C-42/14, which is that contractual provisions may be relevant for classifying operations for VAT purposes. However, in the case of the Budimex judgment, the Court made it clear that whether contractual terms may be taken into account depends on the economic practice in the field relevant for the services. The differences between the above judgments result from the fact that in the case regarding Wojskowa Agencja Mieszkaniowa, C-42/14, the Court was considering the issue of rates for rental services and the relevant ancillary services. However, in the Budimex case, C-224/18, the Court was considering the possibility of postponing the moment of emergence of tax liability in the case of construction services that require verification by the client. As far as composite services are concerned, such as the case with the judgment regarding Wojsko-

[59] Likewise: K. Kasprzyk, M. Verdun (2019, pp. 14–22).

[60] Ibidem.

wa Agencja Mieszkaniowa, the transaction-specific elements are important. These elements characteristic for letting were taken into consideration by the CJEU that declared that "it needs to be assessed, in particular, whether, under the contract, the tenant and the landlord seek, above all, to obtain and let immovable property, respectively, and whether the fact that one party obtains other services provided by the other party is of only secondary importance to them, even if they are necessary for the enjoyment of the property".[61]

The importance of the economic objective of a contract for the determination of the place of a taxable transaction

Taking account of the economic and commercial reality does not only come down to the need to take into consideration the contractual terms, but in some cases, it also requires considering the economic practice. The case law regarding determination of the place of a taxable transaction can be cited as an example of this. In view of the actual practice with respect to a given type of transaction, the Court has concluded that "supply of goods falls within the scope of Article 33 of Directive 2006/112 where the role of the supplier is predominant in terms of initiating and organising the essential stages of the dispatch or transport of the goods.[62] In that regard, in order to determine whether the goods concerned have been dispatched or transported on behalf of the supplier, account must be taken, first, of the significance of the issue of delivering those goods to the purchasers in the light of the commercial practices which characterise the activity carried on by the supplier concerned." In the CJEU's view, "if that activity consists in actively offering goods for consideration to purchasers residing in a Member State other than that in which the supplier is established and in whose territory it does not have an establishment or warehouse, the organisation by that supplier of the means enabling the goods concerned to be delivered to their purchasers constitutes, in principle, an essential part of that activity".[63] Consequently, the Court has taken the view that "Article 33 of Directive 2006/112 must be interpreted as meaning that, when goods sold by a supplier established in one Member State to purchasers residing in another Member State are delivered to those purchasers by a company recommended by that supplier, but with which the purchasers are free to enter into a contract for the purpose of that delivery, those goods must be regarded as dispatched or transported 'by or on behalf of the supplier' where the role of that supplier is predominant in terms of initiating and organising the essential stages of the dispatch or transport of those goods, which it is for the referring court to ascertain, taking account of all the facts of the dispute in the main proceedings".[64] In this respect, the Court's stance was in line with the opinion expressed by the Commission on that case. The Commission stated that "for the application of the distance selling rules, not only the contractual arrangements between the supplier, the transporter, and the customer have to be taken into account but also, and more importantly, the economic reality".[65]

The economic objective of a transaction in the case of classification as a taxable transaction

Analysis of the Court's case law shows which elements of a tax relationship may be affected by

[61] Judgment of the CJEU in Case C-42/14 Wojskowa Agencja Mieszkaniowa, paragraph 37.

[62] Judgment of the CJEU in Case C-276/18 KrakVet Marek Batko, paragraph 63.

[63] Judgment of the CJEU in Case C-276/18 KrakVet Marek Batko, paragraph 69.

[64] Judgment of the CJEU in Case C-276/18 KrakVet Marek Batko, paragraph 82.

[65] Opinion of the AG of 6 February 2020 in Case KrakVet Marek Batko, C-276/18, ECLI:EU:C:2020:81, paragraph 37.

the economic objective of a transaction within the framework of value added tax. The Court's case law has been revised above in order to verify whether the economic objective of a contract affects the classification of a transaction as regards, among others, identification whether transactions should be considered to be composite or separate, who the supplier and the recipient are, and when tax liability arises.

The economic objective of a transaction may be vital to recognise it as a taxable transaction in the first place. In the MEO – Serviços de Comunicações e Multimédia[66] case, the CJEU considered "whether the predetermined amount received by an economic operator where a contract for the supply of services with a minimum commitment period is terminated early by its customer or for a reason attributable to the customer, which corresponds to the amount that the operator would have received for the remainder of that period, should be regarded as payment for a supply of services for consideration within the meaning of Article 2(1)(c) of the VAT Directive, and, as such, be subject to VAT". In this case, the CJEU took into account that the telecommunications company had "a right under the agreements at issue in the main proceedings, in the event of failure to observe the minimum commitment period, to payment of the same amount as it would have received as payment for services which it undertook to supply in the event that the customer had not terminated his contract". In this case, "the early termination of the contract by the customer, or its termination for a reason attributable to that customer, does not alter the economic reality of the relationship between MEO and its customer".[67]

Under these circumstances, the Court declared that "it must be held that the consideration for the amount paid by the customer to MEO is constituted by the customer's right to benefit from the fulfilment, by MEO, of the obligations under the services contract, even if the customer does not wish to avail himself or cannot avail himself of that right for a reason attributable to him". This is because in this case, MEO made it possible for the customer to use the service in question and was not responsible for its discontinuation. The Court noted that if the disputed amount "were characterised as damages to make good for the loss suffered by MEO, the nature of the consideration paid by the customer would be changed, depending on whether or not the customer decides to use the service in question during the period provided for in the contract. Thus, a customer who benefited from services for the entire commitment period stipulated in the contract and a customer who terminated the contract before the end of that period would be treated differently for the purposes of VAT".[68] Consequently, the CJEU concluded that "the amount payable for non-compliance with the minimum commitment period is payment for the services provided by MEO, regardless of whether the customer exercises the right to benefit from those services until the end of the minimum commitment period".[69]

Conclusion

Analysis of the Court's case law allows one to conclude that the economic objective of a contract between the parties to a transaction may be of considerable importance for the determination of the tax effects in VAT. This is because the economic and commercial reality is a fundamental criterion for the operation of the common VAT system, and it should be taken into account. In this respect, significant contractual terms may be important. In addition to the stipulations of the contract between the parties, objective interests of the parties, such as pricing and invoicing, may also be relevant. It is also possible to refer to the economic purpose of supply and the conventional rules and standards applicable in a given field as well as the economic practice.

[66] Judgment of the CJEU in Case C295/17 MEO – Serviços de Comunicações e Multimédia.

[67] Judgment of the CJEU in Case 295/17 MEO – Serviços de Comunicações e Multimédia, paragraph 44.

[68] Judgment of the CJEU in Case 295/17 MEO – Serviços de Comunicações e Multimédia, paragraphs 45–45.

[69] Judgment of the CJEU in Case 295/17 MEO – Serviços de Comunicações e Multimédia, paragraph 48.

The Court's case law indicates a number of limitations in shaping the tax-related facts through the substance of civil law acts (Ciecierski, 2019) In particular, contractual terms "may be disregarded if it becomes apparent that they do not reflect economic and commercial reality but constitute a wholly artificial arrangement which does not reflect economic reality and was set up with the sole aim of obtaining a tax advantage, which it is for the national court to determine."

Adhering to the substance of a civil law act in a tax relationship within the framework of VAT is sometimes dependant on other factors, including the conventional rules and standards existing in the field in which a given service is supplied. The economic objective of a contract should also not be taken into consideration, if that were contrary to the provisions of the Directive that introduce tax exemptions.

Therefore, the economic objective of a contract arising directly from its stipulations or the general economic situation that the contract is concluded in may be a factor that should be taken into account when assessing the tax effects in VAT.

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