AN COIMISIÚN UM ACHOMHAIRC CHÁNACH
TAX APPEALS COMMISSION

40TACD2023

Between

[redacted]

Appellant

and

REVENUE COMMISSIONERS

Respondent

Determination

Introduction

1. This is an appeal to the Tax Appeals Commission ("the Commission") by [redacted] ("the Appellant") pursuant to section 119 of the Value Added Tax Consolidation Act 2010 ("VATCA 2010") against an assessment raised by the Revenue Commissioners ("the Respondent") to Value-Added Tax ("VAT") in the amount of €593,979 for the period of 1 September 2017 – 31 December 2017.

2. The assessment was raised on foot of the cancellation of the Appellant's waiver of exemption from VAT, pursuant to section 96 of the VATCA 2010. The net question to be determined in this appeal is whether the requirement on the Appellant to pay the cancellation sum is incompatible with the principle in EU law of fiscal neutrality.

3. The appeal proceeded by way of a hearing on 17 November 2022.

Background

4. On 22 October 2020, the Respondent raised an assessment to VAT against the Appellant in the sum of €593,979. The assessment arose on foot of the sale of a property, [redacted] ("the property"), which completed on 12 September 2017.

5. On 20 November 2020, the Appellant appealed the assessment to the Commission.

6. In earlier submissions, the Appellant argued *inter alia* that no charge properly arose pursuant to section 96 of the VATCA 2010. Subsequently, but prior to the hearing herein, the Appellant withdrew this argument and accepted that, as a matter of domestic law, a liability to tax arose. Therefore, the sole question under consideration at the hearing was whether the domestic provision imposing the liability breaches EU law.

Legislation

7. Directive 77/388/EC ("the Sixth VAT Directive") stated *inter alia* that

> "*Article 13*
>
> *Exemptions within the territory of the country*
>
> *[…]*
>
> *B. Other exemptions*
>
> *Without prejudice to other Community provisions, Member States shall exempt the following under conditions which they shall lay down for the purpose of ensuring the correct and straightforward application of the exemptions and of preventing any possible evasion, avoidance or abuse…*
>
> *(b) the leasing or letting of immovable property…*
>
> *C. Options*
>
> *Member States may allow taxpayers a right of option for taxation in cases of: (a) letting and leasing of immovable property…*
>
> *Member States may restrict the scope of this right of option and shall fix the details of its use.*
>
> *Article 17*
>
> *1. The right to deduct shall arise at the time when the deductible tax becomes chargeable.*

2. In so far as the goods and services are used for the purposes of his taxable transactions, the taxable person shall be entitled to deduct from the tax which he is liable to pay:

(a) value added tax due or paid within the territory of the country in respect of goods or services supplied or to be supplied by him to another taxable person…"

8. Directive 2006/112/EC ("the Principal VAT Directive") states *inter alia* that

"*Article 135*

1. Member States shall exempt the following transactions…

(l) the leasing or letting of immovable property…

Article 137

1. Member States may allow taxable persons a right of option for taxation in respect of the following transactions…

(d) the leasing or letting of immovable property.

2. Member States shall lay down the detailed rules governing exercise of the option under paragraph 1.

Member States may restrict the scope of that right of option.

[…]

Article 167

A right of deduction shall arise at the time the deductible tax becomes chargeable.

Article 168

In so far as the goods and services are used for the purposes of the taxed transactions of a taxable person, the taxable person shall be entitled, in the Member State in which he carries out these transactions, to deduct the following from the VAT which he is liable to pay:

(a) The VAT due or paid in that Member State in respect of supplies to him of goods or services, carried out or to be carried out by another taxable person…"

9. Section 7 of the Value-Added Tax Act 1972 ("VATA 1972") provided, as at January 2006, that

"(1) (a) Where, but for the provisions of section 6, tax would be chargeable in respect of the supply of any of the services to which paragraph (iv) of the First Schedule relates, a person supplying any such services may, in accordance with regulations, waive his right to exemption from tax in respect thereof. Any such waiver shall extend to all the services to which the said paragraph (iv) relates that the person supplies.

Provided that where a person waives his right to exemption from tax in respect of the leasing or letting of goods which are subject to an agreement of the type referred to in section 4(2C)(a) then that waiver shall only apply to the supply of services under that agreement.

(b) A waiver of exemption from tax under this subsection shall not apply or be extended to any disposal of an interest in immovable goods which is deemed to be a letting of immovable goods to which paragraph (iv) of the First Schedule applies by virtue of section 4(3A)(a)(ii).

(2) A waiver of exemption under subsection (1) shall have effect from the commencement of such taxable period as may be agreed between the person making the waiver and the Revenue Commissioners and shall cease to have effect at the end of the taxable period during which it is cancelled in accordance with subsection (3).

(3) Provision may be made by regulations for the cancellation, at the request of a person, of a waiver made by him under subsection (1) and for the payment by him to the Revenue Commissioners as a condition of cancellation of such sum (if any) as when added to the total amount of tax (if any) due by him in accordance with section 19 in relation to the supply of services by him to which the waiver applied is equal to the total of -

(a) the amount of tax deducted by him in accordance with section 12 in respect of tax borne or paid in relation to the supply of such services,

(aa) the amount of tax deducted by him in accordance with section 12, prior to the commencement of the letting of the immovable goods to which the waiver relates, in respect of or in relation to his acquisition of his interest in, or his development of, those immovable goods,

(b) the amount of tax that would be deductible by him in accordance with section 12 if tax had been chargeable on the transfer of ownership of goods to

him in respect of which the provisions of section 3(5)(b)(iii) were applied, and those goods were used by him in the supply of such services, and

(c) the amount of tax that would be deductible by him in accordance with section 12 if tax had been chargeable on the supply to him of goods or services in respect of which the provisions of paragraph (via) of the Second Schedule were applied, and those goods or services were used in relation to the supply of services by him to which the waiver applied.

(4) Where exemption has been waived under subsection (1) in respect of the supply of any service, tax shall be charged in relation to the person making such waiver during the period for which such waiver has effect as if the service to which the waiver applies was not specified in the First Schedule."

10. Section 96 of the VATCA 2010 provides *inter alia* that

"(1) In this section "waiver" means a waiver of exemption from tax under section 7(1) of the repealed enactment.

(2) A waiver shall cease to have effect at the end of the taxable period during which it is cancelled in accordance with subsection (3).

(3) Provision may be made by regulations for the cancellation, at the request of a person or in accordance with subsection (8) or (12), of a waiver by the person and for the payment by that person to the Revenue Commissioners as a condition of cancellation of such sum (if any) as when added to the total amount of tax (if any) due by him or her in accordance with Chapter 3 of Part 9 in relation to the supply of services by him or her to which the waiver applied is equal to the total of—

(a) the amount of tax deducted by the person in accordance with Chapter 1 of Part 8 in respect of tax borne or paid in relation to the supply of such services,

(b) the amount of tax deducted by the person in accordance with section 12 of the repealed enactment, prior to the commencement of the letting of the immovable goods to which the waiver relates, in respect of or in relation to his or her acquisition of his or her interest in, or his or her development of, those immovable goods,

(c) the amount of tax that would have been deductible by the person in accordance with section 12 of the repealed enactment if tax had been chargeable on the transfer of ownership of goods to him or her in respect of

which section 20(2)(c) was applied, and those goods were used by him or her in the supply of such services, and

(d) the amount of tax that would have been deductible by that person in accordance with section 12 of the repealed enactment if—

(i) tax had been chargeable on the supply to that person of goods or services in respect of which paragraph 7(7) of Schedule 2 was applied, and

(ii) those goods or services were used, in relation to the supply of services to which the waiver applied, by the person.

(4) Where there is a waiver in respect of the supply of a service, tax shall be charged in relation to the person making the waiver during the period for which the waiver has effect as if the service to which the waiver applies was not specified in Schedule 1.

[…]

(12) (a) In this subsection "relevant immovable goods" means immovable goods the tax chargeable on the acquisition or development of which a landlord would be obliged to take into account in accordance with subsection (3) in relation to the cancellation of that landlord's waiver.

(b) This subsection applies where—

(i) on or after 3 June 2009, a landlord has an interest in relevant immovable goods,

(ii) the landlord ceases, whether as a result of disposing of such goods or otherwise, to have an interest in any such goods, and

(iii) on the date when that landlord ceases to have any such interest, that landlord's waiver has not been cancelled in accordance with subsection (3).

(c) Where this subsection applies—

(i) the landlord's waiver of exemption shall be treated as if it were cancelled on the date referred to in paragraph (b)(iii), and

(ii) that landlord shall pay an amount, being the amount payable in accordance with subsection (3) in respect of the cancellation of that

waiver, as if it were tax due by that landlord for the taxable period in which the waiver of exemption is so treated as cancelled."

11. Schedule 1, VATCA 2010 provides that exemption from VAT applies to, *inter alia*,

"*11.(1) The letting of immovable goods…*"

Case Law

12. The scope of Member States' discretion under Article 13C / Article 137 of the VAT Directives has been considered by the Court of Justice of the European Union ("CJEU") in a number of cases over the past twenty five years. The Commissioner sets out hereunder what he considers to constitute the principal case law from the judgments of the CJEU referred to by the parties, following which he summarises what he understands to be the key principles arising.

13. In *Belgocodex SA v Belgian State* Case C-381/97 ("*Belgocodex*"), the CJEU stated *inter alia* that

> "*15. It must be recalled in this regard that Title X (Articles 13 to 16) of the Sixth Directive establishes a system of exemption from VAT for certain transactions. The exemptions include, under Article 13B(b), the letting and leasing of immovable property. However, as far as these transactions are concerned, Member States have the power, under point (a) of the first paragraph of Article 13C, of reintroducing liability to tax, by means of a right of option which they may allow their taxpayers to exercise. Under the second paragraph of Article 13C, Member States may restrict the scope of this right of option and fix the details of its use.*
>
> *16. As the Court has held previously, Member States may, by virtue of this power, allow persons benefiting from the exemptions provided for by the Directive to waive the exemption in all cases or within certain limits or subject to certain detailed rules …*
>
> *17. As the Commission also points out, it follows that the Member States have a wide discretion under Article 13B and C. It is for them to assess whether they should or should not introduce the right of option, depending on what they consider to be expedient in the situation existing in their country at a given time. The freedom to grant or decline to grant the right of option is not restricted in time or by the fact that a contrary decision had been adopted in the past. Member States may therefore, within the sphere of their national powers, also revoke the right of option after having introduced it and return to the basic rule that letting and leasing of immovable property are exempt from tax.*

18. Contrary to what the plaintiff in the main proceedings argues, this solution is not called in question by the principle of fiscal neutrality. Admittedly, this principle, which is laid down in Article 2 of the First Directive and which is inherent in the common system of value added tax, requires, as the fourth and fifth recitals of the Sixth Directive state, that all economic activities should be treated in the same way…

19. However, it does not have the effect attributed to it by the plaintiff in the main proceedings. Since the implementation, by the Sixth Directive, of the harmonised system of exemptions, it is no longer possible to derogate from that system on the basis of a provision of the First Directive. Furthermore, the principle of fiscal neutrality does not preclude the introduction, by a national legislature, of a series of exceptions to the rule of liability to tax, which are, moreover, expressly provided for in Title X of the Sixth Directive. However, where a national legislature has granted taxpayers the right of option, it cannot be inferred from the principle of fiscal neutrality that its choice is irreversible."

14. In *État du grand-duché de Luxembourg v Vermietungsgesellschaft Objekt Kirchberg SARL* Case C-269/03 ("*VOS*"), the CJEU stated *inter alia* that

"*18. VOK and the Commission maintain that the provisions of Article 13(C) of the Sixth Directive relating to the letting or leasing of immovable property cannot be interpreted as meaning that they permit the Member States to adopt legislation, such as that in issue in the main proceedings, involving a process of prior approval leading, in certain cases, to the impossibility of deducting all input VAT.*

19. In that regard, it is appropriate to note that the right to deduct is a fundamental principle of the VAT system. It is important to scrutinise whether an approval process, such as that adopted by the Grand Duchy of Luxembourg, is an improper implementation of the right to opt for taxation provided for by the provisions of Article 13(C) of the Sixth Directive, in that it adversely affects that principle.

20. It is clear from those provisions that the taxation of leasing and letting transactions is a power which the legislature has conferred on the Member States in derogation from the general rule established in Article 13(B)(b) of the Sixth Directive, according to which leasing and letting transactions are, as a rule, exempt. The right to deduct does not therefore operate automatically in that context but only if the Member States have made use of the power under Article 13(C) of the Sixth Directive and subject to the taxpayers exercising the right of option allowed to them.

21. As the Court has previously held, Member States may, by virtue of this power, allow persons benefiting from the exemptions provided for by the Sixth Directive to waive the exemption in all cases or within certain limits or subject to certain detailed rules. It follows that the Member States have a wide discretion under Article 13(B) and (C) of the Sixth Directive…"

15. In *Turn- und Sportunion Waldburg v Finanzlandesdirektion für Oberösterreich* Case C-246/04 ("*Turn- und Sportunion*"), the CJEU stated *inter alia* that

"*27. As the Court has previously held, it is clear from the wording of Article 13(C) of the Sixth Directive that Member States may, by virtue of this power, allow persons benefiting from the exemptions provided for by that directive to waive the exemption in all cases or within certain limits or subject to certain detailed rules…*

28. Article 13(C) of the Sixth Directive thus allows the Member States to grant taxable persons the right to opt for taxation of lettings of immovable property, but also allows them to restrict the scope of that right or withdraw it…

29. It follows that the Member States have a wide discretion under Article 13(C) of the Sixth Directive. It is for them to assess whether they should or should not introduce the right of option, depending on what they consider to be expedient in the situation existing in their country at a given time…

30. Thus, in exercising their discretion with regard to the right of option, the Member States may also exclude certain transactions or certain categories of taxable persons from the scope of application of that right…

31. Nevertheless, as the Commission correctly points out, when the Member States use their ability to restrict the scope of the right of option and to determine the arrangements for its exercise, they are to observe the general objectives and principles of the Sixth Directive, in particular the principle of fiscal neutrality and the requirement for correct, straightforward and uniform application of the exemptions provided for…"

16. In *Finanzamt Steglitz v Ines Zimmermann* Case C-174/11 ("*Zimmermann*"), the CJEU stated *inter alia* that

"*46. In relation to those points, it should be borne in mind that, in the field of VAT, the concept of neutrality is used in different senses.*

47. On the one hand, recalling that the deduction mechanism provided for under the Sixth Directive is intended to relieve the trader entirely of the burden of the VAT payable or paid in the course of all his economic activities, the Court has held that the

common system of VAT seeks to ensure neutrality of taxation of all economic activities, provided that those activities are themselves subject in principle to VAT…

48. On the other hand, according to settled case-law, the principle of fiscal neutrality means that supplies of goods or services which are similar, and which are accordingly in competition with each other, may not be treated differently for VAT purposes…"

17. In *Imofloresmira — Investimentos Imobiliários SA v Autoridade Tributária e Aduaneira* Case C-672/16 ("*Imofloresmira*"), the CJEU stated inter alia that

"*41. In the present case, according to the interpretation adopted by the tax and customs authority, the fact that a property is unoccupied for a certain period interrupts the use of the property for the purposes of the business, requiring the taxable person to adjust the tax deducted, even if it is demonstrated that it still intends to continue to pursue a taxed activity.*

42. It follows from the case-law cited in paragraphs 39 and 40 above that a taxable person retains the right of deduction where that right has arisen, even if that taxable person could not, for reasons beyond its control, use the goods or services giving rise to the deduction in the context of taxed transactions.

43. Any other interpretation of the VAT Directive would be contrary to the principle that VAT should be neutral as regards the tax burden on a business. It would be liable to create, as regards the tax treatment of the same investment activities, unjustified differences between businesses already carrying out taxable transactions and other businesses seeking by investment to commence activities which will in future be a source of taxable transactions. Likewise, arbitrary differences would be established between the latter businesses, in that final acceptance of the deductions would depend on whether or not the investment resulted in taxed transactions…

44. Therefore, the principle of fiscal neutrality precludes national legislation which, by making the final acceptance of the VAT deductions dependent on the results of the taxable person's economic activity, creates, as regards the tax treatment of identical investment activities, unjustified differences between undertakings with the same profile and carrying on the same activity.

[…]

48. Secondly, even if Article 137(2) of the VAT Directive leaves Member States a wide discretionary power to determine the rules governing the exercise of the right of option and even to withdraw it… the Member States could not use that power to infringe

Articles 167 and 168 of that directive by revoking a right of deduction which has already been acquired.

49. A limitation of VAT deductions connected with taxed operations, after the right of option has been exercised, would not concern the 'scope' of the right of option which Member States may restrict by virtue of Article 137(2) of the TVA Directive, but the consequences of exercising that right…"

18. In *Skatteverket v Skellefteå Industrihus AB* Case C-248/20 ("*Skellefteå*"), the CJEU stated *inter alia* that

"*37. The Court has also repeatedly stated that the right of deduction, once it has arisen, is retained, in principle, even if, subsequently, the planned economic activity was not carried out and, therefore, did not give rise to taxed transactions… or if, by reason of circumstances beyond his or her control, the taxable person did not make use of the goods and services which gave rise to a deduction in the context of taxed transactions…*

38. Any other interpretation of the VAT Directive would be contrary to the principle that VAT should be neutral as regards the tax burden on a business. It would be liable to create, as regards the tax treatment of the same investment activities, unjustified differences between businesses already carrying out taxable transactions and other businesses seeking by investment to commence activities which will in future be a source of taxable transactions. Likewise, arbitrary differences would be established between the latter businesses, in that final acceptance of the deductions would depend on whether or not the investment resulted in taxed transactions…

39. It is also apparent from the case-law that, even though Article 137(2) of the VAT Directive gives the Member States a wide discretionary power to determine the rules governing the exercise of the right of option and even to withdraw it, the Member States may not use that power to infringe Articles 167 and 168 of that directive by revoking a right of deduction which has already been acquired… A limitation of VAT deductions connected with taxed transactions, after the right of option has been exercised, would not concern the 'scope' of the right of option which Member States may restrict by virtue of Article 137(2) of the VAT Directive, but the consequences of exercising that right…

40. Therefore, while it is open to the Member States to lay down the conditions and the rules governing the exercise of the right of option, they must not infringe the right

of deduction itself and must comply with the objectives and general principles of the VAT Directive…

41. It follows that Article 137(2) of the VAT Directive must be interpreted as precluding a provision of national legislation, such as Chapter 9, Paragraph 11, of the Law on VAT, which provides, de facto, for the revocation of the right to deduct the input tax paid where that right has been granted to a taxable person in the course of the exercise, by that taxable person, of his or her right of option."

19. In *UAB 'ARVI' ir ko v Valstybinė mokesčių inspekcija prie Lietuvos Respublikos finansų ministerijos* Case C-56/21 ("*Arvi*"), the CJEU stated *inter alia* that

"*19. Thus, Article 137 of the VAT Directive allows the Member States not only to grant taxable persons the right to opt for taxation of transactions covered by that provision, but also allows them to restrict the scope of that right or withdraw it. Accordingly, the Member States have a wide discretion under that article, since it is for them to assess whether they should or should not introduce the right of option, depending on what they consider to be expedient in the situation existing in their country at a given time…*

20. The Member States may also, in exercising their discretion, exclude certain transactions or certain categories of taxable persons from the scope of application of that right…

21. Nevertheless, when the Member States use their ability to restrict the scope of the right of option and to determine the arrangements for its exercise, they are to observe the general objectives and principles of the VAT Directive, in particular the principle of fiscal neutrality and the requirement for correct, straightforward and uniform application of the exemptions provided for…"

20. Therefore, it can be seen from the above case law that Member States have a wide discretion under Article 13C / Article 137 to restrict the scope of the right of option and fix the details of its use (*Belgocodex* and *VOS*). However, when applying that discretion, Member States are obliged to observe the principle of fiscal neutrality (*Turn- und Sportunion*). That principle is used in two senses; it means that that VAT should be neutral as regards the tax burden on a business, and it also means that supplies of goods or services which are similar may not be treated differently for VAT purposes (*Zimmermann*). A taxable person retains the right of deduction where that right has arisen, even if he could not, for reasons beyond his control, use the goods or services giving rise to the deduction in the context of taxed transactions (*Imofloresmira*). Article 137(2) of the VAT Directive must be interpreted as precluding a provision of national legislation which provides for the

revocation of the right to deduct the input tax paid where that right has been granted to a taxable person in the course of the exercise, by that taxable person, of his right of option (*Skellefteå*). It is for Member States to assess whether or not to introduce the right of option; nevertheless, when they use their ability to restrict the scope of the right of option and to determine the arrangements for its exercise, they are to observe the principle of fiscal neutrality (*Arvi*).

Evidence and Submissions

21. Evidence was heard from a member of the Appellant consortium and written and oral submissions were provided by counsel for the parties.

Appellant's Evidence

[redacted]

22. [redacted] is a member of the Appellant consortium, which comprises fifteen individuals. The Appellant purchased the property by way of contract for sale dated 20 December 2004 from [redacted]. The purpose of the purchase for the Appellant was to shelter rental income through a particular scheme available at the time.

23. The Appellant and [redacted] also entered into a development agreement on the same date in respect of the property. Additionally, the Appellant also entered into a put and call option agreement with [redacted] on the same date in respect of the property, which commenced on the seventh anniversary of the agreement and remained exercisable for six months thereafter.

24. Following completion of development, the property comprised fifteen self-contained apartments. On 20 December 2005, the Appellant entered into a lease of the property to [redacted] then the owner of an adjoining hotel. The term of the lease was to commence on 15 December 2004. The lease was subject to a waiver of exemption of VAT, pursuant to section 7 of the VATA 1972.

25. By way of its January/February 2006 VAT return, the Appellant reclaimed VAT of €717,750 on the purchase price and development costs of the property. Total VAT of €41,384 on supplies was accounted to the Respondent from 1 March 2006 to 31 December 2009. Over the same period, the Appellant reclaimed further VAT of €6,820; therefore its net payment over that period was €34,564.

26. In January 2009, [redacted] went into voluntary liquidation, and the Appellant took back control of the property and terminated the lease. Despite the Appellant's efforts, it was not possible to let the property to renters, and the property was vacant from January 2009 until

August 2015. The property was badly vandalised in around 2013 to 2015 and was also the *locus* for anti-social behaviour.

27. In September 2015, the Appellant entered into a caretaker agreement with [redacted] ("the purchaser") with a view to selling the property to him. In January 2017, following the termination of the put and call agreement with [redacted] the Appellant entered into a contract for sale with the purchaser for the property. The purchase price was €750,000 inclusive of VAT (i.e. €660,793 + €89,207 VAT). The sale completed in September 2017.

28. On cross examination, [redacted] confirmed that the Appellant had received tax advice in respect of the transactions, although he stated that he was not aware at the time of the purchase of the property that, if the Appellant waived the exemption for VAT, there was a risk that there would be a clawback of reclaimed VAT.

29. He also stated that the Appellant had considered seeking to enforce the put and call agreement, but [redacted] was not in a financial position to repurchase the property. One member of [redacted] had delayed in relinquishing his rights under the put and call agreement, which had delayed the sale of the property to the purchaser.

30. He stated that the property had been valued at approximately €105,000 - 110,000 per self-contained unit (x 15), but that the purchaser had not been willing to pay this, and had offered €750,000 in total. Given the stress that the property had caused the Appellant, the members of the consortium were eager to sell.

Appellant's Submissions

31. In written submissions, counsel for the Appellant stated that the Respondent had calculated the cancellation sum as follows:

VAT reclaimed on purchase	€717,750
Other VAT reclaimed	€6,820
VAT paid on rents	(€41,384)
VAT on sale	(€89,207)
Cancellation sum	€593,979

32. The waiver of exemption was, in essence, the right which, prior to 1 July 2008, a taxpayer who made lettings of less than ten years had to waive that exemption and account for VAT on the rents received. The purpose of doing so was that the otherwise exempt letting became taxable with the consequence that VAT incurred on the acquisition, development or enhancement of the property, which would otherwise be irrecoverable, became recoverable.

33. Counsel submitted that the requirement to pay a cancellation sum when a property had been used for fully taxable purposes was a clear and manifest breach of the Principal VAT Directive, including the principle of fiscal neutrality. The right to deduct VAT which a taxpayer is liable to pay in respect of supplies to him of goods and services is a directly effective provision of the Principal VAT Directive; *BP Soupergaz Anonimos Etairia Geniki Emporiki-Viomichaniki kai Antiprossopeion v Greek State* Case C-62/93.

34. In this instance, it was not disputed that (a) the Appellant was a taxable person, (b) the Appellant was engaged in economic activity, (c) the Appellant did not engage in any exempt or non-taxable activity, and (d) the Appellant was entitled to deduct, in full, the VAT which it incurred on the acquisition of its interest in the property. Therefore, the only issue in dispute was whether section 96(3) and (12) of the VATCA 2010 could validly impose a retrospective restriction on the Appellant's VAT deduction entitlement as a result of the fact that, due to a downturn in the Irish property market, the VAT it deducted was greater than the VAT for which it accounted.

35. There was no provision or principle under the Principal VAT Directive which authorised the retrospective withdrawal or adjustment of the right to deduct in the current circumstances. The Irish legislation could not retrospectively adjust a previous VAT deduction unless entitled to do so under the Principal VAT Directive. While the Principal VAT Directive did allow for retrospective adjustment where there had been a change of use from a taxable to an exempt or non-taxable use, that had not occurred in this case and there was no suggestion by the Respondent that it had.

36. The right to deduct VAT is so fundamental that it has been held that taxpayers who make no taxable supplies whatsoever are still entitled to deduct all of the VAT they incurred simply by proving that it was their intention to make taxable supplies; *Ryanair Ltd v Revenue Commissioners* Case C-249/17; *Inspector of Taxes v Centime Ltd* [2005] IEHC 32. Section 96(12) of the VATCA 2010 sought to entirely undermine this principle.

37. In *Imofloresmira*, the CJEU considered Portuguese national legislation which provided for the waiver of exemption on lettings but which required that adjustments be made to the deduction amount in the event that the property was vacant for more than two years. The

CJEU held that the adjustment contravened EU law. Counsel submitted that the offending Portuguese legislation was at least ostensibly focused on the question of use of the property in question. However, section 96(3) or (12) applied irrespective of use but purely on the basis that more input tax was deducted than was accounted for in input tax. Counsel submitted that the Irish legislation clearly fell outside the provision allowing for adjustments for change of use (Article 185 of the Principal VAT Directive) since it was not an adjustment imposed by reference to use at all. Section 96(12) simply punished taxpayers who engaged in full taxable activity but made losses, and directly contravened the principle set out in paragraph 44 of the court's judgment, which stated that "*the principle of fiscal neutrality precludes national legislation which, by making the final acceptance of the VAT deductions dependent on the results of the taxable person's economic activity, creates, as regards the tax treatment of identical investment activities, unjustified differences between undertakings with the same profile and carrying on the same activity*." Counsel submitted that this was not just the effect of section 96(12), but precisely what it was designed to do.

38. In oral submissions, counsel stated that fiscal neutrality means two different but related things: (i) it is intended to relieve the trader entirely of the burden of the VAT payable or paid in the course of all of his economic activities, and (ii) it means that supplies of goods or services which are similar, and which are accordingly in competition with each other, may not be treated differently for VAT purposes; *Zimmermann*. In its written submissions, the Respondent had focused on the second meaning but it was important to consider both.

39. In response to the Respondent's submission that the State was permitted, under Article 13C of the Sixth VAT Directive (and subsequently Article 137 of the Principal VAT Directive) to restrict the scope of the option to waive the exemption, counsel argued that this case was not concerned with the scope of the option, but about what limitations could be placed on the right to deduct tax after the taxpayer had exercised the option. The distinction between restricting the scope, which is who gets to avail of the right of option, and restricting the consequences of exercising that right, was critical; *Imofloresmira.* However, even where a member state wishes to restrict the scope of the option, it still must observe the principle of fiscal neutrality; *Arvi.*

40. In response to the Commissioner's question whether the matter should be referred to the CJEU for a preliminary ruling, counsel stated that it was a matter within the Commissioner's discretion. He doubted if the matter would travel to the High Court and subsequently to the Court of Appeal without a reference being made, and therefore, in order to reduce costs, he was supportive of a reference being made at this stage.

41. In reply to the Respondent's oral submissions, counsel stated that the Respondent had argued that the fiscal neutrality which section 96(12) aims to achieve was between those who opt to tax and those who do not opt, meaning there is equality between those who make exempt supplies and those who make taxable supplies. Counsel said no authority had been put forward to show that this was what was meant by fiscal neutrality, and he was not aware of any such authority. The Respondent had accepted that the discretion was subject to fiscal neutrality; therefore, if it was accepted that the Respondent's definition of fiscal neutrality was wrong, the Respondent had to lose the case.

Respondent's Submission

42. In its written submission, the Respondent contended that section 96 was enacted within the discretion afforded to the Irish legislature under Article 13C / Article 137 of the VAT Directives. The default position is that a letting is exempt from VAT with no associated right of input VAT deduction. The option to waive exemption is a choice, and once exercised it is regulated by section 96. It operates in precisely the same way for every landlord who waives exemption. The waiver cancellation amount balances input VAT recovered with output VAT charged such that the principle of fiscal neutrality is not offended. The effect of the waiver cancellation amount is that it ensures that a person who did not waive exemption is treated equitably in comparison with a person who exercised a waiver and that waiver was subsequently cancelled.

43. Counsel argued that, from the domestic legislative provisions and in particular having regard to the discretion afforded to Member States under Article 13C / Article 137, the following important points could be made:

    a. The leasing and letting of immovable goods is exempt from VAT. *Prima facie*, it is a supply which carries no right to VAT recovery.

    b. The Sixth VAT Directive and Principal VAT Directive allow Member States to provide for an option for taxation in respect of the letting of immovable goods. They also clearly state that Member States can restrict the scope of that right of option.

    c. Ireland permitted an option for taxation in the form of the waiver of exemption provided for in section 7 of the VATA 1972 (subsequently repealed), and section 96 of the VATCA 2010.

    d. Whilst the exercise of the waiver granted a right of option for taxation, there were consequences when the waiver cancelled and that was the cancellation sum that

was payable. There was nothing repugnant in this, but in any event, it was within the scope of the discretion afforded to the legislature in enacting section 96.

44. The discretion afforded to Member States under Article 13C / Article 137 was not narrow or circumscribed, but was broad; *VOS: "It follows that the Member States have a wide discretion under Article 13(B) and (C) of the Sixth Directive…"* and *Belgocodex: "…it follows that the Member States have a wide discretion under Article 13B and C. It is for them to assess whether they should or should not introduce the right of option, depending on what they consider to be expedient in the situation existing in their country at a given time. The freedom to grant or decline to grant the right of option is not restricted in time or by the fact that a contrary decision had been adopted in the past.*" The circumstances in *VOS*, where deduction was refused because an application was not made in time regardless of the taxpayer's intention to charge VAT, and *Belgocodex*, where the option was removed in its entirety, were stark examples of the breadth of the exemption afforded.

45. The Respondent provided four examples of scenarios where VAT may or may not be payable under section 96. Counsel contended that the examples demonstrated that the application of the provision was the same across each and every lease or letting of immovable goods. It could reasonably be asked what cause of complaint there was where a provision had been introduced which provided for a waiver of exemption and consequent deductibility of VAT on a supply where the starting point was that that supply was an exempt supply with no deductibility at all.

46. In oral submissions, counsel stated that the rules under consideration in this appeal were historical and that was a factor that the Commissioner should bear in mind when deciding whether or not to refer the matter to the CJEU. The scope of the discretion afforded to Member States under Article 13C / Article 137 were very broad and the Respondent considered that section 96 was enacted within that discretion. The rules were designed to ensure fiscal neutrality in the sense of equality of treatment between persons who do not exercise the waiver and those who do.

47. It was important to bear in mind that, in respect of the leasing of immovable property, there was an obligation to exempt unless the Member States in their discretion decided to allow for a right of option for taxation. Therefore, the situation was different from that pertaining in some of the cases referred to by the Appellant, e.g. *Ryanair Ltd v Revenue Commissioners* Case C-249/17.

48. What section 96 did was provide a restriction as to the scope of the exemption, which had been permitted by the CJEU. It did not interfere with the consequences of waiving the exemption. The condition set out in section 96 was known to everyone at the time of

choosing to adopt the waiver. Within the scope of the option the normal rules of deduction applied, and therefore section 96 could be distinguished from the Portuguese legislation considered in *Imofloresmira.* Section 96 allowed people to waive the exemption subject to certain limits, which the CJEU had permitted in *Belgocodex*. The condition under section 96 only applied at the end of the period when the waiver was in operation, the length of which was entirely for the taxpayer to determine. This was different to *Imofloresmira*, where the adjustment took place during the lifetime of the waiver.

49. The CJEU's judgment in *Arvi* confirmed that legislation like section 96 did not adversely affect the right to deduct, but was legislation which governed the detailed rules for the exercise of the right of option to taxation, and it was the exercise of that right which gave rise to the ability to deduct. Without such a right of option, there would be no ability to deduct at all. This case could be differentiated from *Skellefteå* as there had been no adjustment in this instance; a cancellation sum was not the same as an adjustment, but was simply the rule set at the beginning in relation to the exercise of the right of waiver. The rule was objective and applied to everyone who exercised the right of waiver.

Material Facts

50. The principal facts were not in dispute between the parties. Having read the documentation submitted, and having listened to the oral evidence and submissions at the hearing, the Commissioner makes the following findings of material fact:

    50.1 The Appellant purchased the property in December 2004. In 2006 it reclaimed VAT of €717,750.

    50.2 Despite the Appellant's efforts, the property was vacant and not let from January 2009 until August 2015.

    50.3 Between March 2006 and December 2009, the Appellant paid VAT on rents of €41,384. It further reclaimed VAT of €6,820 and therefore the net payment of VAT was €34,564.

    50.4 The Appellant sold the property in September 2017 for a price of €750,000, including VAT. VAT of €89,207 was paid on the sale.

    50.5 The Respondent subsequently issued a notice of assessment to VAT in the amount of €593,979. This amount was the difference between the amount of VAT reclaimed and the amount of VAT paid and arose on foot of the provisions of section 96(3) and (12) of the VATCA 2010.

Analysis

51. In the High Court case of *Menolly Homes Ltd v. Appeal Commissioners* [2010] IEHC 49, Charleton J. stated at para. 22: "*The burden of proof in this appeal process is, as in all taxation appeals, on the taxpayer. This is not a plenary civil hearing. It is an enquiry by the Appeal Commissioners as to whether the taxpayer has shown that the relevant tax is not payable.*"

52. Section 7 of the VATA 1972 was introduced on foot of the discretion afforded to Member States by Article 13C of the Sixth VAT Directive to allow taxpayers a right of option for taxation in respect of *inter alia* the letting or leasing of immovable property. This created an exception to the general rule, as set out in Article 13B, that the letting or leasing of immovable property was exempt from VAT. The Sixth VAT Directive was replaced by the Principal VAT Directive, with the general exemption of the leasing or letting of immovable property set out in Article 135, and the right of option for taxation set out in Article 137.

53. The Appellant in this case waived its right to exemption from tax, pursuant to section 7 of the VATA 1972. That Act was subsequently replaced by the VATCA 2010, and the right to waiver was repealed and replaced by an option to tax (section 97). Section 96 of the VATCA 2010 continues to govern the operation of waivers granted before 1 June 2008 under section 7 of the VATA 1972.

54. The Appellant's waiver was cancelled, pursuant to section 96(12) of the VATCA 2010, on foot of the sale of the property to the purchaser in September 2017. As it had reclaimed more VAT during the lifetime of the waiver than it had paid, it was obliged to pay a cancellation sum to the Respondent pursuant to section 96(3) and (12). The Appellant claims that this breached the principle of fiscal neutrality.

55. In considering this claim, the starting point should be to recognise that the activity the Appellant was engaged in was, in principle, exempt from VAT. Both Article 13C and Article 137 permit Member States to allow taxpayers a right to opt for taxation, but both allow a considerable scope of discretion to Member States in how that right is framed. Article 13C states that "*Member States may restrict the scope of this right of option and shall fix the details of its use.*" Article 137 states that "*Member States shall lay down the detailed rules governing exercise of the option…Member States may restrict the scope of that right of option.*" The Commissioner does not understand there to be any material difference between these two Articles for the purposes of this appeal, and notes that the CJEU in *Arvi* has described them as "*substantially identical*". The question then arises whether the obligation to pay a cancellation sum under section 96 is within the discretion allowed to Member States under Article 13C / Article 137.

56. The CJEU has recognised the discretion afforded to Member States. In *Belgocodex,* it stated that "*the Member States have a wide discretion under Article 13B and C. It is for them to assess whether they should or should not introduce the right of option, depending on what they consider to be expedient in the situation existing in their country at a given time.*" In *VOS*, it stated that

> "*20. It is clear from those provisions that the taxation of leasing and letting transactions is a power which the legislature has conferred on the Member States in derogation from the general rule established in Article 13(B)(b) of the Sixth Directive, according to which leasing and letting transactions are, as a rule, exempt. The right to deduct does not therefore operate automatically in that context but only if the Member States have made use of the power under Article 13(C) of the Sixth Directive and subject to the taxpayers exercising the right of option allowed to them.*
>
> *21. As the Court has previously held, Member States may, by virtue of this power, allow persons benefiting from the exemptions provided for by the Sixth Directive to waive the exemption in all cases or within certain limits or subject to certain detailed rules. It follows that the Member States have a wide discretion under Article 13(B) and (C) of the Sixth Directive…"*

57. It is clear from those judgments that a member state may withdraw a right of option previously allowed (*Belgocodex*) and may make the exercise of that right subject to a process of prior approval (*VOS)*. While neither of those circumstances are applicable in this instance, it is important to bear in mind that the CJEU has confirmed that Member States have a "*wide discretion*" under Article 13B and C.

58. However, the CJEU has subsequently confirmed that "*when the Member States use their ability to restrict the scope of the right of option and to determine the arrangements for its exercise, they are to observe the general objectives and principles of the Sixth Directive, in particular the principle of fiscal neutrality…*" (*Turn- und Sportunion*). The Respondent contends that section 96 ensures that a person who did not waive exemption is treated equitably in comparison with a person who exercised a waiver and that waiver was subsequently cancelled, and that therefore the principle of fiscal neutrality is not breached.

59. In considering what the principle of fiscal neutrality requires, the Commissioner finds useful the explanation provided by the court in *Zimmermann*:

> "*46. In relation to those points, it should be borne in mind that, in the field of VAT, the concept of neutrality is used in different senses.*

47. On the one hand, recalling that the deduction mechanism provided for under the Sixth Directive is intended to relieve the trader entirely of the burden of the VAT payable or paid in the course of all his economic activities, the Court has held that the common system of VAT seeks to ensure neutrality of taxation of all economic activities, provided that those activities are themselves subject in principle to VAT…

48. On the other hand, according to settled case-law, the principle of fiscal neutrality means that supplies of goods or services which are similar, and which are accordingly in competition with each other, may not be treated differently for VAT purposes…"

60. While *Zimmermann* was not an Article 13C / Article 137 case, the Commissioner is not aware of the CJEU qualifying this interpretation of fiscal neutrality in any such case. Therefore, the Commissioner is satisfied that, when the court states that Member States are to observe the principle of fiscal neutrality in the application of Article 13C / Article 17, they are to observe it in the two senses set out in *Zimmermann.* He considers that the interpretation of the principle provided by the Respondent does not fully encompass these two senses.

61. There was no CJEU case opened that was on all fours with the facts in this appeal. However the Commissioner considers that the closest case referred to was *Imofloresmira.* In that case, the court considered a Portuguese law that provided for an adjustment of VAT initially deducted on the ground that a property had remained unoccupied for more than two years, even if the taxpayer had sought to rent it during that period. The court considered that the domestic law breached the principle of fiscal neutrality:

"*42. It follows from the case-law cited in paragraphs 39 and 40 above that a taxable person retains the right of deduction where that right has arisen, even if that taxable person could not, for reasons beyond its control, use the goods or services giving rise to the deduction in the context of taxed transactions.*

[…]

44. Therefore, the principle of fiscal neutrality precludes national legislation which, by making the final acceptance of the VAT deductions dependent on the results of the taxable person's economic activity, creates, as regards the tax treatment of identical investment activities, unjustified differences between undertakings with the same profile and carrying on the same activity."

62. It seems to the Commissioner that section 96(12) does what the CJEU has stated is impermissible. One taxpayer who deducts VAT and then successfully lets out a property will be treated differently to another taxpayer who similarly deducts VAT at the outset but

who is unsuccessful in attempts to let out a property, whether due to an economic downturn or some other reason beyond his control. The first taxpayer will not be required to pay a cancellation sum, or will pay a smaller sum, compared to the second taxpayer. This appears to constitute a breach of the principle of fiscal neutrality, as set out in *Imofloresmira,* and as explained by the CJEU in *Zimmermann* where its purpose is to *inter alia* "*relieve the trader entirely of the burden of the VAT payable or paid in the course of all his economic activities.*"

63. The Respondent submitted that section 96 restricted the scope of the right of option for taxation, rather than interfering with the consequences of waiving the exemption. Counsel argued that the sum was imposed after the waiver had been cancelled, and was therefore wholly different from the law considered in *Imofloresmira*, which applied an adjustment to the tax deducted for alleged change of use of a property. While the Commissioner accepts that the cancellation sum can only apply after a waiver has come to an end, he does not agree that this means that the principle enunciated in *Imofloresmira* is not applicable. Rather, he considers it necessary to consider the effect of the imposition of the cancellation sum.

64. In *Skellefteå*, the CJEU stated that

> "*The Court has also repeatedly stated that the right of deduction, once it has arisen, is retained, in principle, even if, subsequently, the planned economic activity was not carried out and, therefore, did not give rise to taxed transactions… or if, by reason of circumstances beyond his or her control, the taxable person did not make use of the goods and services which gave rise to a deduction in the context of taxed transactions… A limitation of VAT deductions connected with taxed transactions, after the right of option has been exercised, would not concern the 'scope' of the right of option which Member States may restrict by virtue of Article 137(2) of the VAT Directive, but the consequences of exercising that right…"*

65. The Commissioner considers that the clear effect of section 96 in this appeal is to place a limitation on VAT deductions by the Appellant in circumstances which it was not disputed were outside its control. He does not consider it of material significance whether this limitation occurs during the lifetime of the waiver or at its cancellation, as it does not appear that the jurisprudence of the CJEU discussed herein creates such a distinction. Consequently, the Commissioner considers that the limitation imposed by section 96 concerns the consequences of exercising the right to opt for taxation, rather than the scope of the right. In any event, the Commissioner notes that the CJEU has recently stated that

Member States are to observe the principle of fiscal neutrality when restricting the scope of the right of option; *Arvi.*

66. The Respondent argued that the rules governing the waiver of the exemption were clear and were available to the Appellant at the time of opting for the waiver, including the possibility that it would have to pay a cancellation sum. The Commissioner agrees that this is the case. However, he is satisfied that the CJEU's judgments in *Imofloresmira and Skellefteå* prohibited the limitation of the Appellant's VAT deductions after its waiver was granted, in circumstances where it was unable to let out the property from January 2009 until August 2015. He is further satisfied that the effect of section 96(12) was to limit the Appellant's VAT deductions in such a manner. Consequently, he is satisfied that section 96(12) is in breach of EU law and should be disapplied.

67. In *Commissioner of An Garda Síochána v Workplace Relations Commission* Case C-378/17 ("*WRC*"), the CJEU stated that

> "*38. As the Court has repeatedly held, that duty to disapply national legislation that is contrary to EU law is owed not only by national courts, but also by all organs of the State — including administrative authorities — called upon, within the exercise of their respective powers, to apply EU law…*
>
> *39. It follows that the principle of primacy of EU law requires not only the courts but all the bodies of the Member States to give full effect to EU rules*."

68. The jurisdiction of the Commission to apply EU law, in light of *WRC*, was considered by the Court of Appeal in *Lee v Revenue Commissioners* [2021] IECA 18. Murray J stated that

> "*The Workplace Relations Commission decision applies a principle of European law operative where a national tribunal is seized with a dispute, requiring that it give effect to the supremacy of European law in the course of determining that dispute. If a taxpayer wishes to contend that the application of a particular provision of the TCA breaches EU law, then the Appeal Commissioners must address that contention if it is relevant to the matter with which they are seised and, if it is appropriate and necessary to do so to decide that case, to disapply the provision or otherwise exercise their powers so as to ensure that EU law is not violated.*"

69. Consequently, the Commissioner is satisfied that he has jurisdiction to disapply section 96(12) of the VATCA 2010. He determines that section 96(12) should be disapplied and the assessment raised by the Respondent against the Appellant should be reduced to zero.

70. Finally, the Commissioner has considered whether, alternatively, the matter should be referred to the CJEU for a preliminary ruling. He is satisfied that he has discretion to refer a matter to the CJEU if he considers it appropriate to do so; *WRC*. He is cognisant of the submission of counsel for the Appellant that a reference at this stage would be preferable for his client compared with a potential reference from the High Court or Court of Appeal. Against this, he also notes that section 96 only applies to waivers created prior to 1 June 2008, and as stated by counsel for the Respondent, the section is mainly of historical relevance.

71. In *Wiener SI GmbH v Hauptzollampt Emmerich* Case C-338/95, Advocate General Jacobs commented that

> "*Excessive resort to preliminary rulings seems therefore increasingly likely to prejudice the quality, the coherence, and even the accessibility, of the case-law, and may therefore be counter-productive to the ultimate aim of ensuring the uniform application of the law throughout the European Union… Experience has shown that, in particular in many technical fields, such as customs and value added tax, national courts and tribunals are able to extrapolate from the principles developed in this court's case-law. Experience has shown that that case-law now provides sufficient guidance to enable national courts and tribunals – and in particular specialised courts and tribunals – to decide many cases for themselves without the need for a reference*."

72. The Commissioner considers that it is not necessary to refer this matter to the CJEU for a preliminary ruling. He considers that the court's case law quoted herein provides sufficient guidance to determine the appeal, and furthermore he considers that it would not be an efficient use of the CJEU's resources to refer consideration of a legislative provision that is of mainly historical interest.

Determination

73. In the circumstances, and based on a review of the facts and a consideration of the submissions, material and evidence provided by the parties, the Commissioner is satisfied that section 96(12) of the VATCA 2010 should be disapplied and the assessment to VAT for the period of 1 September 2017 – 31 December 2017 should be reduced to zero.

74. The appeal is hereby determined in accordance with section 949AK of the Taxes Consolidation Act 1997 as amended ("TCA 1997"). This determination contains full findings of fact and reason for the determination. Any party dissatisfied with the determination has a right of appeal on a point of law only within 42 days of receipt in accordance with the provisions set out in the TCA 1997.

Simon Noone

Appeal Commissioner
5th January 2023

The Tax Appeals Commission has been requested to state and sign a case for the opinion of the High Court in respect of this determination, pursuant to the provisions of Chapter 6 of Part 40A of the Taxes Consolidation Act 1997.