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DIRECTORATE-GENERAL
TAXATION AND CUSTOMS UNION
Indirect Taxation and Tax administration
Value added tax

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VALUE ADDED TAX COMMITTEE
(ARTICLE 398 OF DIRECTIVE 2006/112/EC)
WORKING PAPER NO 1061

QUESTION
CONCERNING THE APPLICATION OF EU VAT PROVISIONS

ORIGIN:	**Commission**
REFERENCE:	**Articles 168(e), 178(e) and 201**
SUBJECT:	**Importation of leased goods to be used for taxed activities – right to deduct VAT of the lessee**

1. INTRODUCTION

The VAT Committee discussed in its 98th meeting[1] the possibility for a lessee of imported goods to deduct the VAT paid upon the importation of those goods, when the lessee is designated as liable for the payment of such VAT.

The Commission services on that occasion concluded that the lessee of an imported aircraft is not entitled to deduct VAT in such situations. The conclusion was based on previous guidelines agreed by the VAT Committee[2], where it had been concluded that a taxable person designated as liable for the payment of import VAT pursuant to Article 201 of the VAT Directive is not entitled to deduct such VAT if he does not obtain the right to dispose of the goods as owner and the cost of the goods has no direct and immediate link with his economic activity. Neither of these conditions were fulfilled in the case at stake.

However, the Commission services are aware that some Member States are applying a different criterion to these situations, nevertheless granting a right to deduct the import VAT to the lessee. Furthermore, several rulings of the Court of Justice of the European Union (CJEU) have addressed situations whereby deduction of the VAT paid is allowed for persons who are not the owner of the goods. Therefore, the Commission services think that it is now necessary to clarify whether the conclusions reached in Working paper No 762 should be maintained.

2. SUBJECT MATTER

According to Article 201 of the VAT Directive, upon importation of goods, VAT shall be payable by any person or persons designated or recognised as liable by the Member State of importation. This option appears to be used in cases where the owner of the goods is not established within the EU, to designate the lessee of the goods as liable for the import VAT payment.

According to Article 168(e) of the VAT Directive, a taxable person shall be entitled to deduct the VAT due or paid in respect of the importation of goods into the Member State in which he carries out taxed transactions in so far as those goods are used for the purposes of those taxed transactions. The right to deduct VAT paid on the importation of goods should not be subject to additional substantive requirements. Further, Article 178(e) of the VAT Directive requires that the taxable person must hold an import document specifying him as consignee or importer, and stating the amount of VAT due or enabling that amount to be calculated.

The conditions laid down by Article 168(e) of the VAT Directive are the same as those required for the deduction in the case of VAT due or paid in respect of supplies of goods or services received or in respect of intra-Community acquisitions of goods made. The CJEU has ruled recently in various cases related to the right to deduct of a taxable person who had been charged VAT while not being the owner of the goods. Given that, from a substantive point of view, the conditions to deduct VAT paid upon importation of the goods are not different from those laid down in relation to the acquisition of goods and

[1] Working paper No 762 *Importation of leased goods for taxable activities*.
[2] See guidelines resulting from the 94th meeting of 19 October 2011 – Document A – taxud.c.1(2012)243615 – Working paper No 716 (p. 159).

services, the criteria established by the CJEU in those situations should, in principle, be applicable to the importation of goods in equal measure.

Therefore, the impact of these rulings on the possibility for the lessee of imported goods to deduct the VAT paid upon their importation should be further analysed.

3. COMMISSION SERVICES' OPINION

3.1. Recent case-law of the CJEU

Case C-132/16, *Iberdrola*[3] referred to a private investor, Iberdrola, who purchased several parcels of land in a holiday village in Tsarevo (Bulgaria), in order to construct apartment buildings for seasonal use together with further equipment. Iberdrola entered into a contract with the municipality of Tsarevo for the reconstruction of a waste-water pump station serving that holiday village and commissioned those works from a third party company. Following completion of the works, the buildings that Iberdrola planned to erect in the holiday village could be connected to the pump station. The supply of services made by Iberdrola to the municipality of Tsarevo was free of charge.

In its ruling the CJEU stated that "Article 168(a) of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax must be interpreted as meaning that a taxable person has the right to deduct input value added tax in respect of a supply of services consisting of the construction or improvement of a property owned by a third party when that third party enjoys the results of those services free of charge and when those services are used both by the taxable person and by the third party in the context of their economic activity, in so far as those services do not exceed that which is necessary to allow that taxable person to carry out the taxable output transactions and where their cost is included in the price of those transactions".

The CJEU considered that:

> "33. …**without the reconstruction of that pump station, it would have been impossible to connect the buildings which Iberdrola planned to build to that pump station**, with the result that that reconstruction was essential for completing that project and that, consequently, **in the absence of such reconstruction, Iberdrola would not have been able to carry out its economic activity**.
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> 34. Those circumstances are likely to demonstrate the existence of a direct and immediate link between the reconstruction service in respect of the pump station belonging to the municipality of Tsarevo and a taxed output transaction by Iberdrola, since it appears that the service was supplied in order to allow the latter to carry out the construction project at issue in the main proceedings.
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> 35. The fact that the municipality of Tsarevo also benefits from that service cannot justify the right to deduct corresponding to that service being denied to Iberdrola if the existence of such a direct and immediate link is established.

[3] CJEU, judgment of 14 September 2017, *Iberdrola*, C-132/16, EU:C:2017:683.

> 36. In that regard, it will be necessary to take into account the fact that the input reconstruction service at issue in the main proceedings is a component of the cost of a taxed output transaction by Iberdrola".

Therefore, according to this ruling, the right to deduct VAT in relation to costs incurred by a taxable person is dependent upon whether the costs incurred are necessary in order for the taxable person to carry out his or her economic activity and whether those costs are included in the price of the output transactions. If those conditions are fulfilled, the direct and immediate link between the VAT paid and the economic activity of the taxable person is demonstrated. The CJEU later reached the same conclusion in a very similar case[4].

Further, in case C-405/19, *vos Aanemingen*[5] the CJEU confirmed that the fact that expenditure incurred by a taxable person, in connection with his economic activity, also benefits a third party, does not preclude that taxable person from deducting in full the input VAT paid on that expenditure where, firstly, there is a direct and immediate link between that expenditure and the taxable person's economic activity and, secondly, the benefit to the third party is ancillary to the taxable person's business purposes.

Other judgments are however relevant for the issue of deduction when it comes to the importation of goods by a lessee.

In case C-187/14, *DSV Road*[6], the CJEU on the right to deduct in connection with import stated the following:

> "48. By its fourth question, the referring court asks, in essence, whether Article 168(e) of the VAT Directive must be interpreted as precluding national legislation which excludes the deduction of VAT on import which the carrier, who is neither the importer nor the owner of the goods in question and has merely carried out the transport and customs formalities as part of its activity as a transporter of freight subject to VAT, is required to pay.
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> 49. In that regard, it must be noted that, under the wording of Article 168(e) of the VAT Directive, a right to deduct exists only in so far as the goods imported are used for the purposes of the taxed transactions of a taxable person. In accordance with the settled case-law of the Court concerning the right to deduct VAT on the acquisition of goods or services, that condition is satisfied only where the cost of the input services is incorporated either in the cost of particular output transactions or in the cost of goods or services supplied by the taxable person as part of his economic activities (see judgments in SKF, C-29/08, EU:C:2009:665, paragraph 60, and Eon Aset Menidjmunt, C-118/11, EU:C:2012:97, paragraph 48).
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> 50. Since the value of the goods transported does not form part of the costs making up the prices invoiced by a transporter whose activity is limited to transporting those goods for consideration, the conditions for application of Article 168(e) of the VAT Directive are not satisfied in the present case.
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> 51. It follows from all the foregoing considerations that the answer to the fourth question is that Article 168(e) of the VAT Directive must be interpreted as not

4 CJEU, judgment of 16 September 2020, *Middledeutsche Harstein*, C-528/19, EU:C:2020:712.
5 CJEU, judgment of 1 October 2020, *vos Aanemingen*, C-405/19, EU:C:2020:785.
6 CJEU, judgment of 25 June 2015, *DSV Road*, C-187/14, EU:C:2015:421.

precluding national legislation which excludes the deduction of VAT on import which the carrier, **who is neither the importer nor the owner of the goods** in question and has merely carried out the transport and customs formalities as part of its activity as a transporter of freight subject to VAT, is required to pay."

In this case, the CJEU denied the right to deduct the VAT paid by the transporter, but confirmed the conditions for the right to deduct VAT in relation to costs incurred by a taxable person: the costs incurred are necessary in order for the taxable person to carry out his or her economic activity and these costs are included in the cost of the output transactions.

3.2. Impact on the importation of leased goods where the lessee is designated as liable for payment of import VAT (**imported leased aircraft**)

We will now analyse if the abovementioned conditions can be said to be fulfilled when the lessee is designated as liable for payment of the import VAT due on the leased goods.

First, the lessee is the importer of the goods. According to Article 178(2) of the VAT Directive, as far as the formal conditions for deduction are concerned, it appears that these are fulfilled when the lessee holds an import document specifying him as importer and stating the amount of VAT due or enabling that amount to be calculated.

According to the abovementioned case law, the substantive conditions to deduct VAT must be seen as fulfilled if the taxable person complies with the following two prerequisites:

a) The costs incurred are necessary in order to carry out the economic activity of the taxable person.

b) These costs are included in the cost of his output transactions.

This last condition does not seem to be fulfilled in cases where the importer is the lessee of the goods. With regard to the particular case examined in Working paper No 762, it was stated that the lessee does not actually bear the (overall) costs of the aircraft, simply the amount of the lease to be paid to the owner. Therefore, while the costs of the lease are included in the price of the output transaction of the lessee, that is not the case with the costs of the aircraft itself. The costs of the aircraft are costs for the owner, who passes them on to the lessee as part of the price charged for the lease. We would thus be duplicating that component of the cost for the lessee if we were to consider that the costs of the aircraft are included in the price of the output transactions of the lessee. The costs of the aircraft are borne by the owner only, not by the lessee.

The CJEU followed this reasoning in its Order in case C-621/19 *Weindel Logistik Service*[7]. In this case, an EU company was importing into the EU goods to recondition them. Once the reconditioning operations had been performed, the goods were sold into the EU or exported to third countries. The importer, the EU company, invoiced the reconditioning services to the owner of the goods, a company established in Switzerland. The CJEU considered that a right to deduct could not be granted to an importer who does not dispose of the goods as an owner and where the costs incurred are not included in the

[7] CJEU, order of 8 October 2020 in case 621/19, *Weindel Logistik Service*, EU:C:2020:814.

cost of the output transactions of the importer. The CJEU also referred to the guidelines agreed by the VAT Committee, which follow the same criterion[8].

Further, the lease in question is an operational lease type. Under the EU framework (Regulation (EU) No 965/2012[9] and Regulation (EC) No 1008/2008[10]), such leases are clearly regulated. There are two potential lease types: wet lease (lease of aircraft and crew) and dry lease (lease of aircraft only).

This specific framework provides that "*in order to avoid excessive recourse to lease agreements of aircraft registered in third countries, especially wet lease, these possibilities should only be allowed in exceptional circumstances, such as a lack of adequate aircraft on the Community market, and they should be strictly limited in time and fulfil safety standards equivalent to the safety rules of Community and national legislation*"[11]. As a result, these leasing agreements are subject to strict time-limits.

These elements are relevant for the VAT analysis as they determine the economic background of the transaction. Under these circumstances, allowing a full deduction to the lessee would be disproportionate as the latter will upfront deduct the entire import VAT for the value of the aircraft which the lessee may only use for a very limited period of time. Allowing the deduction to the lessee could lead to problems with the adjustments of the VAT deduction required in cases where the owner, after expiry of the lease, puts this non-EU aircraft to private or more generally non-business uses.

Moreover, the cases of aircraft lease where the aircraft is being brought into the EU under temporary admission with partial relief from customs duties should generally qualify for the exemption from VAT provided under Article 148(f) of the VAT Directive, as most airline companies which are likely to be the lessee carry out international transport. The types of leases for which payment of VAT is required (only domestic transport, utilitarian domestic flights, etc.) are expected to be marginal.

Therefore, the Commission services are of the view that the previous conclusions expressed in Working paper No 762 should be maintained. For the importer to be allowed to deduct the VAT paid on the importation of goods, the goods imported must be necessary to carry out the economic activity of the taxable person and the costs of the importation need to be included in the cost of his output transactions. In the case of importation of an aircraft by the lessee, while the first condition is fulfilled, the second is not, as only the price of the lease and not the costs of the importation of the aircraft are included in the cost of the lessee's output transaction.

In these cases, in order to allow for the deduction of the VAT paid upon importation, Member States could use the margin of discretion granted by Article 201 of the VAT Directive and designate the owner as the importer and, therefore, the person being liable for VAT. This possibility would allow for the owner to deduct the VAT paid upon importation of the aircraft to the extent that it is used for the purposes of economic

8 See footnote 2.

9 Commission Regulation (EU) No 965/2012 of 5 October 2012 laying down technical requirements and administrative procedures related to air operations pursuant to Regulation (EC) No 216/2008 of the European Parliament and of the Council (OJ L 296, 25.10.2012, p. 1).

10 Regulation (EC) No 1008/2008 of the European Parliament and of the Council of 24 September 2008 on common rules for the operation of air services in the Community (OJ L 293, 31.10.2008, p. 3).

11 Regulation (EC) No 1008/2008, recital 8.

activities, allowing to adjust the initial deduction in the case there is a subsequent change in the use of the aircraft.

Further, given the specific legislative framework within which these operations on aircraft take place, and their economic reality, the impact of denying the right to deduct VAT to the lessee on importation should be rather limited. It also reduces the possibilities for abuse, and minimises the difficulties in regularising the VAT deducted when the aircraft, after expiry of the lease, is put to uses which do not give rise to the right to deduct VAT.

4. DELEGATIONS' OPINION

The delegations are requested to give their opinion on this matter.

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