



Newsletter n. 2/2014

**The position of the Court of Justice on the denial of VAT deduction for “awareness” continues, albeit with greater guarantees in cases of subjectively non-existent operations. And the legal uncertainty on the “sentinel tax” taxpayer, together with the failure to meet the EU rules, still remain.**

With the *Maks Pen EOOD* judgement of February 13, 2014 (C-18/13), related to the facts occurred in Bulgaria, the Court of Justice pronounces again on the denial to deduct VAT for awareness, as in the previous judgement *Axel Kittel* of July 6, 2006 (C-439/04 e 440/04).

However, unlike the *Axel Kittel* judgement (when it came to real operations with omitted VAT payment), in this case the facts relate to financial transactions allegedly fictitious, according to the Bulgarian financial administration .

At par. 27 the Court of Justice states that there is a misuse of the right to deduct even in the case in which "a taxable person knew or should have known that, by his purchase, he took part in an operation that was connected with VAT evasion" by recalling, as a basis of this approach, the *Bonik* judgement (C-285/11), par. 38-39. Such a judgement, in turn, cites the *Axel Kittel* sentence of 2006, which first stated the refusal to deduct VAT for “awareness”.

Two remarks can be made in relation to this recent ruling.

- On the one hand it innovates, if compared to *Axel Kittel*, in terms of the **guarantees of the right to deduct**. *Maks Pen* is not limited to the denial of the right to deduct for mere awareness of participating in the fraudulent conduct of others (as stated in the final part of *Axel Kittel*). The denial of VAT deduction is subject to the double condition *a*) that the service is provided by a different supplier (fact inferable, among other things, from the lack of personnel, of material resources and of the necessary assets) **and** *b*) that the taxable person was aware of the supplier's fraudulent behavior.

In this respect, taking into account that the “denial of deduction for awareness” is often invoked in the hypothesis of subjectively non-existent operations, the *Maks Pen* judgment is certainly to be considered positively.

Firstly, the financial administration will have to prove the diversity of the supplier (objective element), and only secondly also the existence of the subjective element.

- The second remark concerns **the relationship between the judgments of the Court of Justice and the primary sources of the Community law**.

It seems clear that the *Maks Pen* judgement applies to the letter the denial of deduction for “awareness” created by the *Axel Kittel* judgement. This is in fact recalled by

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the *Bonik* sentence, which is often cited by *Maks Pen*. The *Bonik* judgement is also recalled, even more recently, by the *Firin OOD* sentence of March 13, 2014 (par. 40-42-44-45).

With respect to these references of previous judgements, and in the absence of a legal text as a basis of the prediction of such an anti-fraud measure, the Italian legal system seems to belong to a *common law* system where the principle of the *stare decisis* prevails.

But in the Italian legal system the principle of legality still prevails, for constitutional choice.

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The judgments of the Court of Justice, nevertheless, provide useful insights.

The judge of the *Maks Pen* judgement is aware of the need for the Community law to be based on the primary sources (Treaty, Directives and Regulations) .

We read at par. 36 of such judgement that “*the national court is bound to interpret the domestic law, as far as possible, in the light of the wording and purpose of the directive ...*”

From the text of the Sixth Directive, as well as from that of the Directive of 2006, no principle of denial of deduction based on a subjective element can be inferred.

On the contrary, what can be inferred is that the derogations to the Directive are up to the Member States<sup>1</sup>, *ergo* with Parliamentary intervention.

The judge of the sentence *Firin OOD*, has clearly stated, at par. 29, that the appeal to the Court of Justice is “*an instrument of cooperation between the Court and the national courts, by means of which the Court provides the national courts with the points of interpretation of the Union law that they need to solve the dispute they are called upon to settle*”.

The duty to comply with the provisions of the law, and above all with the principle of legality is still, therefore, in the hands of the national court.

Edited by  
Giovanni Moschetti

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<sup>1</sup> E.g. art. 27, n.1, of the Sixth Directive provides that “*the Council, acting unanimously on a proposal from the Commission, may authorize each Member State to introduce special measures for derogation to this Directive in order to simplify the tax collection or to prevent tax fraud or evasion*”.