Cross-border juridical VAT double taxation in the framework of European law[*]

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Overview

The thesis deals with the topic of cross-border juridical VAT double taxation within the framework of EU primary law. While double taxation is a recognised problem in the area of direct tax law and numerous mechanisms have been implemented in the past to address it, awareness of the issue in the area of VAT is almost non-existent. Considering the increasing globalisation and the fact that over 170 countries worldwide levy some kind of VAT,[1] the likelihood of double taxation of turnover increases significantly.

The thesis describes the phenomenon of VAT double taxation, causes and constellations in which it occurs, and evaluates it from the perspective of EU fundamental freedoms and EU fundamental rights. Subsequently, proposals for cross-border dispute resolution mechanisms to resolve VAT double taxation are presented and the necessary competences for their introduction are assessed.

Core results

The concept of "double taxation", constellations and causes

The thesis shows that the definitions of the concept of "double taxation" used in the area of direct tax law cannot be applied to VAT. Therefore, an independent definition was developed for VAT. One can distinguish between two types of VAT double taxation: (i) On the one hand, juridical VAT double taxation, i.e. multiple taxation of the same transaction in several states through a multiplication of the places of supply. In the mirror-image situation, double non-taxation can also arise, i.e. a complete absence of taxation of a transaction in all states involved in the transaction. (ii) On the other hand, economic double taxation, i.e. one state levying VAT on a transaction and another state denying input tax deduction on input services received.[2] Subsequently, the thesis only dealt with juridical double taxation.

Juridical VAT double taxation can arise in intra-EU constellations and in mixed constellations. There is a variety of causes for juridical double taxation in both types of constellations. One can differentiate between double taxation due to divergent rules and double taxation despite identical rules.[3] Simply

[*] This document contains a summary of the main findings of the author's doctoral thesis written under the supervision of Prof. Karoline Spies and approved in April 2022. For a complete list of sources used in the course of the analysis, see the published version of the thesis: A. Streicher, *Cross-Border Juridical VAT Double Taxation in the Framework of European Law*, IBFD 2023.

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[1] Comparable taxes at the global level include the Goods and Services Tax (GST), which is levied in Australia, Canada, New Zealand, Singapore, Hong Kong, Malaysia and India, among others, and the Sales Tax, which is levied in the USA, among others.

[2] For a comprehensive overview of the concept of VAT double taxation see, e.g., R. Ismer & K. Artinger, *International Double Taxation under VAT: Causes and Possible Solutions*, Intertax 2017, 595.

[3] See, e.g., R. Ismer & K. Artinger, *International Double Taxation under VAT: Causes and Possible Solutions*, Intertax 2017, 595 (598); J. Englisch, *Wettbewerbsgleichheit im grenzüberschreitenden Handel mit Schlussfolgerungen für indirekte Steuern*, Mohr Siebeck 2008, 772; K. Spies, *Dispute Resolution in VAT: Status Quo under the EU VAT Directive and Room for Improvement*, in CJEU – Recent Developments in Value Added Tax 2006, Linde 2017, 93 (93); T. Ecker, *Digital Economy International Administrative Cooperation and Exchange of Information in the Area of VAT*, in VAT/GST in a Global Digital Economy, Kluwer 2015, 141 (158).

speaking, double taxation due to divergent rules is rooted at the level of the law. Double taxation despite identical rules, on the contrary, is rooted at the level of the tax administration or the judiciary.

In intra-EU constellations, double taxation can arise due to divergent rules, i.e. caused by the diverging domestic implementation of identical provisions or by limits to harmonization in the VAT Directive. However, in such constellation, double taxation mostly arises despite identical rules, i.e. due to deviating interpretations or applications of the same rule.[4] When considering ECJ case law on cases of VAT double taxation, it becomes apparent that the VAT rules in the involved Member States are generally alike but that the problem is that they are interpreted differently or that facts of the case are not appreciated in the same way. Double taxation due to divergent rules is rather the exception in the VAT field in intra-EU constellations even though it occurs again and again that Member States implement provisions of the VAT Directive incorrectly. In the system of a harmonized VAT, there is little room for divergent rules, but it cannot be excluded; a recent example is the incorrect implementation of the Tour Operators Margin Scheme (TOMS) in Austria. However, in most intra-EU cases, double taxation arises despite identical rules specifically because these rules are interpreted or applied differently.

In mixed constellations, double taxation presumably mostly arises due to divergent rules, i.e. because the EU VAT system and the VAT system of the non-EU states are not entirely congruent. Double taxation can, nevertheless, also arise despite the use of identical principles in such constellations because, also here, identical principles or the facts of a case might be appreciated in a deviating way by the involved tax authorities.[5] In this respect, intra-EU constellations and mixed constellations are not at all different. Of course, these two categories of cases are to be treated differently when it comes to the mechanisms available for their resolution.

Existing VAT dispute resolution mechanisms

Against all odds, VAT double taxation exists and can arise in intra-EU constellations as well as in mixed constellations. Currently, there is a lack of mechanisms for effectively resolving VAT double taxation. Domestic mechanisms such as proceedings before domestic courts, domestic arbitration, and unilateral waiver of taxing rights lack a cross-border element and are thus not a reliable aid. There are no mechanisms in international law at all. One mechanism in EU law, namely, the preliminary ruling procedure under Article 267 TFEU, is a promising option to resolve VAT double taxation in intra-EU constellations and most probably also serves this aim in many cases. However, this mechanism also has some downsides because the taxpayer does not have a subjective right to its initiation, it cannot involve more than one Member State at once, and it cannot help to solve cases of VAT double taxation resulting from a diverging appreciation of facts.[6] Consequently, it was analysed further which other mechanisms could effectively resolve cross-border VAT double taxation in intra-EU and mixed constellations.

The relationship of juridical VAT double taxation to the EU fundamental freedoms

Neither Article 110 TFEU nor the fundamental freedoms (in particular the free movement of goods and the freedom to provide services) can effectively resolve juridical VAT double taxation. Due to the shielding effect of the VAT Directive,[7] the fundamental freedoms only are a yardstick in cases of

[4] See, e.g., European Commission, *Consultation Paper: Introduction of a mechanism for eliminating double imposition of VAT in individual cases*, TAXUD/D1/…., 5 January 2007, 3.
[5] See, e.g., P. Rendahl, *EU VAT and Double Taxation: A Fine Line between Interpretation and Application*, Intertax 2013, 461.
[6] For an overview see, e.g., K. Spies, *Dispute Resolution in VAT: Status Quo under the EU VAT Directive and Room for Improvement*, in CJEU – Recent Developments in Value Added Tax 2006, Linde 2017, 93.
[7] See, e.g., A. Cordewener, *Der sachliche, persönliche und territoriale Anwendungsbereich der Grundfreiheiten*, in Europäisches Steuerrecht, Verlag Dr. Otto Schmidt 2018, 203; R. Szudoczky, *The Sources of EU Law and Their Relationships:*

juridical VAT double taxation caused (i) by the VAT Directive itself or (ii) by a faulty implementation of the VAT Directive by a Member State. It can be assumed that the former case does not occur anymore due to the well-advanced technical sophistication and refinement of the place of supply rules in the Directive. The latter case, on the contrary, can be assumed to occur more often. However, in the latter case, the taxpayer is dependent on Member State courts to refer his case to the ECJ – and, if a case is referred to the ECJ, the double taxation issue will often already be resolved in the course of the procedure. In cases of VAT double taxation that can be traced back to a differing interpretation of rules or facts by the Member States, the fundamental freedoms are not a benchmark due to the shielding effect of the VAT Directive.

At first sight, this result seems bizarre. Double income taxation can be measured against the fundamental freedoms. While a review based on the fundamental freedoms is possible for these non-harmonized taxes, it is subject to tight restrictions when it comes to *the* harmonized tax: VAT. However, after all, this outcome is not that strange at all as the VAT Directive not only pursues the isolated aim of harmonizing VAT across the EU but, as an act of secondary law, serves the greater goal of substantiating the fundamental freedoms and creating the common market. Consequently, in an ideal world, there would be no VAT double taxation within the EU, and it would not be necessary to directly rely on the fundamental freedoms.

What is more, the mere observation that VAT double taxation infringes the fundamental freedoms is not sufficient because it is necessary to allocate responsibility to one Member State. Consequently, it must be determined which Member State must restrict its own taxing right in order to effectively resolve the double burden imposed upon the taxpayer. There are constellations for which this determination is easier, i.e. constellations in which double taxation clearly is the fault of one Member State. This is the case when double taxation is a result of a faulty domestic implementation of a provision of the VAT Directive or the result of a Member State ignoring ECJ jurisprudence.

In all other cases, the allocation of the responsibility to resolve double taxation is not that easy. In proceedings before the ECJ, only the incriminated domestic provision is on trial – thus, even if double taxation is the result of the interplay of multiple Member States' domestic provisions, the Court leaves the responsibility with the one state for which the provision is the subject of the procedure. In the *Schul*[8] decision, the Court allocated the duty to resolve double taxation to the import/destination state. However, if the duty to resolve double taxation was automatically allocated to the second state to tax, this would result in "first-come-first-tax" which cannot be a desired condition. In direct tax case law, the ECJ also mentioned that OECD materials such as the Model Convention and Commentary can be consulted for the allocation of taxing rights.[9] This approach could be transferred to the VAT area insofar as the OECD VAT/GST Guidelines contain place of supply rules that could be used as a compromise solution.

Concludingly, the allocation of the responsibility to resolve double taxation, i.e. to stand down from levying VAT, is a tricky issue that demands a solution. Under the current status of EU law, no such solution is available.

The relationship of juridical VAT double taxation to EU fundamental rights

Lessons for the Field of Taxation: Primary Law, Secondary Law, Fundamental Freedoms and State Aid Rules, IBFD 2014, 7.2.1.

[8] CJEU 5 May 1982, C-15/81, *Schul*.

[9] See, e.g., G. Kofler, *Doppelbesteuerungsabkommen und Europäisches Gemeinschaftsrecht*, Linde 2007, 235 et seqq; J. Englisch, *The European Treaties' Implications for Direct Taxes*, Intertax 2005, 313 (324).

The right to property according to Art. 17 CFR prohibits juridical VAT double taxation. A distinction must be made between (i) the existence of an infringement of the fundamental right and (ii) a possible justification of the infringement. Juridical VAT double taxation undoubtedly constitutes an infringement of the right to property, because the same transaction is taxed twice and the taxable person cannot pass on this double tax to the recipient of the goods or service but must bear it himself.

For the assessment of a possible justification of the infringement, a distinction must be made between (i) unlawful and (ii) lawful juridical VAT double taxation.[10] (i) Unlawful juridical VAT double taxation arises from an incorrect transposition of the VAT Directive in a Member State or failure to comply with ECJ case law. This category has an overlap with the above-mentioned category of juridical VAT double taxation due to divergent rules. Unlawful juridical VAT double taxation cannot be justified.

(ii) Lawful juridical VAT double taxation, on the other hand, occurs in cases where a divergent interpretation of rules or assessment of facts leads to double taxation. This category shows an overlap with the above-mentioned category of juridical VAT double taxation despite identical rules. Such interference with the right to property could be justifiable if it is in the public interest and proportionate. However, it is highly doubtful whether there is any reason in the public interest that could justify double taxation. Moreover, legal double taxation of VAT is disproportionate because it imposes an excessive burden on the taxable person. This follows from the facts that, according to its conception, VAT is not supposed to affect the economic capacity of the taxable person and, in addition, no mechanisms exist to combat VAT double taxation.

Of course, also in this area, the practical problem of which state is responsible for resolving the double taxation remains unanswered. In cases of unlawful double taxation, e.g., because a Member State has implemented a provision of the VAT Directive incorrectly, the apportionment of responsibility is easy. However, in cases where each state has acted correctly but where, e.g. VAT systems are incoherent in mixed constellations, such apportionment of responsibility is generally not possible.[11] Thus, in the next chapter, potential VAT dispute resolution mechanisms were discussed that might facilitate the effective resolution of VAT double taxation.

The EU's competence to implement dispute settlement mechanisms

Should the EU institutions wish to take up the problem of juridical VAT double taxation and implement mechanisms for its resolution, the question arises whether the EU has the necessary competences to do so. Three possible mechanisms for intra-EU constellations were analysed: (i) The first possibility is the introduction of a mutual agreement/arbitration procedure in the VAT Directive. For this, the EU has shared competence under Art. 113 TFEU. (ii) The second option is to extend the scope of the EU Dispute Resolution Directive so that it covers not only tax disputes in the area of direct tax law, but also disputes in the area of VAT. The EU also has shared competence for this under Art. 113 TFEU. (iii) A third possibility is to grant taxpayers a subjective right to initiate a preliminary ruling procedure before the ECJ. This is possible by amending the EU Treaties accordingly. A major shortcoming of all the options mentioned is that unanimity between the Member States is required, i.e. a single member state could hinder the implementation of such mechanisms.

One mechanism was analysed for mixed constellations: The conclusion of VAT double taxation agreements with third countries, through which taxation rights are divided between the states involved and a

[10] F. Debelva, *International Double Taxation and the Right to Property: A Comparative, International and European Law Analysis*, IBFD 2019, 10.2.
[11] See also F. Debelva, *International Double Taxation and the Right to Property: A Comparative, International and European Law Analysis*, IBFD 2019, 10.3.

mutual agreement/arbitration clause is introduced.[12] The EU has the exclusive external competence to conclude a VAT DTC with third states to counter VAT disputes in mixed constellations. This competence arises from the *AETR*[13] jurisprudence that is codified in Article 216, paragraph 1, 4th option TFEU. This competence is exclusive pursuant to Article 3, paragraph 2, 3rd option TFEU because the subject matter of the international agreement coincides largely with internal VAT legislation. Thus, isolated Member State action would affect this internal legislation. The EU is exclusively competent to conclude VAT DTCs with third states. A major drawback of this tool, however, is that it requires a myriad of bilateral negotiations between the EU and individual third states unless the EU and a significant number of third states could agree on the conclusion of a multilateral VAT DTC. A follow-up question when it comes to VAT DTCs concluded by the EU is the question on their relationship to the VAT Directive – what if the VAT DTC contains rules that conflict with rules of the VAT Directive? If the VAT Directive and the VAT DTC were applicable to the same transaction, the rules of the VAT DTC would have to be applied primarily. However, most likely, the EU would not conclude a VAT DTC that contains rules that are not compatible with the VAT Directive or, if so, the VAT DTC would contain a type of collision rule. This would also conform with a basic idea of implied external competences, i.e. the EU shall have competence to act externally so as to avoid contradictions with internal legislation.

Arbitration as a possible solution for juridical VAT double taxation

VAT arbitration both in intra-EU constellations and in mixed constellations might, under certain circumstances, be in line with the ECJ's exclusive jurisdiction. In intra-EU constellations, the decisions of the arbitration panel must be subject to review by domestic courts that can initiate preliminary ruling procedures under Article 267 TFEU, or the arbitration panel itself must be able to refer cases to the ECJ or the ECJ must act as an arbitrator. In mixed constellations, the ECJ's exclusive jurisdiction as a knock-out argument against arbitration was significantly restricted in Opinion 1/17.[14] It seems to be possible to install an arbitration system under a VAT DTC concluded between the EU and a third state. Even if the arbitral awards are not subject to review by the ECJ, this does not necessarily collide with the ECJ's exclusive jurisdiction.

The way forward

The thesis has clearly shown that VAT double taxation exists and that it is a serious problem under EU primary law. It might only rarely occur in intra-EU constellations but, as soon as a transaction includes EU states and non-EU states, one and the same transaction is prone to double taxation. This hampers the international trade in goods and services and distorts competition. This problem has not remained hidden from the EU Commission, and it first started a public discussion on the topic in 2007.[15] In its 2020 Action plan for fair and simple taxation, the Commission states:

> *Mechanisms to prevent and to solve disputes concerning the implementation of the VAT Directive are needed at every stage of the VAT transaction life cycle to ensure the VAT principles of legal certainty, neutrality and fairness. The Commission will*

[12] The idea of a VAT/GST model convention was largely developed by Thomas Ecker, see T. Ecker, *A VAT/GST Model Convention*, IBFD 2013.
[13] CJEU 31 March 1971, C-22/70, *Commission of the European Communities v Council of the European Communities European Agreement on Road Transport;* for an overview of the topic see, e.g., C. Heber, *Die Kompetenzverteilung im Rahmen der Austrittsverhandlungen nach Art. 50 EUV unter besonderer Berücksichtigung bestehenden Sekundärrechts*, Europarecht 2017, 581.
[14] CJEU 30 April 2019, Avis 1/17, *Accord ECG UE-Canada*; see also P. Pistone & A. Papulova, *Arbitration Procedure and the Implementation of Arbitral Awards in Domestic Law*, in Tax Treaties and Procedural Law, IBFD 2020, 177.
[15] European Commission, Consultation Paper: Introduction of a mechanism for eliminating double imposition of VAT in individual cases, TAXUD/D1/…., 5 January 2007.

> *examine* [in 2022/23] *all options and, where appropriate, it will come forward with a legislative proposal on a prevention and dispute resolution mechanism for VAT.*[16]

The outcome of this process can be curiously awaited, especially as regards the possible legislative proposal. It is the author's expectation that the Commission will propose the introduction of a MAP/arbitration mechanism into the VAT Directive. It is unclear whether the Commission will also propose a mechanism for mixed constellations. The phrase "disputes concerning the implementation of the VAT Directive" rather points at intra-EU constellations that the Commission wants to tackle. It is rather unlikely that the Commission will also promote a mechanism for mixed constellations. After all, the Commission needs to start somewhere and it is rather obvious to start with intra-EU constellations that can be regulated by internal legislation, then evaluate the outcome and afterwards try to resolve the next problem. Also, any proposal for resolving VAT disputes in mixed constellations will inevitably hit a politically sensitive point. The past years have shown that it triggers considerable political frictions between the EU and its member states whenever the EU tries to use external treaty making powers. In consequence, it seems rather unlikely that the Commission will come forward with a proposal for VAT dispute resolution for mixed constellations in the nearer future. However, in the author's opinion it is inevitable to think about the future of global VAT dispute resolution, because the issue's seriousness will not vanish into thin air by itself. Mechanisms to resolve double taxation in income taxation have already been taken in the 19th century. The 21st century is the right time to do the same for VAT.

[16] European Commission, *Communication from the Commission to the European Parliament and the Council, An action plan for fair and simple taxation supporting the recovery strategy*, COM(2020) 312 final, 15 July 2020, 14.