JUDGMENT OF THE COURT
28 June 1988 *

In Case 3/86

Commission of the European Communities, represented by Johannes Føns Buhl, Legal Adviser to the Commission, and Guido Berardis, a member of its Legal Department, acting as Agents, with an address for service in Luxembourg at the office of G. Kremlis, a member of the Commission's Legal Department, Jean Monnet Building, Kirchberg,

applicant,

v

Italian Republic, represented by Ivo M. Braguglia, avvocato dello Stato, with an address for service in Luxembourg at the Italian Embassy,

defendant,

APPLICATION for a declaration that the Italian Republic has failed to fulfil its obligations under Community provisions and, in particular, Article 25 (3) and (5) of the Sixth Council Directive (77/388/EEC) of 17 May 1977, on the harmonization of the laws of the Member States relating to turnover taxes — Common system of value-added tax: uniform basis of assessment (Official Journal 1977, L 145, p. 1),

THE COURT,

composed of: Lord Mackenzie Stuart, President, G. Bosco, J. C. Moitinho de Almeida and G. C. Rodríguez Iglesias, Presidents of Chambers, T. Koopmans, U. Everling, Y. Galmot, C. Kakouris and F. Schockweiler, Judges,

Advocate General: C. O. Lenz
Registrar: B. Pastor, Administrator

having regard to the Report for the Hearing and further to the hearing on 13 January 1988,

* Language of the Case: Italian.

after hearing the Opinion of the Advocate General delivered at the sitting on 24 February 1988,

gives the following

Judgment

1 By application lodged at the Court Registry on 9 January 1986, the Commission of the European Communities brought an action under Article 169 of the EEC Treaty for a declaration that, by introducing and maintaining in force a flat-rate scheme which is incompatible with Article 25 (3) and (5) of the Sixth Directive (Council Directive 77/388/EEC of 17 May 1977, Official Journal 1977, L 145, p. 1) as regards the unlimited nature of that scheme and the rate of value-added tax (VAT) refunds paid to producers of beef, pork and unconcentrated and unsweetened fresh milk, the Italian Republic has failed to fulfil its obligations under the EEC Treaty and the Sixth Directive.

2 Acting pursuant to Article 34 of Decree No 633 of the President of the Republic of 26 October 1972 introducing value-added tax (*Official Journal of the Italian Republic* No 292, 11.11.1972), Italy established a flat-rate scheme for farmers. In the context of this scheme, the legislature made use of the possibility provided for in Article 25 (3) of the Sixth Directive by laying down a series of flat-rate compensation percentages, which varied according to the different subdivisions of agriculture and groups of products. By a Ministerial Decree of 25 February 1983 (*Official Journal of the Italian Republic* No 58, 1.3.1983), the flat-rate percentage was set at 14%, with effect from 1 March 1983 for beef and pork as well as for unconcentrated and unsweetened fresh milk. That percentage represented a reduction in the rate of 15% previously applied to those categories of products under Law No 889 of 22 December 1980 (Ministerial Decree of 5 January 1981).

3 The Commission claims that the Italian Republic has failed to comply with its obligations in three respects: by the use, in fixing the flat-rate compensation

percentages, of statistics relating to agriculture as a whole, whereas Article 25 (3) of the Sixth Directive provides that such percentages are to be based on macro-economic statistics for flat-rate farmers alone; by the incorporation in the flat-rate scheme in question of the supply of goods and services to flat-rate farmers, whereas, under Article 25 (5) of the Sixth Directive, the flat-rate compensation percentages must be applied only to goods and services which flat-rate farmers have supplied to taxable persons other than flat-rate farmers; and by fixing at too high a level the compensation percentages for beef, pork and milk, which has the effect of affording flat-rate farmers refunds greater than the VAT charged on inputs.

4 Reference is made to the Report for the Hearing for a fuller account of the facts of the case, the course of the procedure and the submissions and arguments of the parties, which are mentioned hereinafter only in so far as is necessary for the reasoning of the Court.

5 It should be observed at the outset that the complaint that account was taken of macro-economic statistics relating to the whole of agriculture for determining the flat-rate compensation percentages payable to producers of beef, pork and fresh milk is subsumed in the complaint that those percentages were set at too high a level. The Commission alleges that the defendant fixed the percentages in question first at 15%, then at 14%, whereas, having regard to the statistics mentioned in Article 25 (3) of the Sixth Directive, they should have been fixed at around 7%.

The complaint that the flat-rate compensation percentages for beef, pork and fresh milk were set at too high a level

6 In setting the flat-rate compensation percentage at 14%, the defendant stated that it based itself on macro-economic statistics relating to the whole of agriculture but was obliged to correct them so as to take account of the specific structure of the Italian stock-farming sector. It pointed out that the large number of small farms carrying on both stock rearing and arable farming use means of production whose high costs are not always perceptible in statistical surveys but nevertheless entail

considerable VAT input charges. It also stated that if the aforesaid percentages had represented for flat-rate farmers a rate of refund higher than the VAT charges on inputs, they would necessarily have brought about an increase in relevant production, whereas the contrary is evidenced both by the steady and progressive reduction in the rate of self-sufficiency recorded in Italy as regards the products in question and by the increase in imports.

7 The first subparagraph of Article 25 (3) of the Sixth Directive provides that 'Member States shall fix the flat-rate compensation percentages, where necessary, and shall notify the Commission before applying them. Such percentages shall be based on macro-economic statistics for flat-rate farmers alone for the preceding three years. They may not be used to obtain for flat-rate farmers refunds greater than the value-added tax charges on inputs. Member States shall have the option of reducing such percentages to a nil rate. The percentage may be rounded up or down to the nearest half point.' The second subparagraph of Article 25 (3) provides 'Member States may fix varying flat-rate compensation percentages for forestry, for the different subdivisions of agriculture and for fisheries'.

8 The macro-economic statistics relating to flat-rate farmers alone, to which the aforementioned provision refers, comprise inputs (intermediate consumption and gross fixed-asset formation) and outputs, (final production, including own consumption), together with the total amount of taxes relating to inputs. The flat-rate compensation percentages are obtained by dividing the latter amount by outputs.

9 In this connection, it should be noted that, at the Court's request, the defendant produced macro-economic statistics relating solely to flat-rate farmers in the sectors in question in respect of the years 1978, 1979 and 1980, on the basis of which, pursuant to Article 25 (3) of the Sixth Directive, the flat-rate compensation percentages have to be determined.

10 The Court must therefore assess whether or not the flat-rate compensation percentages fixed by the Italian Republic since 1981 in respect of the beef, pork and fresh milk sectors are higher than those which ought to have been fixed on the basis of the aforementioned statistics.

11 On the basis of the macro-economic statistics relating to flat-rate farmers alone, supplied by the Italian Government, and applying the abovementioned method of calculation of flat-rate compensation, which is the same as that laid down for the calculation of own resources (Article 25 (12) of the Sixth Directive), the Commission obtained for the years 1978, 1979 and 1980, compensation percentages whose average is clearly lower than those fixed since 1981 for the sectors in question by the Italian Government.

12 It is true that, in accordance with Article 25 (3) of the Sixth Directive the aforementioned macro-economic statistics could only form the basis for calculating flat-rate compensation percentages for the year 1981. However, there is no reason to suppose, and this has not been argued by the Italian Government, that the situation in Italy of farmers benefiting from the flat-rate scheme in the sectors in question changed in subsequent years in such a way as to provide justification for the flat-rate compensation percentages such as those in issue in this case.

13 The argument relied on by the defendant that it was necessary to make certain corrections to the statistics on the ground that they do not reveal the real costs of production of flat-rate farmers, cannot be accepted. No document has been submitted to the Court that might justify such corrections on the basis of concrete statistics.

14 It is true that Italian production in the sectors in question has not increased but this finding is not such as to show that the defendant fixed the flat-rate compensation percentages correctly. The possibility cannot be ruled out that excessive compensation percentages, representing, in reality, aid to the sectors in question, have the effect of preventing a fall in production.

15 Finally, if, as the defendant argues, the rate of self-sufficiency has not increased, that cannot necessarily be ascribed to the neutral effect of the compensation but may be attributable to other factors such as an increase in consumption.

16 It follows that, by fixing at 15% and then at 14% the flat-rate compensation percentages for the beef, pork and unconcentrated and unsweetened fresh milk sectors with effect from 1981 and 1983 respectively, the Italian Republic has failed to fulfil its obligations under Article 25 (3) of the Sixth Directive.

The complaint relating to the application of flat-rate compensation percentages to supplies of goods and services to flat-rate farmers

17 The applicant claims that Article 34 of Presidential Decree No 633 is contrary to Article 25 (5) of the Sixth Directive, inasmuch as it provides that the flat-rate compensation percentages are also applicable to the supply of goods and services to flat-rate farmers.

18 According to the defendant, paragraphs 5 and 8 of Article 25 of the Sixth Directive do not preclude the application of the flat-rate compensation percentages to the supply of goods and services to flat-rate farmers; all that they rule out is that in such cases the compensation be paid by the public authorities under Article 25 (6).

19 It must be stated that such an interpretation of Article 25 (5) and (8) of the Sixth Directive is incompatible with the letter and the spirit of those provisions.

20 Article 25 (5) states clearly that: 'The flat-rate percentages provided for in paragraph 3 shall be applied to the price, exclusive of tax, of the agricultural

products and agricultural services supplied by the flat-rate farmers to taxable persons other than a flat-rate farmer. This compensation shall exclude all other forms of deduction'. Article 25 (8) provides that: 'As regards all supplies of agricultural products and agricultural services other than those covered by paragraph 5, the flat-rate compensation is deemed to be paid by the purchaser or customer'.

21 The effect of those provisions taken together is that, when goods or services are supplied to flat-rate farmers or to non-taxable persons, the flat-rate compensation percentages should not be applied. In such cases compensation for the value-added tax charge on inputs is obtained by the payment of an all-in price for those goods or services which is deemed to include that charge. The invoicing of the flat-rate amount would in those circumstances serve no useful purpose since the buyer or the recipient of the service would be unable to deduct the input tax.

22 It follows that, by providing for the application of the flat-rate compensation percentages to the supply of goods and services to flat-rate farmers, the Italian Republic has failed to fulfil its obligations under the Treaty and Article 25 (5) and (8) of the Sixth Directive.

Costs

23 Under Article 69 (2) of the Rules of Procedure, the unsuccessful party is to be ordered to pay the costs. Since the Italian Republic has failed in its submissions, it must be ordered to pay the costs.

On those grounds,

THE COURT

hereby:

(1) Declares that, in the context of value-added tax and the flat-rate scheme for farmers, the Italian Republic, by fixing at 15% and then at 14% the flat-rate compensation percentages for the beef, pork and unconcentrated and unsweetened fresh milk sectors with effect from 1981 and 1983 respectively and by providing for the application of the flat-rate compensation percentages to the supply of goods and services to flat-rate farmers, has failed to fulfil its obligations under the Treaty and Article 25 (3), (5) and (8) of the Sixth Council Directive (77/388/EEC) of 17 May 1977;

(2) Orders the Italian Republic to pay the costs.

Mackenzie Stuart Bosco Moitinho de Almeida

Rodríguez Iglesias Koopmans Everling

Galmot Kakouris Schockweiler

Delivered in open court in Luxembourg on 28 June 1988.

J.-G. Giraud
Registrar

A. J. Mackenzie Stuart
President