JUDGMENT OF THE COURT (First Chamber)

10 July 2008 *

In Case C-25/07,

REFERENCE for a preliminary ruling under Article 234 EC by the Wojewódzki Sąd Administracyjny we Wrocławiu (Poland), made by decision of 11 December 2006, received at the Court on 25 January 2007, in the proceedings

Alicja Sosnowska

v

Dyrektor Izby Skarbowej we Wrocławiu Ośrodek Zamiejscowy w Wałbrzychu,

THE COURT (First Chamber),

composed of P. Jann, President of Chamber, A. Tizzano (Rapporteur), A. Borg Barthet, M. Ilešič and E. Levits, Judges,

* Language of the case: Polish.

Advocate General: J. Mazák,
Registrar: B. Fülöp, Administrator,

having regard to the written procedure and further to the hearing on 22 November 2007,

after considering the observations submitted on behalf of:

— Ms Sosnowska, by M. Sworobowicz, doradca podatkowy,

— the Polish Government, by E. Ośniecka-Tamecka, H. Majszczyk and M. Jarosz, acting as Agents,

— the Commission of the European Communities, by K. Herrmann and D. Triantafyllou, acting as Agents,

after hearing the Opinion of the Advocate General at the sitting on 26 February 2008,

gives the following

Judgment

1 This reference for a preliminary ruling concerns, first, the interpretation of the third paragraph of Article 5 EC, read in conjunction with Article 2 of First Council Directive 67/227/EEC of 11 April 1967 on the harmonisation of legislation of Member States concerning turnover taxes (OJ, English Special Edition 1967, p. 1), as amended by the Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of assessment (OJ 1977 L 145, p. 1) ('the First VAT Directive') and Article 18(4) of the Sixth Directive 77/388, as amended by Council Directive 2005/92/EC of 12 December 2005 (OJ 2005 L 345, p. 19) ('the Sixth VAT Directive'). Secondly, the reference relates to the interpretation of Article 27(1) of the Sixth VAT Directive.

2 The reference has been made in the context of proceedings brought by Ms Sosnowska ('the applicant') against the Dyrektor Izby Skarbowej we Wrocławiu Ośrodek Zamiejscowy w Wałbrzychu (Director of the Tax Chamber of Wrocław, the 'Dyrektor') relating to an application for repayment of excess value added tax ('VAT') paid by the applicant.

Legal context

Community legislation

3 Article 2 of the First VAT Directive provides:

'The principle of the common system of value added tax involves the application to goods and services of a general tax on consumption exactly proportional to the price of the goods and services, whatever the number of transactions which take place in the production and distribution process before the stage at which tax is charged.

On each transaction, value added tax, calculated on the price of the goods or services at the rate applicable to such goods or services, shall be chargeable after deduction of the amount of value added tax borne directly by the various cost components.

The common system of value added tax shall be applied up to and including the retail trade stage.'

4 The first paragraph of Article 18(2) of the Sixth VAT Directive states:

'The taxable person shall effect the deduction by subtracting from the total amount of value added tax due for a given tax period the total amount of the tax in respect of

which, during the same period, the right to deduct has arisen and can be exercised under the provisions of paragraph 1.'

5 The first paragraph of Article 18(4) of the Sixth VAT Directive provides:

'Where for a given tax period the amount of authorised deductions exceeds the amount of tax due, the Member States may either make a refund or carry the excess forward to the following period according to conditions which they shall determine.'

6 Under Article 27(1) of the Sixth VAT Directive:

'The Council, acting unanimously on a proposal from the Commission, may authorise any Member State to introduce special measures for derogation from the provisions of this Directive, in order to simplify the procedure for charging the tax or to prevent certain types of tax evasion or avoidance. Measures intended to simplify the procedure for charging the tax, except to a negligible extent, may not affect the amount of tax due at the final consumption stage.'

National law

7 Article 87(1) and (2) of the Polish Law on the tax on goods and services (Ustawa o podatku od towarów i usług) of 11 March 2004 (Dz. U of 2004, No 54, heading 535, 'the Law on VAT') provide:

'1. Where the amount of deductible input VAT … exceeds the output VAT, taxable persons shall enjoy the right to a reduction of the output tax due for the following periods by the said difference or to a refund of such a difference into his bank account.

2. … the tax difference shall be refunded … within 60 days from the day on which the return was submitted by the taxable person. Where further investigation is required into whether or not the refund should be granted, the tax office may extend that period until the necessary investigations have been carried out. …

…'

8 Article 97 of the Law on VAT provides:

'1. Prior to making the first intra-Community supply or acquisition, the taxable persons referred to in Article 15 who are under a duty to register as active VAT payers shall be obliged to notify the head of a tax authority of their intention to carry out such activities, by filing the application for registration referred to in Article 96.

…

5. In the case of taxable persons who commence the activities referred to in Article 5 and taxable persons who commenced such activities within less than 12 months prior to filing the notification referred to in paragraph (1), and who have been registered as European Union VAT payers [the 'new taxable persons'], the period for refunding the tax difference referred to in Article 87(2) … shall extend to 180 days. …

6. In the case of taxable persons referred to in paragraph (5), the principles and repayment periods laid down in Article 87(2) to (6) shall apply from the date of the return relating to the period after a period of 12 months or four quarters in respect of which the taxable person has lodged a tax return and has paid in due time the taxes constituting State revenue, including his liabilities for the tax on the income of natural persons.

7. The provisions of Paragraph (5) shall not apply if the taxable person lodges with a revenue office a guarantee, by way of (i) a security deposit or (ii) material security or (iii) a bank guarantee, to the value of PLN 250 000, hereinafter referred to as a "security deposit".'

The dispute in the main proceedings and the questions referred for a preliminary ruling

9 In her VAT return for the month of January 2006, the applicant reported payment of excess VAT to the amount of PLN 44 782. Relying on Article 18(4) of the Sixth VAT Directive, she then applied to the tax office of Świdnica for repayment of that excess to her within a period of 60 days from the date of submission of her VAT return.

10 On the basis of Article 87(1) and (2), and Article 97(5) and (7) of the Law on VAT, the tax office of Świdnica rejected her application. The opinion of that office was that the applicant could not obtain the repayment of the excess VAT within the period of

60 days, because, since she had commenced her activities less than 12 months earlier and since she had not supplied to the tax office a special deposit within the meaning of Article 97(7), she did not satisfy the conditions established by the Law on VAT for entitlement to the repayment sought.

11 The applicant submitted a complaint against that decision to the Dyrektor, who upheld the decision of refusal.

12 The applicant was not satisfied with that decision and brought an action before the Wojewódzki Sąd Administracyjny we Wrocławiu (Regional Administrative Court of Wrocław). That court was uncertain whether the national provisions in question were compatible with Community law and therefore stayed proceedings and referred the following two questions to the Court for a preliminary ruling:

'(1) Does the third paragraph of Article 5 EC, in conjunction with Article 2 of the [First VAT Directive] and Article 18(4) of the [Sixth VAT Directive] confer on a Member State the right to incorporate into national provisions on VAT the rules in Article 97(5) and (7) of the [Law on VAT]?

(2) Or, do the rules laid down in Article 97(5) and (7) of the [Law on VAT] constitute special measures to prevent certain types of tax evasion or avoidance within the meaning of Article 27(1) of the [Sixth VAT Directive]?'

The questions referred for a preliminary ruling

The first question

13 By its first question, the referring court asks essentially whether Article 18(4) of the Sixth VAT directive must be interpreted as precluding national legislation, such as that at issue in the main proceedings, which, in order to allow inquiries necessary to prevent tax evasion and avoidance, extends from 60 to 180 days, starting from the date of submission of the taxable person's VAT return, the period available to the national tax office for repayment of excess VAT to a category of taxable persons, unless those persons lodge a security deposit to a value of PLN 250 000.

14 It must be recalled at the outset that, in accordance with settled case-law, the right, guaranteed by Article 17 of the Sixth VAT Directive, of taxable persons to deduct the VAT they have already paid on goods purchased and services received as inputs from the VAT which they are liable to pay is a fundamental principle of the common system of VAT established by the relevant Community legislation (see, in particular, to that effect, Joined Cases C-286/94, C-340/95, C-401/95 and C-47/96 *Molenheide and Others* [1997] ECR I-7281, paragraph 47, and Case C-78/00 *Commission* v *Italy* [2001] ECR I-8195, paragraph 28).

15 As the Court has consistently held, it is clear that the right to deduct is an integral part of the VAT scheme and as a general rule may not be limited. In particular, that right is exercisable immediately in respect of all the taxes charged on transactions relating to inputs (see, notably, Case C-62/93 *BP Supergas* [1995] ECR I-1883, paragraph 18; Joined Cases C-110/98 to C-147/98 *Gabalfrisa and Others* [2000] ECR I-1577, paragraph 43; and Case C-368/06 *Cedilac* [2007] ECR I-12327, paragraph 31).

16 It is relevant, moreover, to note that where, for a given tax period, the amount of the deductible tax exceeds the amount of tax due and therefore the taxable person cannot effect the deduction by subtraction in accordance with Article 18(2) of the Sixth VAT directive, Article 18(4) provides that the Member States may either make a refund or carry the excess forward to the following period according to conditions which they are to determine.

17 As regards the former possibility, which is at issue in the main proceedings, the Court has made it clear that, while the Member States have a certain freedom to manoeuvre in determining the conditions for the refund of excess VAT, those conditions cannot undermine the principle of neutrality of the VAT tax system by making the taxable person bear the burden of the VAT in whole or in part. In particular, such conditions must enable the taxable person, in appropriate circumstances, to recover the entirety of the credit arising from that excess VAT. This implies that the refund is made within a reasonable period of time by a payment in liquid funds or equivalent means, and that, in any event, the method of refund adopted must not entail any financial risk for the taxable person. (see *Commission* v *Italy*, paragraphs 32 to 34).

18 Consequently, the question from the referring court must be examined in the light of those fundamental principles, set out in the preceding paragraphs, of the common system of VAT.

19 It is apparent from the order for reference that, under the provisions of the Law on VAT determining the conditions for repayment of excess VAT to the taxable person, the tax office has available to it a period of 60 days from the date on which the taxable person submits his VAT return to make such a repayment; that period is extended to 180 days when, as in the case of the applicant in the main proceedings, the taxable persons concerned are new taxable persons who have not lodged a security deposit, within the meaning of Article 97(7) of the Law on VAT.

20 It is therefore clear that new taxable persons are subject to conditions for the refund of excess VAT which are more onerous than those to which other taxable persons

are subject. Accordingly they have to bear, at least to the extent of the amount of excess VAT to be repaid, the financial burden of VAT for a particularly long period.

21 The Republic of Poland maintains that lengthening of the period is justified by the fact that the persons concerned are taxable persons newly liable to VAT, who are not known to the tax office and in relation to whom more extensive inquiries must be made in order to prevent any tax evasion and avoidance.

22 As the Court has already had occasion to make clear, the Member States have a legitimate interest in taking appropriate steps to protect their financial interests and the prevention of possible tax evasion, avoidance and abuse is an objective recognised and encouraged by the Sixth Directive (see, to that effect, *Molenheide and Others*, paragraph 47; Case C-255/02 *Halifax and Others* [2006] ECR I-1609, paragraph 71; and Joined Cases C-439/04 and C-440/04 *Kittel and Recolta Recycling* [2006] ECR I-6161, paragraph 54).

23 None the less, as the Advocate General observes in point 20 of his Opinion, Member States must, in accordance with the principle of proportionality, employ means which, whilst enabling them effectively to attain such an objective, are the least detrimental to the objectives and principles laid down by the relevant Community legislation, which include the fundamental principle of the right to deduct VAT (see *Molenheide and Others*, paragraphs 46 and 47; Case C-409/04 *Teleos and Others* [2007] ECR I-7797, paragraphs 52 and 53; and Case C-271/06 *Netto Supermarkt* [2008] ECR I-771, paragraphs 19 and 20).

24 It is clear from the case-law that national legislation determining conditions for repayment of excess VAT which are more onerous for one category of taxable persons because of a presumed risk of evasion, without making any provision for the taxable person to demonstrate the absence of tax evasion or avoidance in order to take advantage of less restrictive conditions, is not a means proportionate to the objective of combating tax evasion and avoidance and has a disproportionate effect on the objectives and principles of the Sixth VAT Directive (see, by analogy, in

relation to exclusions from the right to deduct, Joined Cases C-177/99 and C-181/99 *Ampafrance and Sanofi* [2000] ECR I-7013, paragraph 62, and, in relation to preventive attachment, *Molenheide and Others*, paragraph 51).

25 That is exactly the case, as determined in paragraph 20 of this judgment, of the national legislation in the main proceedings.

26 It is clear from the order for reference that Article 97(5) and (7) of the Law on VAT apply generally and preventively to new taxable persons, without making any provision for such persons to demonstrate the absence of a risk of tax evasion or avoidance.

27 Similarly, the national provisions at issue do not appear to be in conformity with the condition laid down in the case-law, as stated in paragraph 17 of this judgment, that repayment of the excess VAT must be made within a reasonable time. As was stated in the order for reference, the period for repayment of 180 days laid down for new taxable persons is, on the one hand, six times longer than the one month applicable accounting period for VAT and, on the other hand, three times longer than the period applied to other taxable persons, while the Polish authorities have offered no argument capable of explaining why it is necessary, in order to prevent tax evasion and avoidance, to establish a difference in treatment of such a scale.

28 Moreover, such a long period appears even less necessary when, in any event, the tax office has the power, under Article 87(2) of the Law on VAT, if it is useful to make wider inquiry into the lawfulness of repayment and to obtain the necessary clarification, to extend the period of 60 days within which repayment must be made.

29 Lastly, as regards the possibility offered to new taxable persons by Article 97(7) of the Law on VAT to lodge a security deposit in order to take advantage of the normal

period of 60 days for the obtaining of repayment of excess VAT, that cannot affect the considerations set out in the preceding paragraphs.

30 As is argued by the Commission, the security deposit is not proportionate either to the amount of the excess VAT to be repaid or to the economic size of the taxable person.

31 In particular, the lodging of such a security deposit is likely, contrary to what is required by the case-law referred to in paragraph 17 of this judgment, to entail a not inconsiderable financial risk for undertakings which have just commenced their activities and may, consequently, lack significant resources.

32 In reality, the effect of the obligation to put in place such a security deposit, in order to be able to take advantage of the period which ordinarily applies, is only to replace the financial burden associated with the fact that the amount of the excess VAT is tied up for a period of 180 days with the burden consequent on the amount of the security deposit being tied up. There is even less justification when, first, the latter amount may, as in the case in the main proceedings, be greater than the amount of the excess VAT at issue, and, second, the length of time over which the security deposit is tied up is greater than the period for repayment of the excess VAT laid down for new taxable persons. Under Article 97(6) of the Law on VAT, the security deposit can be released only after a period of 12 months, on condition that the taxable person has paid all of the taxes relating to that period for which he is liable to the State.

33 In those circumstances, the reply to be given to the first question is that Article 18(4) of the Sixth VAT Directive and the principle of proportionality preclude national legislation, such as that at issue in the main proceedings, which, in order to allow the investigations required to prevent tax evasion and avoidance, extends from 60 to 180 days, as from the date of submission of the taxable person's VAT return, the period available to the national tax office for repayment of excess VAT to a category of taxable persons unless those persons lodge a security deposit to a value of PLN 250 000.

The second question

34 By its second question, the referring court essentially asks whether the provisions of Article 97(5) and (7) of the Law on VAT can be regarded as 'special measures for derogation' intended to prevent certain types of tax evasion or avoidance, within the meaning of Article 27(1) of the Sixth VAT directive.

35 It must be borne in mind that Article 27(1) of the Sixth VAT Directive provides that the option of a Member State to introduce such derogating measures is subject to a specific procedure, in particular requiring the agreement of the Council of the European Union, acting unanimously.

36 However, as the Advocate General states in point 39 of his Opinion and as is correctly pointed out by the Commission, the documents before the Court do not disclose that the measures at issue were authorised by the Council, in accordance with that provision, as special measures for derogation from the Sixth VAT directive.

37 That being the case, provisions such as those within Article 97(5) and (7) of the Law on VAT cannot fall within the scope of Article 27(1).

38 Consequently the reply to be given to the second question is that provisions, such as those at issue in the main proceedings, do not constitute 'special measures for derogation' intended to prevent certain types of tax evasion or avoidance, within the meaning of Article 27(1) of the Sixth VAT directive.

Costs

39 Since these proceedings are, for the parties to the main proceedings, a step in the action pending before the national court, the decision on costs is a matter for that court. Costs incurred in submitting observations to the Court, other than the costs of those parties, are not recoverable.

On those grounds, the Court (First Chamber) hereby rules:

1. **Article 18(4) of the Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of assessment, as amended by Council Directive 2005/92/EC of 2 December 2005, and the principle of proportionality preclude national legislation, such as that at issue in the main proceedings, which, in order to allow investigations required to prevent tax evasion and avoidance, extends from 60 to 180 days, as from the date of submission of the taxable person's VAT return, the period available to the national tax office for repayment of excess VAT to a category of taxable persons, unless those persons lodge a security deposit to a value of PLN 250 000.**

2. **Provisions such as those at issue in the main proceedings do not constitute 'special measures for derogation' intended to prevent certain types of tax evasion or avoidance within the meaning of Article 27(1) of the Sixth Directive 77/388, as amended by Directive 2005/92.**

[Signatures]