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VALUE ADDED TAX COMMITTEE
(ARTICLE 398 OF DIRECTIVE 2006/112/EC)
WORKING PAPER NO 762

QUESTION
CONCERNING THE APPLICATION OF EU VAT PROVISIONS

ORIGIN: Italy

REFERENCES: Articles 30, 61, 70, 71, 168, 178 and 201

SUBJECT: Importation of leased goods for taxable activities

1. INTRODUCTION

The Italian authorities have solicited the opinion of the VAT Committee on the application of the provisions of the VAT Directive in the case of the importation of leased goods.

The text of the question is annexed to this document.

2. SUBJECT MATTER

The Italian tax administration is faced with the situation in which taxable persons in Italy lease an aircraft from non-EU suppliers and introduce them into Italy under temporary admission with a partial relief from customs duties. Under the Italian VAT legislation, implementing inter alia Article 201 of the VAT Directive, the lessee of the aircraft in such a case becomes liable both for the payment of import VAT and of the VAT on the lease of such an aircraft (as, in the given situation, the aircraft cannot benefit from any of the exemptions provided for in Article 148 of the VAT Directive).

The question arises as to whether the principle of fiscal neutrality is not breached in the case where the lessee is obliged to account not only for the VAT on the lease but also for import VAT on the leased goods.

3. THE COMMISSION'S OPINION

3.1. Single supply or distinct supplies for the purpose of VAT

Article 2 of the VAT Directive defines the transactions subject to VAT:

- (a) the supply of goods for consideration by a taxable person acting as such;
- (b) the intra-Community acquisition of goods for consideration;
- (c) the supply of services for consideration by a taxable person acting as such;
- (d) the importation of goods.

Although this provision defines importation as a transaction, the importation does not in itself constitute a transaction because it is not an 'action' between two persons, but merely a transfer of goods carried out by one person. In order to avoid confusions in the text the importation is further referred to as a 'taxable event'.

It is clear from this provision and from the case law of the Court of Justice of the European Union (CJEU)¹ that the importation of goods and the supply of services constitute separate taxable events.

It is true that the CJEU has held that a transaction may comprise of several elements and that it must be determined whether for VAT purposes it is to be regarded as consisting of a single supply or of several distinct and independent supplies.

¹ See case 15/81 *Schul*, paragraph 14 and case C-305/03, *Commission v United Kingdom*, paragraph 33.

The Commission services however take the view that in the present case there is only one transaction – supply of a leasing service, in relation to which there are two separate taxable events (the importation, and the leasing service). The notion of "principal-ancillary service" therefore is not applicable to this case, taking into account also that those taxable events happen at different times and the tax may become chargeable to different persons.

3.2. Analysis of each taxable event

3.2.1. Importation of goods

Importation is defined in Article 30 of the VAT Directive as the entry into the EU of goods which are not in free circulation within the meaning of Article 29 of the TFEU.

According to Article 70 of the VAT Directive, the chargeable event shall occur and import VAT shall become chargeable when the goods are imported. As an exception, Article 71 of the VAT Directive provides that in cases where on entry into the EU, goods are placed under temporary importation arrangements with total exemption from import duty, the chargeable event shall occur and VAT shall become chargeable only when the goods cease to be covered by those arrangements.

Following on from those provisions, the importation of goods that are placed under temporary admission with *partial* exemption from customs duties shall be subject to import VAT in accordance with the provisions of Article 70 of the VAT Directive.

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 the [imported] goods are used for the purposes of those taxed transactions.

Import VAT is payable by any person designated or recognised as liable by the Member State of importation (Article 201 of the VAT Directive). In the case in question Member States have therefore a discretion to designate as liable to pay import VAT either the owner of the aircraft, the recipient of the aircraft (lessee) or any other person, such as, for example, a customs representative.

Depending on who is designated as liable for import VAT that person may or may not be entitled to the VAT deduction. Possible scenarios and their impact on VAT deduction are analysed below.

3.2.1.1. Owner designated as the person liable for payment of import VAT

The owner uses that aircraft for his taxable economic activities, that is, the taxable leasing of the aircraft. He is consequently entitled to a right of deduction of the VAT, including import VAT, incurred in relation with this lease.

This right however can only be exercised if the importer holds an import document specifying him as the consignee or importer, and stating the amount of VAT due or enabling that amount to be calculated (Article 178(e) of the VAT Directive).

If the owner is not established within the EU, this right shall be exercised through a refund in accordance with the provisions of the 13th VAT Directive (86/560/EEC) subject to the limitations applied by the importing Member State in line with the provisions of the mentioned directive.

3.2.1.2. Lessee designated as the person liable for payment of import VAT

In cases where the owner of the goods is not established within the EU, the lessee could clear the goods for customs purposes himself and could be designated by the Member State of importation as liable for the import VAT payment.

According to guidelines agreed by the VAT Committee² a taxable person designated as liable for the payment of import VAT pursuant to Article 201 of the VAT Directive shall not be entitled to deduct it if (1) he does not obtain the right to dispose of the goods as owner and (2) the cost of the goods has no direct and immediate link with his economic activity.

Whilst the lessee of an aircraft may not be regarded as having a right to dispose of the aircraft as owner, it still has to be established whether the cost of that aircraft has an immediate and direct link with his economic activities.

However, the lessee does not actually bear the costs of the aircraft simply the amount of the lease to be paid to the owner. These costs, although directly related, are not the actual costs of the aircraft.

Therefore, following the VAT Committee guidelines, the lessee is not entitled to a VAT deduction because both (1) and (2) above apply in this case. This is irrespective of whether or not the procedural conditions of Article 178(e) of the VAT Directive are fulfilled.

3.2.1.3. Customs representative designated as the person liable for payment of import VAT

The Commission services restate their opinion³ that any person, designated as liable to pay import VAT pursuant to Article 201 who is not the owner of the imported goods, does not hold on their own a right to deduct that VAT.

It is clear that the customs representative does not obtain the right to dispose of the goods as the owner, nor do the costs of the goods have a direct and immediate link with his economic activities (which are merely limited to the customs clearance).

The VAT deduction in this case may be exercised by the owner of the aircraft. The customs representative would have to ensure that the conditions of Article 178(e) of the VAT Directive are fulfilled and transfer the relevant documentation to enable him to exercise the right to deduct.

² See guidelines resulting from the 94th meeting of 19 October 2011 – Document A – taxud.c.1(2011)864736 – Working paper No 705.

³ See guidelines resulting from the 94th meeting of 19 October 2011 – Document C – taxud.c.1(2012)243615 – Working paper No 716 final.

3.2.2. Supply of services

According to Article 44 of the VAT Directive the place of supply of services to a taxable person acting as such shall be the place where that person has established his business (or if provided to a fixed establishment, at the place where that fixed establishment is located).

Following on from those provisions, under Article 44 of the VAT Directive, the lease of an aircraft, other than the short-term lease, , shall be taxed at the place of establishment of the EU customer.

The VAT exemption could apply in accordance with the provisions of Article 148 of the VAT Directive if the aircraft is used by airlines operating for reward chiefly on international routes or was used by State institutions; in accordance with Article 371 and point (11) of Annex X, part B of the VAT Directive if these exemptions were applied prior to January 1st 1978.

According to Article 168(a) of the VAT Directive in so far as the services are used for the purposes of the taxed transactions of a taxable person, the taxable person shall be entitled, in the Member State in which he carries out these transactions, to deduct the VAT due or paid in that Member State in respect of supplies to him of goods or services, carried out or to be carried out by another taxable person.

The fiscal neutrality in the case where the aircraft is leased from a non-EU supplier is therefore ensured by the application of the reverse charge mechanism pursuant to Article 196 and the right to deduct the VAT if the aircraft is used for taxed activities.

3.2.3. The question of possible double taxation

Although the VAT Directive provides for two separate taxable events, it is appropriate to analyse whether the rules of the VAT Directive do not undermine their purpose in this specific case.

It is true that the recipient of the service, if liable to pay import VAT, bears an additional administrative burden in comparison to the situation of the lease of the aircraft located within the EU.

However, the purpose of import VAT is to ensure that all the goods entering the EU bear the same VAT burden as those located in the EU at the time of sale. The aircraft entering the EU from the third country was purchased without EU VAT.

Therefore, the import VAT payment in this case ensures that taxable persons leasing aircraft from outside the EU are put on an equal footing to those leasing aircraft from inside the EU.

In most of the cases, this will not appear to have any financial impact, as the aircraft are used only for taxable leases (with the import VAT being deducted afterwards). However, this issue may become relevant in relation to the adjustments of the VAT deduction in cases where the non EU aircraft would, after a certain period of time, be affected to e.g. non-business uses.

It is therefore the Commission's view that the application of import VAT on the goods leased from outside the EU does not undermine the purposes of the VAT Directive.

3.3. Conclusion

In summary, the Commission is of the view that the importation of the aircraft for the purposes of leasing, and its onward lease constitutes for VAT purposes separate taxable events.

In cases where the lessee is designated by the Member State as liable for import VAT payment, it is not entitled to deduct this import VAT in accordance with the provisions of Articles 168(e) and 178(e) of VAT Directive.

The payment of import VAT and VAT on the lease does not breach fiscal neutrality as the right of deduction in principle is ensured for both transactions in cases where that aircraft is used for taxed economic activities.

4. DELEGATIONS' OPINION

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

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Question from Italy

Interpretation of Articles 61 and 71 of Directive 2006/112/EC

2.1 Question

The question concerns the application of the VAT provisions in cases of the temporary admission of aircraft introduced into the territory of the Community as a result of a chartering and/or hiring contract. More in detail, the question regards the use of the aircraft in the territory of the Community on the strength of a so-called dry lease contract, envisaging the payment by EU lessee of a monthly rental fee to a extra-EU lessor, and its subsequent re-exportation.

It must be specified that such aircraft is not intended for international transport, and thus it cannot benefit from the exemptions referred to in Article 148 of Directive 2006/112/EC.

Temporary admission is the customs procedure ruled by Article 162 et seq. of the Modernized Customs Code (Regulation 450 of 2008) and in Articles from 553 to 584 of the Commission Regulation laying down provisions for the implementation of the Community Customs Code (Regulation 2454/93 and subsequent amendments and additions).

In particular, according to the definition laid down in Article 162 of the Modernized Customs Code, under the temporary admission procedure, non-Community goods intended for re-export may be used in the customs territory of the Community with total or partial relief from import duties, provided that certain conditions are met.

More in detail, the abovementioned case comes under the situation for the application the temporary admission procedure with partial relief from import duties, since the aircraft, even if owned by persons established outside the EU, are used by persons established within the EU on the basis of charter or hiring contracts, and therefore do not fall under any of the exceptions contemplated by the Community rules for the application of the temporary admission procedure with total relief (see Article 558 of the Regulation implementing the Community Customs Code).

In such a case, as provided for by Article 165 of the aforesaid Modernized Customs Code, *“The amount of import duties in respect of goods placed under the temporary admission procedure with partial relief from import duties shall be set at 3% of the amount of import duty which would have been payable on those goods had they been released for free circulation on the date on which they were placed under the temporary admission procedure.*

That amount shall be payable for every month or fraction of a month during which the goods have been placed under temporary admission with partial relief from import duty.

2. The amount of import duty shall not exceed that which would have been payable if the goods in question had been released for free circulation on the date on which they were placed under the temporary admission procedure.”

For VAT purposes, according to Article 71 of Directive 2006/112/CE, where goods are placed under temporary admission arrangements with total exemption from import duty, *“the chargeable event shall occur and VAT shall become chargeable only when the goods cease to be covered by those arrangements or situations.”* Furthermore, the second subparagraph of the aforesaid Article 71 stipulates that, where imported goods are subject to customs duties, *“the chargeable event shall occur and VAT shall become chargeable when the chargeable event in respect of those duties occurs and those duties become chargeable”*.

From the above it can be inferred that, in the above cases, the goods introduced into the Community under temporary admission must pay VAT upon importation, in accordance with the second sub-paragraph of Article 71, and that the same goods cannot benefit from the exemptions referred to in Article 148 of Directive 2006/112/EC.

Furthermore, the customer established within the Community must also pay to his supplier the rental fees for the use of the same good, and consequently, at the same time, such case constitutes a supply of services taxable in the place of the recipient (Article 44 of Directive 2006/112/EC).

The result of this situation, i.e. a double taxation of the same transaction, hardly seems compatible with the principle of VAT neutrality.

In view of the above, Italy would like to solicit the opinion of the VAT Committee on the following:

In the first place, whether VAT is chargeable on goods (e.g. aircraft) placed under temporary admission arrangements with partial relief from import duties (given that the conditions for total relief from the duties are not met), in cases where the supply of services (chartering or hiring) relating to them is then subject to VAT;

In the second place, whether Article 71 of Directive 2006/112/EC is compatible with the customs provisions.

2.2 Opinion and proposed solution

In the opinion of the Italian Revenue Agency, a transaction which basically constitutes a single operation cannot be subject to VAT twice.

Consequently, for the purposes of applying Directive 2006/112/EC, only one chargeable event should be deemed to occur – the actual introduction of the good in the territory of the Community pursuant to Article 71, or, alternatively, the payment of the rental fees on part of the user of the good in accordance with Article 44.

For both such solutions it is necessary to adopt a flexible and non-literal interpretation of the Community provisions, so as to consider that one taxable event is “absorbed” by another, which is regarded as preponderant.