News from the Member States

Hungary

VAT Refunds under EU Jurisprudence

The *Kúria*, the Supreme Court of Hungary, issued a guiding decision no. 1/2014 in the field of administrative law which deals with the relationship between the provision of State aid and the repayment of VAT, based on the preliminary ruling of the Court of Justice provided in case C-191/12.[1] The decision confirms that the refusal of a Member State to repay the entirety of the VAT may be justified by the fact that this was covered by the State aid granted to the tax subject, provided that the economic burden relating to the refusal to deduct value added tax has been completely neutralized. In its guiding decision, the *Kúria* describes in detail how the courts reviewing administrative decisions can comply with the requirements set by the Court of Justice from the point of view of national procedural rules.

The plaintiff of the main proceedings concluded a subsidy contract with the Ministry of Agriculture and Rural Development as funds provider, aimed at enabling it to finance a project under the operational programme for agriculture and rural development. According to the VAT Act in force at that time, it was not possible to deduct, proportionally to the amount of the aid, the part of the input VAT paid on costs relating to the subsidized project. In addition, under Ministry of Finance guidelines, the eligible expenditure included the part of the VAT which corresponded to a percentage of the project financed by the aid. The funds provider granted an amount of HUF 90,000,000, which corresponded to 43.44 % of the eligible expenditure for the project.

The total eligible expenditure for the project was HUF 207,174,606, including HUF 18,645,714 in VAT which was not deductible. The assessment of VAT relating to development expenditure was included in the monthly VAT returns for September and November 2005, and also those for December 2005 and January 2006, with a view to claiming to offset the tax in the following period. Under the Law on VAT, the plaintiff in the main proceedings was unable to exercise its right to deduct HUF 4,440,000 of VAT relating to development expenditure paid in advance and calculated in the return for September 2005, and a further HUF 13,282,000 calculated in the return for November 2005, which represented a total of HUF 17,722,000.

With reference to the judgment of the Court of Justice in the case C-74/08, *PARAT Automotive Cabrio*,[2] which held that Article 17(2) and (6) of the Sixth Directive[3] must be interpreted to the effect that it precludes national legislation which, in the case of the acquisition of goods subsidised by public funds, allows the deduction of related VAT only up to the limit of the non-subsidised part of the costs of that acquisition, the plaintiff of the main proceeding submitted to the tax authority regularisation declarations for the relevant periods, in which it applied for repayment of the VAT which the limitation on the right to deduct had prevented it from deducting HUF 17,722,000 in total and late payment interest.

In response to that request, the first-instance tax authority set the tax deductible and the sums to be paid to the plaintiff in the main proceedings at a lower amount than that declared by the plaintiff in its regularisation declarations. The tax authority upheld those decisions, noting that the plaintiff had already obtained, by means of aid, an amount corresponding to 43.44 % of the non-deductible VAT. Therefore, pursuant to the General Law on Taxation, that sum had to be regarded as having been passed on.

Hearing the appeal for an amendment or annulment of the decisions made by the tax authority, the court of first instance found that those appeals were well-founded. It annulled the decisions at issue on the grounds that they unlawfully restricted the right to deduct – contrary to case C-74/08

1 C-191/12 – *Alakor Gabonatermelő és Forgalmazó* [2013] ECR n.y.r.

2 C-74/08 – *PARAT Automotive Cabrio* [2009] ECR I-03459.

3 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 145/1.

– and ordered the tax authority to recommence its assessment procedure.

The tax authority requested the *Kúria* to review the judgment, claiming, in particular, that the plaintiff in the main proceedings had already received, in the form of aid, part of the VAT which it sought to recover in the regularisation declarations. Consequently, according to the tax authority, only the part of the VAT which was not offset by that aid ought to have been subject to repayment.

The *Kúria* decided to stay the proceedings and referred questions to the Court of Justice for a preliminary ruling. In its preliminary ruling, the Court ruled that the principle of repayment of taxes levied in a Member State in infringement of the rules of EU law must be interpreted as meaning that it does not preclude that State from refusing to repay part of the value-added tax, the deduction of which had been precluded by a national measure contrary to European Union law, on the grounds that that part of the tax had been subsided by aid granted to the taxable person and financed by the European Union and by that State, provided that the economic burden relating to the refusal to deduct value added tax has been completely neutralised, which is for the national court to determine.

Based on this, the *Kúria,* by referring to the preliminary ruling, declared that Article 17(2) of the Sixth Directive precludes the national legislation from generally restricting the right to deduct VAT so that it applies to all supplies relating to products where State aid has been granted. The Member States must repay the whole amount of the VAT, the deduction of which was hindered by the violation of EU laws. The aim of the right to reclaim the amount repaid without legal grounds is to cure the non-compliance with EU law. The repayment can be exceptionally refused with the reason that it would lead to unjust enrichment, if it can be established that the tax has been passed on to another tax subject.

Thus, a Member State may refuse reimbursement of a tax with the reason of unjust enrichment if the economic burden caused by the tax is completely neutralized. In order to establish whether the reimbursement was exclusively aimed at the neutralizing of the economic burden, or whether it leads to the unjust enrichment of the tax subject, an economic analysis must be carried out during which all relevant circumstances and evidence must be assessed. In this respect, attention must be paid to the circumstance whether the amount of the aid granted to the applicant in the main proceedings would have been less if the latter had not been prevented from exercising its right to deduct.

In the instant case, the amount of the subsidy was calculated by referring to the eligible expenses of the project, which included both the net costs of the project and the non-deductible VAT. Therefore, it must be assessed whether, if the eligible expenses had been calculated by disregarding the non-deductible VAT, the amount of the aid ought to have been less than that which was actually granted. Were that the case, the excess resulting from the higher amount of the aid which the plaintiff accordingly was able to benefit from would be the consequence of the fact that part of the non-deductible VAT had been covered by that aid. The economic burden relating to the part of the tax corresponding to that excess would, on that basis, be subsidised by the funds provider and not by the plaintiff.

It follows that, in order to neutralise the economic burden relating to the prohibition on deducting VAT, the amount of the repayment which the applicant in the main proceedings may claim must correspond to the difference between, first, the amount of VAT which the plaintiff was unable to deduct due to the national legislation of which the incompatibility with EU law was pointed out in *PARAT Automotive Cabrio*, and, second, the amount of the aid granted to the plaintiff which exceeds that which would have been granted had it not been prevented from exercising its right to deduct.

The *Kúria* established that the tax authority as defendant could not take into account the above principles when reviewing the regularisation declarations and passing its decisions, since the EU law was interpreted only later, based on the request of the *Kúria* for a preliminary ruling.

The *Kúria* may review the administrative decisions on the basis of the legislation in force at the time of the passing of such decisions and the facts established in such decisions. These decisions, however, do not include an economic assessment or data, facts or other evidence which would enable the national court to pass a decision as to whether or not, in the decisions subject to the procedure, the non-compliance with EU law has been cured pursuant to the interpretations set out in cases C-74/08 and C-191/12.

In the review procedure, furthermore, there is no room to take evidence or to reconsider evidence, so the *Kúria* may pass its decisions based on the available data only.

The first instance court, although it may take evidence, cannot take over the competence of the administrative authority, thus it cannot decide in respect of such facts, circumstances and evidence which were not raised during the administrative proceedings and consequently could not serve as a basis for the decision. Furthermore, the evidence procedure before the first instance court cannot be extended beyond the framework of the procedure and the court must annul the administrative decisions and oblige the administrative authorities to re-commence the procedure if the court considers that the decision of the administrative authority should be based on another legal ground.

Therefore, the *Kúria* established that the decision of the court of first instance was correct as for the operational part, where it annulled the decisions and obliged the tax authority to re-commence the procedure. However, the first instance court was not in a position to properly justify its decision since the interpretation provided by the Court of Justice was not yet available and, therefore, the first instance court could not give a proper guidance to the tax authority on how to proceed. As a consequence of this, the *Kúria* maintained the first instance decision and amended the motivational part thereof. According to the *Kúria*, the tax authority will have to carry out an evidencing procedure during the first instance procedure, and as a result of the evidencing, the decisions passed on the merits must comply with the relevant rules of both the EU and the national legislation.

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