Entitlement to VAT refund where taxable person applied higher VAT rate than required by law 2/18/24

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In this article we explore Ruling C-606/22 from the Court of Justice of the European Union (CJEU) on the entitlement to a refund of value added tax (VAT) where the taxable person has applied a higher rate of VAT than what the law prescribes. This ruling is important because it explains how the VAT directive's principles should be applied in practice where a cash-register receipt has been issued to the customer, which is practically impossible to amend in order to show the correct rate of VAT and to refund the overpaid tax to the customer.

The ruling deals with a dispute between the Polish tax authority and company B. sp. z o.o. over a refund of VAT on sports club subscriptions sold by the company. The company filed adjusted VAT returns in the belief that the transaction qualified for a reduced rate of 8% (not 23%) based on the tax authority's change of practice. The tax authority refused to recognise a VAT overpayment for the periods in question and said the company had not issued adjusted tax invoices as required by the Polish VAT Act. The tax authority also said that since the company had collected a 23% VAT (not 8%) from its end consumers, it must pay the entire amount to the government in order to prevent unjust enrichment.

The Polish administrative courts that heard the case arrived at conflicting conclusions. The court of first instance reversed the tax authority's decision and recognised that VAT adjustments can be based on cash-register receipts. The court of second instance upheld the tax authority's appeal and asked the CJEU to make a preliminary ruling on how the VAT directive and VAT principles should be interpreted in this matter.

The CJEU ruling states that the VAT directive and VAT principles do not permit any practice that prohibits adjustments to the VAT paid, where goods and services have been supplied to consumers at an unreasonably high rate of VAT, solely because the transaction is supported by a cash-register receipt and not a tax invoice. In this case, too, the taxable person must have the option of claiming a VAT refund.

The court additionally examines whether refunding the VAT to the taxable person would cause unjust enrichment. The court states that enrichment has not occurred if it can be established that the taxable person having applied a 23% VAT based on the tax authority's initial interpretation was in a less favourable situation than its direct competitors having applied a reduced rate of VAT. A less favourable situation may exist either because this rate was partially or fully transferred to product prices, affecting the company's ability to compete with prices charged by its competitors and therefore possibly affecting also the company's sales volumes, or because of a profit reduction the company made to keep its prices competitive. Accordingly, the practice of the member state's tax authority as described by the national court is also contrary to the principle of tax neutrality. The CJEU case law implies that Union law does not prohibit the national system of law from providing for a refusal to reimburse taxes withheld by mistake if this gives unjust enrichment to persons entitled to such reimbursement. Under Union law, a refund of any taxes, duties or charges collected improperly is not mandatory if it is found that the person who was supposed to pay them has in fact transferred them to other subjects. Each member state's internal system

of law must prescribe conditions in which such requirements can be met, yet those conditions must be consistent with the principles of equivalence and effectiveness. Thus, on condition that the economic burden the wrongful tax places on the taxable person must be completely neutralised, the member state may refuse to refund the overpaid VAT on the grounds that a refund would lead to the taxable person's unjust enrichment. Whether there is unjust enrichment, which a refund of wrongfully paid tax under EU law would give the taxable person, and how big that enrichment is, are questions of fact coming within the competence of the national court because it freely evaluated evidence submitted to it at the end of an economic analysis that considers all the relevant circumstances.

The CJEU comes to the conclusion that even where a cash-register receipt has been issued, the taxable person having applied too high a rate of VAT by mistake has the right to file a refund claim with the member state's tax authority because it can cite the taxable person's unjust enrichment only if an economic analysis that considers all the relevant circumstances leads the tax authority to find that the economic burden the wrongfully collected tax places on the taxable person is completely neutralised.

The Attorney General's findings imply that this case might just as well pose no risk of the government losing tax revenues because the service was supplied only to end consumers who do not have the right to deduct input VAT. The Attorney General goes on to explain that the taxable person's unjust enrichment does not occur if a fixed price is agreed. The fact that end consumers have paid a final price computed incorrectly (because it included too much VAT and too little profit) does not prevent a refund.

We believe the ruling could encourage VAT refunds in similar cases in Latvia because it shows that taxable persons should have the option to adjust their tax base and that they could get a refund if they have applied the wrong rate of VAT, even if it were difficult to adjust the supporting documents and refund the wrongly collected tax to the customer. In that case we should conduct an economic analysis to establish the presence or absence of unjust enrichment.a