Grant Thornton

Margin scheme on second-hand goods

VAT Alert

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Judgment of the European Court of Justice no. C-127/22 dated May 4, 2023, BTK case

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1. Introduction

With judgment C-365/22 dated May 17, 2023, IT case, the European Court of Justice deals with a very peculiar matter concerning the extension of the scope of application of the margin scheme for second-hand goods also to spare parts of end-of-life and non-usable cars which are sold as a whole.

In the case at issue, a Belgian taxable person registered for VAT purposes which purchased completely damaged vehicles (which could not be repaired/modified to be reused as they were) from insurance companies and resold them as "wrecks" or together with spare parts that the client could use.

Uncertainties derived from the fact that in the past, with judgment C-471/15 Sjelle Autogenbrug dated January 18, 2017, the Court of Justice ruled in favour of the application of the margin scheme also if the sale would concern spare parts sold individually after removing them from end-of-life vehicles.

In the context analysed by the Court, the matter is quite specific, since it is aimed at ensuring whether the generic sale of a second-hand transport means, which is in no way suitable for reuse, can fall within the scope of application of the margin scheme, even though the aim of the sale is to allow the client to use spare parts.

2. Sale of second-hand goods"

It should be preliminarily highlighted that, according to recital no. 51 of VAT Directive (2006/112/EC), the application of a special scheme (such as the margin scheme) to second-hand goods as well as to works of art, collectors' items or antiques is aimed at avoiding double taxation and/or distortion of competition between taxable persons in relation to such transactions.

Moreover, as provided under art. 311, paragraph 1 of VAT Directive, "second-hand goods" refer to "movable tangible property that is suitable for further use as it is or after repair, other than works of art, collectors' items or antiques and other than precious metals or precious stones as defined by the Member States". However, the application of the margin scheme by the dealer of the abovementioned goods is related to the fact that the same purchased second-hand goods (as in the case at issue) from another person who could not exercise the right to deduct input tax (private consumer, taxable person carrying VAT-exempt transactions, etc.). In fact, as stated in judgment C-365/22 under analysis, "neither that person nor the taxable dealer being able to deduct" the VAT amount incorporated in the price of the good subject to such scheme (compare to point 23).

In fact, pursuant to art. 315 of VAT Directive, the margin realized by the taxable dealer of the good is "equal to the difference between the selling price charged by the taxable dealer for the goods and the purchase price". Therefore, the taxable base of sales of goods subject to the margin scheme is the margin realized by the

taxable dealer, net of VAT applied on the same margin. Based on this system, double taxation is avoided, since taxation is not applied again on the whole purchase price of the good which implicitly includes paid input VAT that has not been deducted.

3. Conclusions of the European Court

After clarifying the scope of application of the margin scheme, under point 25 of the judgment the European Court states that the required condition is that vehicles "*have not in fact been sold simply in order to be scrapped or transformed into another object*", *since, in that case, the good sold* "*is no longer in the same economic cycle and therefore does not qualify for the special margin scheme*".

On the other hand, the clarified impossibility to reuse sold goods, not even after repair, for the same purpose they were originally produced for, should not impact the qualification of the vehicle sold for their component "reusable" spare parts as second-hand good.

In fact, referring to the remarks of the EU Commission, the European Court states that "*an interpretation allowing a definitively end-of-life vehicle, as a second-hand good, to fall within the margin scheme because some of its components are suitable for further use*" is in line with the principles of the margin scheme (i.e., avoid double taxation) (compare to point 23). And this is true regardless of the fact that the taxable dealer resold the whole vehicle rather than only spare parts after removing them from the vehicle.

In this regard, there is the possibility to "*take into account objective factors such as the presentation and state of the vehicles, the subject matter of the contract, the price for which those vehicles were sold, the method of charging or the economic activity of the person who acquired those vehicles*" (compare to point 27).Therefore, if the other conditions required are met, too, end-of-life vehicles can be qualified as second-hand goods, even if they cannot be reused as such, if they include "*parts which maintain the functionalities that they possessed when new so that they can be reused as such or after repair and, secondly, [if] it is established that those vehicles remained in the same economic cycle because of that reuse of parts*".

The margin scheme applied to second-hand goods, as defined under Law Decree no. 41/1995, does not include a specific provision on the application of such special regime to the resale of an end-of-life vehicle for its spare parts, which can be reused even after repair.
In circular letter no. 28/E dated 21 June 2004, the Revenue Office, referring to previous circular letter no. 177 dated 22 June 1995 of the Ministry of Finance, deemed it suitable to provide clarifications on the system by making a clear distinction between the margin scheme and the scheme applied to wrecks, though admitting the possibility that both can be applied in some cases.
Specifically, this is the case in which a wreck dealer purchases a car to be scrapped from a private person and resells single still-usable spare parts. The margin scheme applies to the sale of spare parts, while the scheme for wrecks is applied to the other part of the good, which is to be considered actually as wreck.
In fact, circular letter no. 28/E dated 2004 can be considered as an anticipation of the provisions of the European Court of Justice in judgment C-471/15, according to the above specifications. However, the extension included in judgment C-365/22 represents a clear stance by the EU Court, which clearly requires a review of the system and will have to be implemented in the domestic VAT system, though applying all precautions indicated by the EU Court to avoid frauds and tax evasion.

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