

By PwC Deutschland | 03. August 2025

# ECJ referral regarding the review of protection of good faith in tax assessment proceedings

**The Supreme Tax Court referred to the European Court of Justice the question whether, in accordance with the principle of effectiveness, EU law precludes a national practice whereby the taxpayer's good faith in fulfilling the conditions for the margin scheme is not taken into account during the tax assessment procedure but rather considered later in fully separate proceedings.**

## Background

The plaintiff (GmbH) is involved in the trading of watches. In its VAT returns, the GmbH applied the so-called margin scheme (Section 25a of the German VAT Act) on certain sales. Under this simplified rule, not the entire sales price of the watch is subject to VAT but only the difference between the sales price and the purchase price. This margin scheme may be applied, i. a., if the supplier who sold the watch to the plaintiff is also a retailer, who applies the margin scheme and who confirms this status on the relevant invoices.

The tax office later found out that some of the information provided on the suppliers' invoices was inaccurate. The plaintiff pointed out that it had acted in good faith and was entitled to rely on the information provided by its suppliers. The tax office nonetheless set the VAT based on the standard rate which was later confirmed by the tax court of first instance. The tax court did not consider it necessary to examine whether the plaintiff had acted in good faith because it was only permitted to invoke the issue of good faith in a separate procedure on grounds of the statutory concessionary rule (Section 227 Fiscal Code) and not at an earlier procedural stage, i. e. when contesting the tax assessment notice.

## Decision

The Supreme Tax Court considers it doubtful under EU law if Germany is permitted to oblige taxpayers to take further proceedings (to obtain equitable relief) to protect their good faith. Taxpayers cannot be expected to undergo further proceedings because that would cause them disproportionate difficulties in terms of duration, complexity, and associated costs. The Supreme Tax Court is especially critical of the significant duration of the proceedings and the double cost risk that a taxpayer must take if he first must bring legal action against the tax assessment and, shortly thereafter, legal action against a negative decision in his quest for a equitable relief.

The Supreme Tax Court had already referred a similar question to the ECJ twice before in other contexts and different scenarios (regarding input VAT deduction and direct claims). In both cases, the ECJ – in the end - did not need to answer the question because it was no longer relevant in the case at hand due to other reasons. Therefore, and because the issue is still open for clarification, the Supreme Tax Court has again referred the question to the ECJ, this time with regard to the margin taxation.

After review and examination of **the previous case law of the ECJ**, the Supreme Tax Court 's preliminary conclusion is as follows:

In the case *Litdana* of 18 May 2017 C-624/15 the ECJ held, that Article 314 of the VAT Directive must be interpreted as precluding the competent authorities of a Member State from denying a taxable person the right to apply the margin scheme where he received an invoice that includes references relating both to the margin scheme and to exemption from VAT, even if it is apparent from a subsequent check carried out by those authorities that the taxable dealer supplying the second-hand goods had not actually applied that scheme to the supply of those goods, unless it is established by the competent authorities that the taxable person did not act in good faith or did not take every reasonable measure in his power to satisfy himself that the transaction carried out by him does not result in his participation in tax evasion.

This implies that, contrary to previous German practice, the margin scheme cannot be denied at the very earliest procedural stage (appeal against the tax assessment notice) on the grounds that the objective criteria are not met. The refusal to apply the margin taxation in the plaintiff's assessment procedure could therefore be contrary to EU law if the plaintiff was acting in good faith in this respect.

Issues of protection of legitimate expectations in matters of the margin scheme which are not already examined at the time of tax assessment create disproportionate difficulties for the taxable person as to length, complexity and costs associated with that additional legal procedure (ECJ, Opinion of 5 July 2017 in the case Geissel and Butin C-374/16 and C-375/16, para. 73). Those difficulties are, in the Opinion of the Advocate General Wahl, more significant when, for claims which essentially concern the same or related legal issues and/or the same or related transactions, the taxable person is required to commence, in parallel, two or more sets of judicial proceedings.

**If** protection of legitimate expectations were to be considered only in subsequent separate proceedings for equitable relief on the grounds of the concessionary rule under Section 227 Fiscal Code, the tax court of first instance would have been right to dismiss the action. The Supreme Tax Court would then have to reject the plaintiff's appeal as unfounded. **If, on the other hand,** protection of legitimate expectations must already be examined by appealing the tax assessment, the former court decision will have to be overturned as it had previously not examined whether such aspects would apply to the plaintiff, especially whether the plaintiff acted in good faith.

#### **Source:**

Supreme Tax Court decision of 19 February 2025 XI R 23/24 - published on 31 July 2025.

#### **Schlagwörter**

concession, good faith, waiver