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By PwC Deutschland | 01 May 2024

ECJ: Free-of-charge supplies of heat to other taxable persons subject to VAT at cost price

Following a request for a preliminary ruling from the Supreme Tax Court the European Court of Justice decided that the transfer free of charge of heat produced by a taxable person to other taxable persons is treated as a VATable supply of goods for consideration. It is irrelevant in that regard whether the recipients use the heat for purposes entitling to an input VAT deduction.

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Background

The plaintiff in the main proceedings (Y) operates a heat and power plant producing biogas. The biogas was used in 2008 for the decentralized production of electricity and heat. Most of the electricity generated was supplied to the general electricity grid and paid for by the grid operator. The heat generated during that operation was partly re-used in Y's production process.

In 2007, Y transferred 'free of charge' most of the heat produced to contractor A so that the latter could dry wood in containers and, in 2008, to company B, which used the heat for its asparagus fields. Both contracts specified that the amount of the payment was to be determined on an individual basis according to the economic situation of the user of the heat without that payment being specified in the contracts themselves.

Since Y did not invoice for the heat transferred to A and B, the tax office took the view that the heat was applied free of charge for the benefit of A and B. In the absence of a purchase price, the tax office calculated the taxable amount on the basis of cost, in accordance with Section 10(4) No. 1 VAT Act which provides that "the transaction is assessed (…) on the basis of the purchase price plus ancillary costs for the goods or for comparable goods or in the absence of a purchase price based on the production cost, in each case as at the transaction date".

ECJ decision

In answering **the first question** referred, the ECJ held that „*the transfer free of charge of heat produced by a taxable person to other taxable persons for the purposes of their economic activities constitutes a removal of, by that first taxable person, goods (assets) from his business free of charge, which is treated as a supply of goods for consideration, and irrespective whether the recipients use the heat for purposes that entitle them to an input VAT deduction*".

In order to avoid situations in which final consumption goes untaxed, the disposal free of charge of the goods removed (withdrawn) from a taxable persons business must be subject to subsequent taxation, irrespective of the recipient (with the exception the removal of goods for business use as samples or as gifts of small value (ECJ, judgment of 30 September 2010, *EMI Group* **C?581/08**, paragraph 19 and the case-law cited).

It follows that the imposition of VAT on the disposal of goods of free of charge, referred to in Article 16 (1) of the VAT Directive, has no exception other than that relating to transactions consisting of gifts of small value and samples coming within the scope of Article 16 (2) of the VAT Directive. In the present case, the heat disposed and transferred free of charge cannot be regarded as a gift of small value or a sample.

With regard to **the second and third questions** the ECJ states that (as to the cost price as basis for the VAT) „*the cost price (i. e. the cost to the business), within the meaning of that provision, includes not only direct manufacturing or production costs but also indirectly attributable costs, such as financing costs, whether or not those costs have been subject to input value added tax*".

Here, the ECJ notes that it is for the tax office to determine the cost price in the light of all the relevant

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factors and that this involves a detailed examination of the value elements that indicate that price, which must be determined at the time the removal from the business of Y was made. But it is in no way apparent from the wording of Article 74 of the VAT Directive that the cost price should be based solely on the direct manufacturing or production costs or on the costs which have been subject to input VAT.

Reference:

ECJ, judgment of 25 April 2024 (**C?207/23**), *Finanzamt X*.

Keywords

Supply of goods, free-of-charge