**Case C-174/08**

**NCC Construction Danmark A/S**

**v**

**Skatteministeriet**

(Reference for a preliminary ruling from the Østre Landsret)

(Sixth VAT Directive – Article 19(2) – Deduction of input tax – Hybrid taxable person – Goods and services used for both taxable and exempt activities – Calculation of the deductible proportion – Definition of 'incidental real estate transactions' – Self-supply – Principle of fiscal neutrality)

Summary of the Judgment

1. *Tax provisions – Harmonisation of laws – Turnover taxes – Common system of value added tax – Deduction of input tax – Goods and services used both for transactions in respect of which tax is deductible, and for transactions in respect of which tax is not deductible*

*(Council Directive 77/388, Art. 19(2))*

2. *Tax provisions – Harmonisation of laws – Turnover taxes – Common system of value added tax – Deduction of input tax*

*(Council Directive 77/388)*

1. Article 19(2) of the Sixth Directive 77/388 on the harmonisation of the laws of the Member States relating to turnover taxes is to be interpreted as meaning that the sale, in the case of a building business, of buildings constructed on its own account cannot be classified as an 'incidental real estate transaction' within the meaning of that provision, where that activity constitutes the direct, permanent and necessary extension of its business. In those circumstances, it is not necessary, in this case, to assess to what extent that sales activity, viewed separately, entails a use of goods and services on which value added tax is payable.

(see paras 34-35, operative part 1)

2. The principle of fiscal neutrality cannot preclude a building business, which is required to pay value added tax on supplies relating to construction effected on its own account (self-supply), from being unable fully to deduct the value added tax relating to the general costs incurred thereby, since the turnover from the sale of buildings thus constructed is exempt from value added tax.

Admittedly, that principle of fiscal neutrality was intended by the Community legislature to reflect, in matters relating to value added tax, the general principle of equal treatment. However, while that latter principle, like the other general principles of Community law, has constitutional status, the principle of fiscal neutrality requires legislation to be drafted and enacted, which requires a measure of secondary Community law. The principle of fiscal neutrality may, consequently, be the subject, in such a legislative measure, of detailed rules resulting from the application of Article 19(1) in conjunction with Article 28(3)(b) of the Sixth Directive 77/388 on the harmonisation of the laws of the Member States relating to turnover taxes, and point 16 of Annex F to that directive,

according to which a taxable person carrying out both taxable activities and exempt activities of selling real estate cannot deduct fully the value added tax on its general costs.

Furthermore, the principle of fiscal neutrality cannot properly be relied upon to preclude the application of the provisions of the Sixth Directive transposed by national legislation since, with the contested provisions transposing the Sixth Directive the national legislature, taking due account of the general principle of equal treatment and in order to avoid distortions of competition in the internal market, wished to put building businesses which carry on, beside their building activity, an exempt activity of selling real estate, on the same footing as building developers who, given the exempt nature of that latter activity, cannot deduct the value added tax on supplies relating to construction by third-party businesses to which they have recourse.

(see paras 41-43, 46-47, operative part 2)

JUDGMENT OF THE COURT (Fourth Chamber)

29 October 2009 (*)

(Sixth VAT Directive – Article 19(2) – Deduction of input tax – Hybrid taxable person – Goods and services used for both taxable and exempt activities – Calculation of the deductible proportion – Definition of ‘incidental real estate transactions’ – Self-supply – Principle of fiscal neutrality)

In Case C?174/08,

REFERENCE for a preliminary ruling under Article 234 EC by the Østre Landsret (Denmark), made by decision of 17 April 2008, received at the Court on 28 April 2008, in the proceedings

**NCC Construction Danmark A/S**

v

**Skatteministeriet,**

THE COURT (Fourth Chamber),

composed of K. Lenaerts, President of the Third Chamber, acting as President of the Fourth Chamber, R. Silva de Lapuerta, E. Juhász, G. Arestis and J. Malenovský (Rapporteur), Judges,

Advocate General: Y. Bot,

Registrar: C. Strömholm, Administrator,

having regard to the written procedure and further to the hearing on 23 April 2009,

after considering the observations submitted on behalf of:

– NCC Construction Danmark A/S, by B. Møll Pederson, advokat,

– the Danish Government, by B. Weis Fogh, acting as Agent, and by D. Auken, advokat,

– the Commission of the European Communities, by D. Triantafyllou and S. Schønberg, acting as Agents,

after hearing the Opinion of the Advocate General at the sitting on 18 June 2009,

gives the following

**Judgment**

1 This reference for a preliminary ruling concerns the interpretation of the second sentence of Article 19(2) of 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, p. 1) ('the Sixth Directive'), and the scope of the principle of fiscal neutrality with regard to turnover taxes.

2 The reference has been made in the course of proceedings between NCC Construction Danmark A/S ('NCC') and Skatteministeriet (Ministry of Fiscal Affairs) regarding the right to partial deduction of the value added tax ('VAT') on NCC's general costs.

**Legal context**

*Community legislation*

3 Under Article 2(1) of the Sixth Directive, the following is to be subject to VAT: 'the supply of goods or services effected for consideration within the territory of the country by a taxable person acting as such'.

4 Article 5(7)(a) of the Sixth Directive is worded as follows:

'Member States may treat as supplies made for consideration:

(a) the application by a taxable person for the purposes of his business of goods produced, constructed, extracted, processed, purchased or imported in the course of such business, where the [VAT] on such goods, had they been acquired from another taxable person, would not be wholly deductible'.

5 Article 6(3) of the Sixth Directive states:

'In order to prevent distortion of competition and subject to the consultations provided for in Article 29, Member States may treat as a supply of services for consideration the supply by a taxable person of a service for the purposes of his undertaking where the [VAT] on such a service, had it been supplied by another taxable person, would not be wholly deductible.'

6 Article 17(2)(a) of the Sixth Directive provides that, in so far as the goods and services are used for the purposes of his taxable transactions, the taxable person shall be entitled to deduct from the tax which he is liable to pay VAT due or paid within the territory of the country in respect of goods or services supplied or to be supplied to him by another taxable person.

7 It follows from Article 17(5) of the Sixth Directive that, as regards goods and services to be used by a taxable person both for transactions covered by Article 17(2) and (3) in respect of which VAT is deductible, and for transactions in respect of which VAT is not deductible, only such proportion of the VAT is to be deductible as is attributable to the former transactions. This

proportion is to be determined, in accordance with Article 19, for all the transactions carried out by the taxable person.

8 Article 19(1) and (2) of the Sixth Directive is worded as follows:

‘Calculation of the deductible proportion

(1) – The proportion deductible under the first subparagraph of Article 17(5) shall be made up of a fraction having:

– as numerator, the total amount, exclusive of [VAT], of turnover per year attributable to transactions in respect of which [VAT] is deductible under Article 17(2) and (3),

– as denominator, the total amount, exclusive of [VAT], of turnover per year attributable to transactions included in the numerator and to transactions in respect of which [VAT] is not deductible … .

The proportion shall be determined on an annual basis, fixed as a percentage and rounded up to a figure not exceeding the next unit.

(2) By way of derogation from the provisions of paragraph 1, there shall be excluded from the calculation of the deductible proportion, amounts of turnover attributable to the supplies of capital goods used by the taxable person for the purposes of his business. Amounts of turnover attributable to transactions specified in Article 13B(d), in so far as these are incidental transactions, and to incidental real estate and financial transactions shall also be excluded. …’

9 In accordance with the transitional provision provided for in Article 28(3)(b) of the Sixth Directive, the Member States may, during the transitional period referred to in Article 28(4), continue to exempt the activities set out in Annex F of that directive. Annex F includes, at point 16: ‘supplies of those buildings and land described in Article 4(3)’.

*National legislation*

10 The VAT law (Momsloven) transposes the Sixth Directive into Danish national law.

11 With regard to internal supplies to the business, Paragraph 6(1) of that law provides that VAT is payable by taxable persons who carry out building work and who, on their own account and on their own land, construct buildings for sale, whereas Paragraph 6(2) thereof provides that, for buildings for which VAT is to be paid under Paragraph 6(1), work carried out and materials used for that purpose are to be treated as supplies made for consideration and, accordingly, as supplies subject to tax.

12 Paragraph 13(1)(9) of the VAT law exempts the supply of real estate from VAT.

13 As regards the right to deduct, Paragraph 37 of the VAT law provides that ‘[r]egistered businesses may, in their input tax return, deduct the tax paid on purchases of goods and services used solely for the undertaking’s supplies which are not exempt under Paragraph 13’.

14 With regard to purchases intended for mixed use, Paragraph 38 of the VAT law provides that ‘[f]or goods and services which a registered business uses for purposes giving entitlement to deduction under Paragraph 37 as well as for other purposes of the business, a deduction may be made for that portion of the tax which is proportional to the turnover in the registrable part of the business. In the turnover declaration, account shall not be taken of turnover amounts relating to the supply of capital goods which have been used for the purposes of the business. … Nor shall

account be taken of turnover amounts attributable to incidental real estate transactions …'

## The dispute in the main proceedings and the questions referred for a preliminary ruling

15 NCC is a building and contracting business. It carries out construction projects, including in particular engineering, planning, consultancy and labour activities in the building sector on behalf of other parties and on its own account.

16 The sale of real estate constructed on its own account is not the applicant's principal activity, but rather a separate activity which derives from the building work subject to VAT.

17 Since the Danish VAT law exempts the sale of buildings constructed on its own account from VAT, NCC was required, as a hybrid taxable person, to calculate a proportion in order to establish the amount in respect of which it had a right to deduct VAT on the costs common to its two activities (general costs).

18 For the purpose of that calculation, NCC did not take into consideration the turnover from the sale of buildings constructed on its own account. It submitted that that activity of selling real estate should be regarded as an 'incidental real estate transaction' within the meaning of the second sentence of Article 19(2) of the Sixth Directive.

19 The Danish tax authorities changed their practice as from 1 April 2002, taking the view that the activity of selling real estate carried out by a building business could not be treated in the same way as an 'incidental real estate transaction'. The result for the company was that input VAT on its common costs was thereafter only partially deductible.

20 NCC, which sought to benefit from full deduction of VAT attributable to its common costs, disputed the view of Skatteministeriet.

21 In those circumstances, the Østre Landsret decided to stay proceedings and to refer the following questions to the Court for a preliminary ruling:

'1. Is the term "incidental real estate transactions" in the second sentence of Article 19(2) of the Sixth Directive ... to be interpreted as covering the activities of a taxable building business in connection with the subsequent sale of buildings constructed by the building business on its own account, as an activity fully subject to VAT, with a view to resale?

2. Does the answer to question 1 depend on the extent to which the sales activities, viewed separately, entail the use of goods and services on which VAT is payable?

3. Is it consistent with the principle of neutrality of VAT for a building business which, under the legislation of the Member State in question – based on Article 5(7) and Article 6(3) of the Sixth Directive – is required to pay VAT on its internal supplies in connection with the construction of buildings on its own account with a view to their subsequent sale, to have only a partial right to deduct VAT for general costs incurred in the building business, on the ground that the subsequent sale of the real estate is, under the Member State's VAT legislation, exempt from VAT on the basis of Article 28(3)(b) of the Sixth Directive …, read in conjunction with point 16 of Annex F?'

## The questions referred

*The first and second questions*

22 By its first two questions, which it is appropriate to examine together, the referring court seeks essentially to ascertain, first, whether Article 19(2) of the Sixth Directive is to be interpreted

as meaning that the sale, by a building business, of buildings constructed on its own account can be classified as an ‘incidental real estate transaction’ within the meaning of that provision and, next, whether, in the context of that classification, it is appropriate, in this case, to assess to what extent that activity, viewed separately, entails a use of goods and services on which VAT is payable.

23 It should be borne in mind at the outset that, in determining the scope of a provision of Community law, its wording, context and objectives must all be taken into account (Case C?162/91 *Tenuta il Bosco* [1992] ECR I?5279, paragraph 11; Case C?315/00 *Maierhofer* [2003] ECR I?563, paragraph 27; and Case C?280/04 *Jyske Finans* [2005] ECR I?10683, paragraph 34).

24 Furthermore, it follows from the need for uniform application of Community law and from the principle of equality that the terms of a provision of Community law which makes no express reference to the law of the Member States for the purpose of determining its meaning and scope must normally be given an autonomous and uniform interpretation throughout the Community (see to that effect, inter alia, Case C?321/02 *Harbs* [2004] ECR I?7101, paragraph 28, and Case C?195/06 *Österreichischer Rundfunk* [2007] ECR I?0000, paragraph 24).

25 In that regard, Article 19(2) of the Sixth Directive makes no express reference to the law of the Member States for the purpose of determining its meaning and scope and its terms do not, by themselves, with certainty permit the inference that it covers an activity such as that at issue in the main proceedings.

26 In those circumstances, it is important to take into account the context and objectives of that provision.

27 As regards, first, its context, Article 19 of the Sixth Directive is part of Title XI thereof, which sets out the rules governing deduction. The right to deduct, which is laid down in Article 17(2) of that directive, and relates to the input tax on the goods and services used by the taxable person for the purposes of his taxable transactions, is meant to relieve the trader entirely of the burden of the VAT payable or paid in the course of all his economic activities. The common system of VAT consequently ensures complete neutrality of taxation of all economic activities, provided that they are themselves subject in principle to VAT (see, inter alia, Case C?435/05 *Investrand* [2007] ECR I?1315, paragraph 22 and the case-law cited).

28 Where the taxable person effects both taxable transactions, in respect of which VAT is deductible, and exempt transactions, in respect of which VAT is not deductible, Article 17(5) of the Sixth Directive provides that only such proportion of the VAT is deductible as is attributable to the taxable transactions. That proportion is to be calculated according to the detailed rules set out in Article 19 of that directive.

29 While Article 19(1) of that directive provides that the deductible proportion is to be made up of a fraction having, as numerator, the turnover attributable to taxable transactions and, as denominator, the total turnover, Article 19(2) provides that, by way of derogation, amounts of, inter alia, turnover attributable to ‘incidental real estate transactions’ are to be excluded. However, there is no definition of an ‘incidental real estate transaction’ in the Sixth Directive.

30 As regards, next, the objective of Article 19(2), this is, in particular, apparent from the Explanatory Memorandum to the proposal for the Sixth Directive, which was submitted by the Commission of the European Communities to the Council of the European Communities on 29 June 1973 (see Bulletin of the European Communities, supplement 11/73, p. 20). In the words of that Memorandum ‘[t]he factors mentioned in this paragraph must be excluded from the calculation of the proportion lest, being unrepresentative of the taxable person’s business activity, they should

deprive the amount of any real significance. Such is the case with sales of capital items and real estate and financial transactions which are only ancillary operations, that is to say are only of secondary importance in relation to the total turnover of the business. These factors are only excluded if they are not part of the usual business activity of the taxable person'.

31 In that regard, as is apparent from the case-law of the Court in which it took that objective as its basis, an economic activity cannot be classified as 'incidental' for the purposes of Article 19(2) of the Sixth Directive if it constitutes the direct, permanent and necessary extension of the business (Case C?306/94 *Régie dauphinoise* [1996] ECR I?3695, paragraph 22), or if it entails a significant use of goods and services subject to VAT (Case C?77/01 *EDM* [2004] ECR I?4295, paragraph 76).

32 It is therefore in the light of that case-law that the Court must reply to the question referred by the national court.

33 With regard to the fulfilment of the first condition, the sale of buildings that a building company has built on its own account cannot be regarded as an activity incidental to its taxable business activity, which consists of the construction of buildings on behalf of third parties or on its own account. Indeed, as it arises from the same construction activity, it is a direct extension thereof. The general organisation of its activities requires it, from the start and on a regular and permanent basis, to plan the construction of a certain number of buildings on its own account, however few they may be, which it intends subsequently to sell itself. The resulting activity of sales of real estate does not therefore appear to be incidental, but is the necessary consequence of a deliberate intention on the part of the company to develop in the context of its business, the activity of selling buildings which it has constructed on its own account. It contributes to the business objectives of the taxable person and is carried out with a commercial purpose (see, by analogy, *EDM*, paragraph 67).

34 In those circumstances, an activity of selling real estate, such as that at issue in the main proceedings, must be regarded as constituting the direct, permanent and necessary extension of the taxable business of the company, and it is not necessary, in this case, to assess to what extent that sales activity, viewed separately, entails a use of goods and services on which VAT is payable.

35 Having regard to the foregoing considerations, the answer to the first two questions is that Article 19(2) of the Sixth Directive is to be interpreted as meaning that the sale, in the case of a building business, of buildings constructed on its own account cannot be classified as an 'incidental real estate transaction' within the meaning of that provision, where that activity constitutes the direct, permanent and necessary extension of its business. In those circumstances, it is not necessary, in this case, to assess to what extent that sales activity, viewed separately, entails a use of goods and services on which VAT is payable.

*The third question*

36 By its third question, the referring court essentially asks the Court whether it is consistent with the principle of fiscal neutrality for a building business, which is required to pay VAT on supplies relating to construction effected on its own account (self-supply), not to be able fully to deduct the VAT relating to the general costs incurred thereby, since the turnover from the sale of buildings thus constructed is exempt from VAT.

37 NCC claims that, although the turnover from its activity of selling real estate is exempt from VAT, the activity of constructing buildings on its own account was taxed (as self-supply and notwithstanding the lack, by definition, of corresponding turnover) on the basis of the cost price of

that activity plus the normal profit margin in that sector of activity. In those circumstances, NCC maintains that, although subject to VAT, it has been deprived of the possibility of obtaining reimbursement of VAT relating to goods and services (general costs) used for the purposes of a taxed activity (the construction of buildings on its own account). It maintains that such a situation is not consistent with the requirements of the principle of fiscal neutrality.

38 Furthermore, NCC asserts that the particular manner in which the Kingdom of Denmark has chosen to implement the exemption provisions of the Sixth Directive means that it is placed in a worse position than building businesses under that directive, according to which they are entitled to full VAT deduction for all general costs.

39 First of all, it should be noted that the principle of fiscal neutrality resulting from the provisions of Article 17(2) of the Sixth Directive implies that a taxable person may deduct all the VAT levied on goods and services acquired for the exercise of his taxable activities (see, to that effect, Case C?98/07 *Nordania Finans and BG Factoring* [2008] ECR I?1281, paragraph 19).

40 In that regard, it is necessary to add that, according to settled case-law, the principle of fiscal neutrality, and, in particular, the right to deduct, as an integral part of the VAT scheme, is a fundamental principle underlying the common system of VAT established by the relevant Community legislation (see Case C?25/07 *Sosnowska* [2008] ECR I?5129, paragraphs 14 and 15, and Case C?74/08 *PARAT Automotive Cabrio* [2009] ECR I?0000, paragraph 15).

41 That principle of fiscal neutrality was intended by the Community legislature to reflect, in matters relating to VAT, the general principle of equal treatment (see, to that effect, Case C?309/06 *Marks & Spencer* [2008] ECR I?2283, paragraph 49, and the case-law cited).

42 However, while that latter principle, like the other general principles of Community law, has constitutional status, the principle of fiscal neutrality requires legislation to be drafted and enacted, which requires a measure of secondary Community law (see, by analogy, with regard to the protection of minority shareholders, Case C?101/08 *Audiolux and Others* [2009] ECR I?0000, paragraph 63).

43 The principle of fiscal neutrality may, consequently, be the subject, in such a legislative measure, of detailed rules, such as those, implemented in Danish law, resulting from the application of Article 19(1) in conjunction with Article 28(3)(b) of the Sixth Directive, and point 16 of Annex F to that directive, according to which a taxable person carrying out both taxable activities and exempt activities of selling real estate cannot deduct fully the VAT on its general costs.

44 It is also appropriate to point out that the general principle of equal treatment, of which the principle of fiscal neutrality is a particular expression at the level of secondary Community law and in the specific area of taxation, requires similar situations not to be treated differently unless differentiation is objectively justified (*Marks & Spencer*, paragraph 51 and the case-law cited). It requires, in particular, that different types of economic operators in comparable situations be treated in the same way in order to avoid any distortion of competition within the internal market, in accordance with the provisions of Article 3(1)(g) EC.

45 In implementing the provisions of the Sixth Directive, the Member States were obliged to take into account the principle of equal treatment, like the other general principles of Community law, which, having constitutional status, bind those Member States when they take action in the field of Community law (see, to that effect, Case C?107/97 *Rombi and Arkopharma* [2000] ECR I?3367, paragraph 65, and Case C?396/98 *Schloßstrasse* [2000] ECR I?4279, paragraph 44).

46 As is apparent from the pleadings of the Danish Government, with the contested provisions

transposing the Sixth Directive the Danish legislature, taking due account of the general principle of equal treatment and in order to avoid distortions of competition in the internal market, wished to put building businesses which, like NCC, carry on, beside their building activity, an exempt activity of selling real estate, on the same footing as building developers who, given the exempt nature of that latter activity, cannot deduct the VAT on supplies relating to construction by third-party businesses to which they have recourse. In those circumstances, the principle of fiscal neutrality cannot properly be relied upon to preclude the application of the provisions thus transposed.

47 Having regard to the foregoing considerations, the answer to the third question is that the principle of fiscal neutrality cannot preclude a building business, which is required to pay VAT on supplies relating to construction effected on its own account (self-supply), from being unable fully to deduct the VAT relating to the general costs incurred thereby, since the turnover from the sale of buildings thus constructed is exempt from VAT.

**Costs**

48 Since these proceedings are, for the parties to the main proceedings, a step in the action pending before the national court, the decision on costs is a matter for that court. Costs incurred in submitting observations to the Court, other than the costs of those parties, are not recoverable.

On those grounds, the Court (Fourth Chamber) hereby rules:

1. **Article 19(2) of the 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 is to be interpreted as meaning that the sale, in the case of a building business, of buildings constructed on its own account cannot be classified as an 'incidental real estate transaction' within the meaning of that provision, where that activity constitutes the direct, permanent and necessary extension of its business. In those circumstances, it is not necessary, in this case, to assess to what extent that sales activity, viewed separately, entails a use of goods and services on which value added tax is payable.**

2. **The principle of fiscal neutrality cannot preclude a building business, which is required to pay value added tax on supplies relating to construction effected on its own account (self?supply), from being unable fully to deduct the value added tax relating to the general costs incurred thereby, since the turnover from the sale of buildings thus constructed is exempt from value added tax.**

[Signatures]

* Language of the case: Danish.