ECJ rules on VAT treatment of business samples and promotional goods

The European Court of Justice (ECJ) issued an important decision on 30 September 2010 on the VAT treatment of sample goods and business gifts given free of charge by a music company in the course of promoting its artists (EMI Group Ltd. v. The Commissioners for Her Majesty’s Revenue & Customs (Case C-581/08)). In the taxpayer favorable decision, the Court ruled that no VAT is due on free sample CDs given to promoters and the media to promote the music. The ECJ broadly followed the 15 April 2010 opinion of Advocate General Jääskinen.

Background

EMI Group Limited (EMI), a U.K. company engaged in the production and sale of recorded music and music publishing, distributed free copies of recordings (including on CDs) to various persons to promote newly released music. Some CDs were given to individuals who were in a position to assess the commercial quality of the recording and influence the level of exposure of the artist, such as individuals working in media and music promoters, who further distributed the CDs to their own contacts. It is common practice in the music industry for many sample CDs to be distributed to “pluggers” who then send the CDs on to their contacts in the music industry to promote the new music.

Under U.K. law, VAT must be charged on all but one sample given to the same person. From 1987 until 2003, EMI accounted for VAT on the promotional CDs, but the company later took the position that no VAT was due and requested a VAT refund on the grounds that U.K. legislation failed properly to implement a provision of the Sixth VAT Directive (i.e. article 5(6)). Article 5(6) provides that goods used for business purposes as samples or gifts of small value should not be treated as a supply of goods for consideration. The U.K. tax authorities rejected EMI’s claim that VAT should not be paid on the distributed free copies of music recordings.

The case was heard before the U.K. VAT Tribunal in 2004 and the Tribunal decided to refer questions to the ECJ to consider the interpretation of the terms “samples” and “gifts of small value.”

ECJ decision

The ECJ has clarified the definition of a sample to mean a specimen of a product that is intended to promote the sale of that product. Importantly, the ECJ recognized that it may be necessary for a number of samples to be distributed to the same recipient; for example, in EMI’s case, music promoters received multiple sample CDs and distributed these to their own contacts in the music industry and the media. The ECJ suggested that, to prevent the risk of samples getting into the supply chain, Member States may require taxpayers distributing samples to take certain precautions, such as mandatory labeling.

The ECJ also held that Member States may set a ceiling for the value of small value gifts (so the U.K.’s annual limit of GBP 50 for gifts is compatible with EC VAT law). However, the Court said that national legislation must not prevent multiple gifts being given to different individuals with the same employer.

Businesses affected

This is an important case that impacts any business that distributes or wishes to distribute “samples” or “gifts of small value” in EU countries where the rules are similar to those applying in the U.K. In light of the ECJ decision, the U.K. and several other EU Member States likely will be forced to change their rules on the VAT treatment of samples and business gifts. Businesses that have accounted for VAT, or not reclaimed the appropriate VAT on samples or business gifts, should consider submitting retrospective claims as soon as possible, if they have not already done so.

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