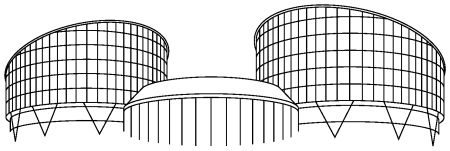

EUROPEAN COURT OF HUMAN RIGHTS
COUR EUROPÉENNE DES DROITS DE L'HOMME

FOURTH SECTION

DECISION

Application no. 39689/05
Krasimir Milchev ATEV
against Bulgaria

The European Court of Human Rights (Fourth Section), sitting on 18 March 2014 as a Chamber composed of:

Ineta Ziemele, *President,*
Päivi Hirvelä,
George Nicolaou,
Nona Tsotsoria,
Zdravka Kalaydjieva,
Krzysztof Wojtyczek,
Faris Vehabović, *judges,*

and Fatoş Aracı, *Deputy Section Registrar,*

Having regard to the above application lodged on 28 October 2005,

Having regard to the observations submitted by the respondent Government and the observations in reply submitted by the applicant,

Having deliberated, decides as follows:

THE FACTS

1. The applicant, Mr Krasimir Milchev Atev, is a Bulgarian national, who was born in 1962 and lives in Troyan.

2. The Bulgarian Government ("the Government") were represented by their Agent, Mrs N. Nikolova, of the Ministry of Justice.

A. The circumstances of the case

3. The facts of the case, as submitted by the parties, may be summarised as follows.

1. Background information

4. The applicant was born in 1962 and lives in Troyan. He is a sole trader, registered on an unspecified date under the name ET Atev – Krasimir Atev, with an office in Letnitsa. He is engaged in various commercial activities. Under Bulgarian law his business does not have a distinct legal personality.

5. In 1994 the applicant registered his business for value-added tax ("VAT").

6. In December 1998 and December 1999 the applicant purchased electrical devices from another sole trader ("the supplier"). The supplier issued the relevant invoices and, as it appears, indicated on them the VAT charged. In 2000 the tax authorities conducted a VAT audit of the supplier. On 15 May 2000 he was issued with a tax assessment which made no mention of the goods supplied in December 1998 and December 1999.

2. The 2003 tax assessment and appeal proceedings

7. In June 2003 the Lovech Territorial Tax Directorate conducted a VAT audit of the applicant for the periods, in particular, from 1 to 31 December 1998 and from 1 to 31 December 1999. On 18 July 2003 it issued him with a tax assessment whereby it refused him the right to deduct the VAT of 19,570.78 Bulgarian levs (BGN), (9,980 euros (EUR)), which the supplier had charged him in December 1998 and December 1999. It also ordered that interest be paid in the amount of BGN 12,312.02 (EUR 6,278).

8. The applicant appealed against the 2003 tax assessment. On 17 September 2003 the director of the Veliko Turnovo Territorial Tax Directorate upheld the 2003 tax assessment in its entirety. The authorities stated that in order to recognise the applicant's entitlement to have the input VAT deducted, the VAT had to be entered in the accounting records of the supplier (see paragraph 13 below). Therefore, they would have to cross-check those records and verify that the VAT had been properly reflected as an obligation to the State budget. When the cross-check was carried out, however, the supplier declared that the relevant accounting records had been lost. Since the authorities could not verify whether the VAT had been reflected accordingly, they refused to deduct it. As for the applicant's argument that his supplier's 2000 tax assessment did not contain any irregularities regarding the said supplies, the authorities dismissed it as being irrelevant for the proceedings at issue.

9. The applicant sought judicial review. During the proceedings and following a request on the part of the applicant, the Veliko Turnovo Regional Court ordered an expert report. The applicant put questions to the expert. In a judgment of 30 July 2004 the court dismissed the applicant's appeal and upheld the 2003 tax assessment. The court found that the tax authorities' refusal to recognise the applicant's right to have the VAT he

had paid deducted was correct because the supplier's accounting records had been lost, making it objectively impossible to verify whether the VAT had been properly charged and reflected as an obligation to the State budget. The court also noted that although the applicant had had an opportunity to do so, he had not questioned the expert about those supplies and had failed to rebut the statements of the tax authorities in the tax assessment.

10. The applicant lodged a cassation appeal, and in a final judgment of 10 May 2005 the Supreme Administrative Court upheld the tax assessment. The court found that during the proceedings the applicant had submitted only documents originating from his own accounting records. Those documents, however, could not have served as evidence given the subject matter of the case. The court further noted that the applicant had failed to question the expert about the contested supplies. Having regard to the applicant's failure to rebut the authorities' findings and in the absence of the supplier's accounting records, the court concluded that it had been impossible to establish whether the VAT had been entered in them, which was one of the pre-conditions *sine qua non* for allowing the applicant to have the input VAT deducted.

3. Other developments

11. It is unclear whether the supplier was penalised for his failure to keep his accounting records diligently and in line with the relevant domestic provisions (see paragraph 16 below).

12. On an unspecified date the applicant paid part of the debt under the 2003 tax assessment, namely BGN 5,132.63 (EUR 2,624). In 2005 enforcement proceedings were instituted against the applicant for the collection of the remaining debt. It is unclear how the proceedings unfolded until 2010, when they were apparently resumed. The proceedings were still pending at the time of the latest information from the applicant.

B. Relevant domestic law and practice

1. Relevant VAT legislation and the Accountancy Act 2001

13. Under the VAT Act 1993, input VAT, referred to as "tax credit" in domestic legislation, was the amount of VAT which a taxable person had been charged on goods or services received under a chargeable transaction or from the importing of goods or services (section 24(1)). The VAT was to be charged by the supplier (section 24(2)(2)). The recipient should have been in possession of a VAT invoice which met the statutory requirements (section 24(2)(6)). In order for the recipient to have the right to deduction of VAT, it was mandatory for the supplier to have reflected the VAT charged to the recipient in his accounting records as an obligation to the State budget

(section 24(2)(2) with reference to paragraph 3(e) of the Additional Provisions of the VAT Act 1993).

14. The relevant provisions of the VAT Act 1999, which replaced the 1993 Act, are summarised in the case of *Bulves AD v. Bulgaria* (no. 3991/03, §§ 20-28, 22 January 2009). In particular, the supplier's obligation to reflect the VAT that he has charged in his accounting records remained unchanged (section 64(1)(2) in relation to section 55(6) of the 1993 Act).

15. The VAT Act 2007 replaced the 1994 Act to include in national legislation the latest EU legislation in the sphere of VAT. The explicit requirement that, in order for the right to have input VAT deducted to arise, the supplier had to have reflected it in his accounting records, was abandoned.

16. Pursuant to the Accountancy Act 2001, accounting documents relating to tax obligations must be maintained by the trader for a period of up to five years after the expiry of the statutory time-limit for the relevant obligation (section 42(1)(3)). Failure to observe that obligation is sanctioned by an administrative penalty (section 47(4)).

2. Civil proceedings for damages against the supplier

17. The general rules of the law of tort are set out in sections 45 to 54 of the Obligations and Contracts Act 1951 ("the 1951 Act"). Section 45(1) provides that everyone is obliged to make good the damage which they have, through their fault, caused to another. Under section 45(2), fault is presumed until proved otherwise.

18. In that connection, a recipient may successfully seek pecuniary damages from a supplier when the latter has acted in violation of the relevant VAT provisions, resulting in the authorities' refusal to deduct the input VAT (for example, if the supplier has failed to issue an invoice and to enter the tax in its accounting records, issued invoices but failed to enter the tax in its monthly declaration to the authorities, or failed to submit the relevant documents proving that he has discharged his VAT reporting obligations to the authorities) (реш. № 1158 от 5 ноември 2008 г. на ВКС по гр. д. № 3225/2007 г., IV г. о.; опр. № 55 от 3 февруари 2009 г. на ВКС по т. д. № 742/2008 г., II т. о.; опр. № 170 от 30 декември 2008 г. на ВКС по т. д. № 480/2008 г., II т. о.; реш. № 304 от 20 октомври 2005 г. на АС-Велико Търново по гр. д. № 151/2005 г.; реш. № 110 от 9 юли 2010 г. по в. т. д. № 41/2009 г. на АС-Варна; реш. от 10 юни 2010 г. на ОС-Стара Загора по гр. д. № 1164/2009 г.; реш. № 476 от 9 май 2011 г. на РС-Велико Търново по гр. д. № 4230/2010 г.). The compensation granted for the pecuniary damage suffered is usually in the amount of the paid VAT plus the relevant interest.

3. State liability for damages

19. Section 1 of the State and Municipalities Responsibility for Damage Act 1988 (*Закон за отговорността на държавата и общините за вреди* – "the 1988 Act") provides that the State and municipalities are liable for damage suffered by individuals (and since 1 January 2006 also legal persons) as a result of unlawful decisions, actions or omissions by their organs and officials committed in the course of, or in connection with, the carrying out of administrative action.

COMPLAINT

20. The applicant complained about the tax authorities' refusal to recognise his right to have input VAT deducted on account of his supplier's failure to provide evidence that he had complied with his own VAT reporting obligations. He relied, in particular, on Articles 3, 5 § 1, 6 § 1, 8 § 1, 13 and 14 of the Convention and Article 1 of Protocol No. 1 thereto.

THE LAW

21. Relying on Articles 3, 5 § 1, 6 § 1, 8 § 1, 13 and 14 of the Convention and Article 1 of Protocol No. 1 thereto, the applicant complained about the tax authorities' refusal to recognise his right to have input VAT deducted on account of his supplier's failure to discharge his own VAT-reporting obligations. His complaint falls to be examined solely under Article 1 of Protocol No. 1, which reads as follows:

> "Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.
>
> The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties."

22. The Government submitted that the applicant had failed to exhaust domestic remedies because he had not lodged a claim for compensation against his supplier under the 1951 Act (see paragraphs 17-18 above). Nor had he brought a claim against the relevant authorities under section 1 of the 1988 Act (see paragraph 19 above). The Government further submitted that the present case differed from *Bulves AD* (cited above). They argued that the applicant had not been diligent in complying with his VAT-reporting

obligations because he had accepted invoices issued by his supplier in which the relevant VAT had not been properly indicated. The Government further stated that the authorities' decision to refuse to deduct the VAT had been correct because the supplier had not inserted the charged VAT in his accounting records and, consequently, the VAT had not been paid by the supplier. The Government argued that in order to safeguard fiscal stability, in such cases the authorities had to impose the burden to pay the relevant VAT on the recipient, in this case the applicant. The Government also maintained that, despite the procedural opportunity to do so, the applicant had failed to rebut the findings of the tax authorities during the court proceedings. Lastly, the Government pointed out, as a positive development, the fact that the VAT Act 2007 did not contain such a requirement in order for the right to have VAT deducted to arise.

23. The applicant maintained his complaints that the authorities had applied an automatic approach and had unfairly refused to recognise his right to have the input VAT deducted.

24. The Court notes at the outset the Government's contention that the applicant could have brought a claim for compensation against the supplier under section 45 of the 1951 Act before the civil courts in order to vindicate his right. While admittedly suing a private individual cannot be regarded as a remedy for the purposes of exhaustion of domestic remedies in respect of an act on the part of the State (see *Pine Valley Developments Ltd and Others v. Ireland*, judgment of 29 November 1991, Series A no. 222, p. 22, § 48; and *Zlínsat, spol. s r.o., v. Bulgaria*, no. 57785/00, § 55, 15 June 2006), the Court sees no reason why it could not be taken into account, together with other relevant factors, in the overall assessment as to whether the necessary balance between the public and private interest was achieved. For that reason, the issue is examined in the following paragraphs in the context of the proportionality analysis.

25. As for the Government's objection that the applicant could have brought a claim for damages against the tax authorities under section 1 of the 1988 Act, the Court considers that it need not decide on this issue, as the complaint is in any event manifestly ill-founded for the following reasons.

26. The Court notes that it is not in dispute between the parties that the matters complained of constituted an interference with the peaceful enjoyment of the applicant's possessions. In the case of *Bulves AD* (cited above, §§ 53-58) the Court accepted that in a similar situation Article 1 of Protocol No. 1 to the Convention was applicable. The Court sees no reason to depart from that approach and accepts that the authorities' refusal to allow VAT deduction interfered with the applicant's property rights.

27. The Court further considers that the impugned interference was lawful and pursued a legitimate aim in the public interest: to secure the payment of the VAT.

28. However, even if it is lawful and in the public interest, an interference with the right to the peaceful enjoyment of possessions must strike a fair balance between the demands of the general interest and the applicant's rights. In particular, there must be a reasonable relationship of proportionality between the means employed and the aim sought to be realised (see, among many other authorities, *Sporrong and Lönnroth v. Sweden*, 23 September 1982, § 69, Series A no. 52).

29. In this connection, the Court notes that it has recognised that the Contracting States have a wide margin of appreciation when passing laws for the purpose of securing the payment of taxes (see *Gasus Dosier- und Fördertechnik GmbH v. the Netherlands*, 23 February 1995, § 60, Series A no. 306-B; *AGOSI v. the United Kingdom*, 24 October 1986, § 52, Series A no. 108; *Jokela v. Finland*, no. 28856/95, § 57, ECHR 2002-IV; and *Bulves AD*, cited above, § 63). Decisions in this area commonly involve the consideration of political, economic and social questions which the Convention leaves within the competence of the Contracting States. The Court therefore respects the legislature's assessment unless it is devoid of reasonable foundation (see *National & Provincial Building Society, Leeds Permanent Building Society and Yorkshire Building Society v. the United Kingdom*, 23 October 1997, §§ 80-82, *Reports of Judgments and Decisions* 1997-VII; *Nazarev and Others v. Bulgaria* (dec.), no. 26553/05 et al., 25 January 2011; and *M.A. and 34 Others v. Finland* (dec.), no. 27793/95, 10 June 2003).

30. In the case of *Bulves AD* (cited above, § 71) the Court considered the wide margin of appreciation given to States in taxation matters. It found that the interference was disproportionate as a result of a rigid interpretation of the relevant legislation by the domestic authorities. The refusal to deduct VAT had been automatic and carried out without an adequate review of relevant factors such as (i) the timely and full discharge by the applicant company of its VAT reporting obligations; (ii) the applicant company's inability to secure compliance by its supplier with its VAT reporting obligations; and (iii) the fact that there was no fraud in relation to the VAT system of which the applicant company had knowledge or the means of obtaining such knowledge. However, in the case of *Bulves AD* (cited above, § 50) the Court did not have at its disposal examples of relevant domestic judgments and therefore did not examine, in the context of the proportionality analysis, the possibility of the applicant company to lodge a claim for damages before the civil courts in order to seek compensation from its supplier for the authorities' refusal to deduct the VAT charged.

31. Turning to the case at hand, the Court will first examine the three relevant factors set out in the case of *Bulves AD*. The Court notes in this regard that in the course of the domestic proceedings there has been no statement made by the relevant domestic authorities, and no indication whatsoever that the applicant did not discharge on time and in full his VAT

reporting obligations. Such an argument was raised for the first time in the respondent Government's observations. However, they failed to submit any documents (including copies from the contested invoices) to corroborate their suggestion. Therefore, the Court, based on the evidence at its disposal, will proceed on the basis that the applicant complied diligently with the relevant VAT provisions. Furthermore, the Court cannot overlook the fact that the tax authorities imposed the burden of the supplier's failure to maintain his accounting records entirely on the applicant (see paragraphs 8-10 above*)*. The authorities did so despite the fact that the applicant did not have the power to secure compliance by the supplier with either his VAT reporting obligations or the requirements of the Accountancy Act 2001. Moreover, there is no indication that there was any fraud in relation to the VAT system of which the applicant had knowledge or the means of obtaining such knowledge.

32. Bearing in mind the above, the Court observes that the same factors which were considered as relevant for the proportionality analysis in the case of *Bulves AD* were also not properly reviewed by the domestic authorities in the present case. No particular weight was attached to them in deciding whether the applicant had the right to have the input VAT deducted. In conclusion, in the case at hand the authorities applied a similar rigid approach towards the applicant (compare and contrast *Nazarev and Others*, cited above, where the applicants' complaints were declared inadmissible because the domestic authorities had carried out a thorough and individualised review of the relevant circumstances).

33. The Court will now examine whether the combination of other relevant factors, such as the possibility for the applicant to bring civil proceedings against his supplier and the importance of the public interest within the context of the State's wide margin of appreciation were sufficient to counterbalance that state of affairs.

34. In this connection, the Court notes that at the time of the events the applicant had at his disposal a tort claim under the 1951 Act. As evident by the case-law referred to in paragraph 18 above, when applying the 1951 Act in similar situations, the domestic courts examined claims against non-diligent suppliers and granted compensation for pecuniary damage in the amount of the VAT paid plus the relevant interest. In the case at hand, the uncertainty as to whether the supplier did settle his obligations towards the tax authorities, the objective impossibility for the authorities to establish that, and their final goal to secure payment of taxes led to the imposition of the tax burden on the applicant. At the same time, by not keeping his accounting records for the statutory period, the supplier was clearly in breach of the relevant provisions and thus the applicant's claim had reasonable prospects of success. In conclusion, the Court considers that in the present circumstances a claim under the 1951 Act, had the applicant made recourse to it, could have provided adequate redress.

35. The Court takes note of the Government's position that fiscal stability, which is undoubtedly of public interest, must be protected by measures directed at ensuring the payment of taxes. It reiterates that fiscal stability may require a complex system of rules regarding charges, exemptions, deductions and reimbursements aimed at preserving financial stability and the proper collection of VAT (see *Bulves AD*, cited above, § 65). Still in the context of the public interest, the Court is in principle ready to accept a more rigid approach applied by the authorities towards diligent traders with the aim of securing the collection of taxes (see, for example, *Gasus Dosier- und Fördertechnik GmbH*, cited above, § 61). In the present case, the Court considers that the rule that any VAT charged must be reflected in the accounting records of the supplier in order for the recipient to have the right to deduction of the input VAT, despite its stringency and subsequent abandonment (see paragraph 15 above), fell within the State's margin of appreciation and served as a guarantee of the actual payment of that tax.

36. The Court further notes that in contrast to the case of *Bulves AD*, where albeit with some delay, the applicant company's supplier had paid the VAT due on the chain of supplies and for that reason the refusal to allow the applicant company to deduct the input VAT was not justified by any indication of negative repercussions on the State budget (see *Bulves AD*, cited above, §§ 67-68), in the present case the absence of the supplier's accounting records objectively impeded a proper verification of these circumstances. In this regard the interference with the applicant company's interests in the case of *Bulves AD* was entirely attributable to the authorities' automatic approach and not to the supplier's conduct. In contrast to the case of *Bulves AD* in the case at hand the actions of the authorities pursued the public interest of maintaining fiscal stability and securing the collection of taxes, which is inherent in any taxation system. The Court considers that in so far as the interference with the applicant's rights in the present case was triggered by the supplier's failure to maintain diligently his accounting records and resulted in a similarly automatic approach of the authorities towards the applicant, this situation was further balanced by the possibility of the applicant to seek and obtain compensation from his supplier within the framework of civil proceedings for damages. For the Court, and having in mind the wide margin of appreciation given to States in the area of taxation matters, that suffices for the conclusion that in the case at hand, a fair balance was struck between the protection of the applicant's rights and the demands of the general interest.

37. Accordingly, the Court finds that the complaint is manifestly ill-founded and must be rejected in accordance with Article 35 §§ 3 (a) and 4 of the Convention.

For these reasons, the Court unanimously

Declares the application inadmissible.

Fatoş Aracı	Ineta Ziemele
Deputy Registrar	President