



VAT alert Belgium

CJEU advocates broad application of VAT on early termination fees

On 11 June 2020, [the CJEU confirmed](#) that amounts received by an economic operator after an early termination of a service contract that requires a customer to comply with a tie-in period, are considered as remuneration for a supply of services, and therefore subject to VAT. This is also the case where the early termination charge is less than the amount that the provider would have received if services would have continued for the remainder of the contract.

Background

Vodafone (Portuguese branch), concludes telecommunication service contracts with its customers. Some of these contracts include special promotions that are subject to conditions that tie customers in for a predetermined minimum period ('the tie-in period'). Failure by the customers to comply with this minimum period (for reasons attributable to themselves) results in the customers still having to pay the amounts provided in the contract.

Under national law, the amount to be paid when the tie-in period is not complied with has to be calculated in proportion to the tie-in period part that has already been completed. Furthermore, Portuguese suppliers are limited to demanding a reasonable amount for services actually delivered, and are not allowed to pursue a customer for damages.

Vodafone self-assessed VAT based on the amounts received in relation to non-compliance with the tie-in period. However, Vodafone then filed an administrative appeal challenging that VAT self-assessment, because it considered that the amounts were not subject to VAT.

CJEU ruling

In earlier cases, the Court already found that predetermined amounts received by an economic operator after early contract termination are subject to VAT where it concerns 1) a contract with a minimum commitment period, 2) the termination is applied before the end of the period, by the customer or for a reason attributable to the customer, and 3) the amount corresponds to the sum that the operator would have received for the remainder of that period in the absence of such termination (MEO C-295/17 and UniCredit Leasing C-242/18).

In the Vodafone case, the CJEU underlines the irrelevance of the claimed amounts not enabling Vodafone to obtain the same income as that which would have been received if the customer had not terminated the contract early.

What matters to the Court is that, from an economic perspective, the amount due upon the early termination of the contract **seeks to guarantee the operator a minimum contractual revenue for the service provided.**

Where customers do not comply with the tie-in period, a supply of services must be regarded as having been made and the termination fee subject to VAT, since those customers were placed in a position to benefit from those services.

Impact

The CJEU appears to advocate a broader approach to applying VAT on early termination fees in this judgment, as compared to its previous case law, where the consideration amount played a role.

It is therefore key for companies charging contractual penalties for early termination to review their terms and conditions to define whether or not these can fall outside the scope of VAT.

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