Reports of Cases

OPINION OF ADVOCATE GENERAL
BOBEK
delivered on 10 April 2018 [1]

Case C-154/17

SIA 'E LATS'
joined parties:
Valsts ieņēmumu dienests

(Request for a preliminary ruling from the Augstākā tiesa (Supreme Court, Latvia))

(Reference for a preliminary ruling — Value added tax (VAT) — Notion of 'second-hand goods' — Notion of 'precious metals or precious stones')

I. Introduction

1. SIA 'E LATS' is a trader and a taxable person for the purposes of VAT. It offers loans to individuals against security in the form of goods containing precious metals or precious stones. Unredeemed pledges are resold by SIA 'E LATS' to other traders, principally for the extraction of precious metals or precious stones. Those traders are liable to pay VAT.

2. A special VAT regime for second-hand goods was applied by SIA 'E LATS' to those resale transactions. The competent tax authority, however, did not agree that that special regime was applicable. It found that the goods resold by SIA 'E LATS' were not second-hand goods within the meaning of the applicable tax legislation. As a result it required SIA 'E LATS' to pay an additional amount of VAT.

3. It is in this context that the Augstākā tiesa (Supreme Court, Latvia) has asked the Court to provide the interpretation of the specific provision of Directive 2006/112/EC ('the VAT Directive') [2] that regulates the VAT applicable to second-hand goods. In particular, the referring court enquires about the scope of the 'precious metals or precious stones' exception found in the definition of 'second-hand goods'. It also asks whether certain features of the resale transaction affect the scope of that exception.

II. Legal framework

A. The VAT Directive

4. Recital 51 of the VAT Directive provides that it 'is appropriate to adopt a Community taxation system to be applied to second-hand goods, works of art, antiques and collectors' items, with a view to preventing double taxation and the distortion of competition as between taxable persons'.

1 Original language: English.

2 Council Directive of 28 November 2006 on the common system of value added tax (OJ 2006 L 347 p. 1).

5. Chapter 4 of Title XII of the VAT Directive contains rules on special arrangements for second-hand goods, works of art, collectors' items and antiques. More specifically, Article 311 of that directive provides:

'1. For the purposes of this Chapter, and without prejudice to other Community provisions, the following definitions shall apply:

(1) "second-hand goods" means movable tangible property that is suitable for further use as it is or after repair, other than works of art, collectors' items or antiques and other than precious metals or precious stones as defined by the Member States;

…'

B. Latvian law

6. Article 138 of the Pievienotās vērtības nodokļa likums ('the VAT Law') establishes that special VAT arrangements apply to transactions involving second-hand goods, works of art, collectors' items and antiques. According to the order for reference, this provision implements inter alia Article 311 of the VAT Directive.

7. According to the order for reference, there are other relevant national rules, provided for in Articles 183 and 184 of the Ministru kabineta 2013. Gada 3. Janvāra noteikumi Nr. 17 'Pievienotās vērtības nodokļa likuma normu piemērošanas kārtība un atsevišķas prasības pievienotās vērtības nodokļa maksāšanai un administrēšanai' (Regulation No 17 of the Council of Ministers of 3 January 2013 on the procedure for implementing the provisions of the VAT Law and various requirements for the payment and administration of VAT, 'Regulation No 17'). Article 183 of Regulation No 17 defines second-hand goods as tangible objects which have been used and are suitable for further use in the same way without transformation or after repair, other than works of art, collectors' items or antiques. Article 184 of the same regulation excludes precious metals or precious stones from the notion of second-hand goods, while also stating that articles containing precious metals or precious stones shall be covered by the notion of second-hand goods if they were delivered or transferred for sale by the seller, mentioned in Article 138 of the VAT Law. In addition, the second sentence of Article 184 states that the articles, which correspond to Chapters 71, 82, 83, 90 or 96 of the Combined Nomenclature, are considered to be articles containing precious metals or precious stones.

III. Facts, national proceedings and the questions referred

8. SIA 'E LATS' ('the Appellant') is a trader and a taxable person for the purposes of VAT. It offers loans to individuals who, according to the order for reference, are not liable to pay VAT. In providing the loans, it takes pledges, which are goods containing precious metals or precious stones such as chains, pendants, rings, wedding rings, spoons, and dental material.

9. The Appellant resold unredeemed pledges to other traders, who are also persons liable for VAT. The goods were graded according to the metal they contained as well as the purity thereof. They were resold by weight so that those precious metals or stones could be extracted ('the transactions at issue').

10. The Appellant applied the special VAT arrangements for second-hand goods to the transactions at issue, as provided for in Article 138 of the VAT Law.

11. The Valsts ieņēmumu dienests ('the tax authority', Latvia) considered that the goods that the Appellant resold constituted scrap: they were not second-hand goods and so the special VAT arrangements for second-hand goods could not apply. Accordingly, it adopted a decision requiring the Appellant to pay an additional amount of VAT.

12. The Appellant brought an action for annulment against that decision. The Administratīvā apgabaltiesa (Regional Administrative Court, Latvia) dismissed the appeal holding that the Appellant had applied Article 138 of the VAT Law to the transactions at issue incorrectly. It held that the goods of gold, silver and other precious materials had been sold by the Appellant as scrap, not as second-hand goods.

13. The case is now pending before the Augstākā tiesa (Supreme Court), the referring court. The latter notes that it may be understood that the special arrangements under Article 311(1)(1) of the VAT Directive do not apply to goods containing precious metals or precious stones that are sold, not as second-hand goods, but solely for extraction of the precious metals or precious stones contained therein. That court takes the view that such goods are not 'second-hand goods' but are 'precious metals or precious stones'. It also considers that in this regard, Article 311(1)(1) of the VAT Directive does not allow for any discretion of the Member States.

14. In those circumstances, the Augstākā tiesa (Supreme Court) decided to stay the proceedings and to refer the following questions to the Court of Justice:

'(1) Must Article 311(1)(1) of Council Directive 2006/112/EC on the common system of value added tax be interpreted as meaning that used articles, acquired by a trader, that contain precious metals or precious stones (as in the present case) and are resold principally in order for those precious metals or precious stones to be extracted, may be regarded as second-hand goods?

(2) If the answer to question 1 is in the affirmative, is it relevant, for the purpose of limiting the application of the special arrangements, that the trader knows that the subsequent buyer intends to extract the precious metals or precious stones present in the used articles, or are the objective characteristics of the transaction (the quantity of goods, legal status of the counterparty to the transaction, etc.) relevant?'

15. Written submissions were made by the Latvian Government and the European Commission. The Latvian Government, the Commission and the Appellant also made oral submissions at a hearing that took place on 25 January 2018.

IV. Assessment

16. This Opinion is structured as follows. First, I will set out the scope and the logic of the notion of 'second-hand goods' which is found in Article 311(1)(1) of the VAT Directive (A). Second, I will turn to the exception that the latter provision sets out for precious metals or precious stones, seeking to capture the purpose and logic of that exception (B). On the basis of these two general points, I shall then provide some guidance relating to the relevant circumstances that are to be taken into account in order to assess whether the goods at issue can be classified as second-hand goods (C).

A. The notion of 'second-hand goods'

17. Article 311(1)(1) of the VAT Directive defines second-hand goods as 'movable tangible property that is suitable for further use as it is or after repair, other than works of art, collectors' items or antiques and other than precious metals or precious stones as defined by the Member States'.

18. Thus, in order to fall within the definition set out in Article 311(1)(1) of the VAT Directive, the goods in question must unite two positive conditions: (i) 'movable tangible property' which is (ii) 'suitable for further use as it is or after repair'; and avoid a negative one (iii): 'other than works of art, collectors' items or antiques and precious metals or precious stones as defined by the Member States'.

19. There is no doubt that the goods at issue are 'movable tangible property'. Thus, the first condition is clearly met. The point of contention in the present case concerns the combined reading of the second (positive) condition and its exact relation to the third (negative) condition.

20. In order to assess that interaction I will first consider the objectives pursued by the special VAT arrangements for second-hand goods (1) before turning to the first of the contentious elements of the definition, that is, 'suitability for further use' (2).

1. Objectives of the special VAT arrangements applicable to second-hand goods

21. Second-hand goods are subject to the profit-margin scheme, which derogates from the common VAT regime: instead of being calculated based on the sales price, the VAT due is calculated based on the difference between the purchase and sales prices of goods.[3]

22. The profit-margin scheme is an exception to the general VAT regime. The scope of the goods falling under that scheme must thus be interpreted narrowly[4] and should not go beyond what is necessary to achieve the objective sought.[5]

23. However, precious metals or precious stones are excluded from the notion of second-hand goods (and, by the same token, from the derogating profit-margin scheme). Thus, that notion is effectively *an exception to an exception*, which means that goods falling under the precious metals or precious stones exception revert back to the general VAT regime.[6]

24. It follows from recital 51 of the VAT Directive that the special VAT arrangements for second-hand goods was introduced so as to prevent double taxation and the distortion of competition.[7] While 'the common system of VAT aims in principle to tax the economic value added at different stages in the production and distribution process',[8] the VAT collected in respect of second-hand goods raises the specific problem of the VAT burden being borne twice.

25. That happens when a taxable dealer acquires goods from a non-taxable person and pays the VAT included in the purchase price, while that trader cannot subsequently deduct it. In other words, when a non-taxable person buys goods, he or she has to pay the applicable VAT as a part of the purchase price. When that person sells these goods to a taxable dealer, that taxable dealer will, in principle, not

3 See Subsection 1 of Section 2 of Chapter 4 of the VAT Directive ('Margin scheme'). Article 313(1) provides that in 'respect of the supply of second-hand goods, works of art, collectors' items or antiques carried out by taxable dealers, Member States shall apply a special scheme for taxing the profit margin made by the taxable dealer, in accordance with the provisions of this Subsection'. Pursuant to Article 315, 'the taxable amount in respect of the supply of [inter alia the second-hand goods] shall be the profit margin made by the taxable dealer, less the amount of VAT relating to the profit margin. The profit margin of the taxable dealer shall be equal to the difference between the selling price charged by the taxable dealer for the goods and the purchase price'.

4 Concerning the interpretation of Article 314 of the VAT Directive, see judgment of 18 May 2017, *Litdana* (C-624/15, EU:C:2017:389, paragraph 23 and the case-law cited).

5 Judgment of 8 December 2005, *Jyske Finans* (C-280/04, EU:C:2005:753, paragraph 35 and the case-law cited).

6 See, in a different context, judgment of 15 January 2002, *Libéros* v *Commission* (C-171/00 P, EU:C:2002:17, paragraph 27). See also Opinion of Advocate General Jacobs in *Zoological Society* (C-267/00, EU:C:2001:698, point 19).

7 This two-fold objective has been recalled by the Court in the judgment of 3 March 2011, *Auto Nikolovi* (C-203/10, EU:C:2011:118, paragraphs 47 and 48).

8 Judgment of 1 April 2004, *Stenholmen* (C-320/02, EU:C:2004:213, paragraph 27).

have the possibility to deduct the VAT paid initially and contained in the purchase price. In this way, the taxable dealer has to pay VAT again and double taxation occurs. This is precisely the situation that the special VAT arrangements for second-hand goods seek to avoid by providing that the VAT due by the taxable dealer is determined based on the difference between the purchase and sale prices. [9]

26. In this sense, the Court explained that to 'tax, on its overall price, the supply by a taxable dealer of second-hand goods …where the price at which that dealer purchased those goods includes a sum of input VAT which was paid by a person falling within one of the categories identified in Article 314(a) to (d) of [the VAT] directive and which neither that person nor the taxable dealer was able to deduct, would lead to such double taxation'. [10]

27. Such accumulation of taxation in the context of second-hand goods was acknowledged quite early. [11] The Commission noted in that regard that the absence of special rules concerning works of art, antiques, collectors' items and used goods led to the situation in which 'a finished item reintroduced into the economic circuit would once again be fully subject to value added tax and the taxable person wishing to resell the item be unable to deduct the tax included in the item's purchase price …The resulting difference in the tax burden would be an inducement to bypass ordinary commercial channels'. [12]

2. Suitability for further use

28. The second condition of Article 311(1)(1) of the VAT Directive concerning the 'suitability for further use' was interpreted by the Court in *Sjelle Autogenbrug*. That case concerned end-of-life motor vehicles which had been purchased to be sold as spare parts. The Court explained that 'suitability for further use' had to be examined on the basis of whether the object at issue has '*maintained the functionalities*' it possessed when new. [13] The Court held that the notion of 'second-hand goods' does not exclude 'movable tangible property that is suitable for further use as it is or after repair, coming from other property in which it was incorporated as a component. The fact that used property which forms part of other property is separated from the latter does not call into question the characterisation of the property removed as "second-hand goods", to the extent that it may be reused "as it is or after repair"'. [14]

29. The key element of the definition of 'suitability for further use' is thus the *maintained functionality of the same type*. However, in the context of the present case, the factual fulfilment of that condition appears to be the apple of discord between the parties.

30. At the hearing, the Appellant argued in essence that the condition of 'suitability for further use' has been met to the extent that the goods at issue, such as rings, can still be used as rings, independently of whether they are sold by weight (which, according to the Appellant, is not an uncommon phenomenon in the jewellery business). Even an engagement ring bearing an inscription (such as the word 'forever') can be considered as suitable for further use because, clearly, it is still a ring and can still be worn.

9 See to that effect, for example, judgment of 8 December 2005, *Jyske Finans* (C-280/04, EU:C:2005:753, paragraphs 38 to 41).

10 Judgment of 18 May 2017, *Litdana* (C-624/15, EU:C:2017:389, paragraph 26 and the case-law cited). See, in this sense also, judgment of 1 April 2004, *Stenholmen* (C-320/02, EU:C:2004:213, paragraph 25).

11 See judgment of 5 December 1989, *ORO Amsterdam Beheer and Concerto* (C-165/88, EU:C:1989:608, paragraph 16). See, by analogy, judgment of 27 June 1989, *Kühne* v *Finanzamt München III* (C-50/88, EU:C:1989:262, paragraphs 9 to 10). See also point 1.2 of the Opinion of the Economic and Social Committee of 21 June 1989 on the proposal for a Council Directive supplementing the common system of value added tax and amending Articles 32 and 28 of Directive 77/388/EEC — Special arrangements for second-hand goods, works of art, antiques and collectors' items (OJ 1989 C 201, p. 6).

12 See Proposal for a seventh Council Directive on the harmonisation of the laws of the Member States relating to turnover taxes — common system of value added tax to be applied to works of art, collectors' items, antiques and used goods (OJ 1978 C 26, p. 2).

13 Judgment of 18 January 2017 (C-471/15, EU:C:2017:20, paragraphs 32 to 33). Emphasis added.

14 Judgment of 18 January 2017, *Sjelle Autogenbrug* (C-471/15, EU:C:2017:20, paragraph 31).

31. The Appellant's position about the suitability for further use has not been embraced by the Latvian Government. That government acknowledges that under national law, namely Article 184 of Regulation No 17,[15] articles containing precious metals or precious stones are considered to be second-hand goods. At the same time, according to that government, such articles can only be classed as second-hand goods if they are still suitable for use of *the same type* and provided that they are assessed based on their *individual* value. According to that government, that was not the case of the goods at issue sold by weight and as scrap in view of the precious elements that would be extracted.

32. At the hearing the Appellant explained in detail that only 5% of the resold unredeemed pledges considered by the tax authorities in the main proceedings were unsuitable for further use and that repairing those goods would be too costly. The Appellant also maintained that other goods were evaluated and sold individually for retail or in bulk, in which case their price was determined by weight. These goods were, according to the Appellant, suitable for further use without repair. The Appellant argued at the hearing that the above described features of the 5% of unredeemed pledges affected the conclusions made by the tax authority in respect of all the goods considered. The result is that the VAT treatment reserved for that specific 5% of the goods was applied to the goods considered in their entirety.

33. The Commission finds that the goods at issue were not suitable for further use either due to their nature (dental material) or due to their condition (damaged or personally customised goods). The absence of suitability for further use is, according to the Commission, also evidenced by the circumstances in which the transaction at issue took place.

34. An accurate understanding of the relevant factual elements is certainly of paramount importance for the assessment of the case, including before this Court. However, factual assessments are exclusively for the national courts to carry out. This Court is bound by the facts as ascertained and presented by the referring court. I wish to make that point clear in view of a number of factual statements made in particular by the Appellant, the purpose of which was essentially to convince this Court that the national authorities and, by implication, the national courts, omitted relevant facts and/or incorrectly assessed them.

35. Thus, the starting point for the legal assessment under EU law is based on the description of the goods as characterised by the referring court in its order for reference and reflected in the wording of its first preliminary question. I therefore take for granted that, as the first question stipulates, the items made of precious metals or precious stones were resold by the Appellant *for extraction*, that is, to be reused *as raw material*.

36. If that is indeed the case, which is exclusively for the national court to ascertain and to assess, then my suggestion is that in such a situation, for reasons that I shall explain in detail in the following sections of this Opinion, the precious metals or previous stones exception indeed applies. Such goods as described by the referring court are not second-hand goods and fall back under the general VAT regime.

37. However, beyond the essentially factual assessment of the nature of a concrete transaction, there lies a deeper issue that I have already outlined and that I understand is fuelling the first question referred by the national court: the relationship between the *suitability for further use* condition and the *precious metals or precious stones* exception. I do agree that that relationship is difficult to describe because the second condition of Article 311(1)(1) of the VAT Directive is defined by the use

15 Above, point 7 of this Opinion.

(*functionality*) of the object concerned, whereas the third condition — the precious metals or precious stones exception — is defined by the *material* in question. If one adds to that complexity the fact that the second condition is an EU law based one, whereas the third condition is explicitly left for the Member States to define, it is quite clear that the two definitions are likely to clash or overlap.

38. The oral submissions made at the hearing revealed uncertainties about that relationship: Does the fact that a used ring is made of gold exclude that ring automatically from the notion of second-hand goods (and from the profit-margin scheme) because, aside from being used and being suitable for further use, it is also made out of a precious metal? Or does the used condition and suitability for further use prevail over the precious metal or precious stone quality, which would mean that any used object that is suitable for further use and made of precious metals or precious stones must always be considered as a second-hand good, and thus included in the profit-margin scheme?

39. In order to define the precise relationship between these two notions, the specific purpose, logic, and history of the precious metals or precious stones exception needs to be outlined first.

B. The precious metals or precious stones exception

40. On a first reading of the text of Article 311(1)(1) of the VAT Directive, it appears clear that 'precious metals or precious stones' are simply excluded from the notion of second-hand goods, in a similar way to the exclusion of 'works of art, collectors' items' [and] 'antiques'.

41. That apparent similarity must, however, be considered in its context. 'Works of art, collectors' items' [and] 'antiques' are excluded from the notion of second-hand goods but are still included in the profit-margin scheme. For that purpose, they are simply defined in separate provisions of the VAT Directive.[16] By contrast, precious metals or precious stones are excluded from the notion of second-hand goods and, by the same token, they are also excluded from the profit-margin scheme. Moreover, the definition of 'precious metals or precious stones' is explicitly left to the Member States.

42. Since consideration of the wording of Article 311(1)(1) of the VAT Directive (including its different language versions) does not illuminate any further the precise relationship between the notions of suitability for further use and the precious metals or precious stones exception, I shall turn to the legislative history of that exception (1) before considering its objective and purpose (2).

1. Legislative history

43. The first proposal[17] that considered precious metals or precious stones in the context of the profit-margin scheme defined 'used goods' as 'movable property other than [works of art, collectors' items and antiques] that has been used and is suitable for reuse as it is or after repair'.[18] Interestingly, Article 3(4) of that proposal stated that the scheme for used goods 'shall not apply to supplies of *used goods made of gold or any other precious metal or containing precious stones*'.[19] At the same time, the suggested definition of 'works of art', 'collectors' items' and 'antiques' included goods made of gold or any other precious metals or containing precious stones, where the value of such precious materials does not exceed 50% of the selling price.[20] That proposal was nevertheless withdrawn in November 1987 due to lack of agreement.

16 See Parts A, B and C of Annex IX to the VAT Directive.

17 Proposal for a seventh Council Directive of 11 January 1978 on the harmonisation of the laws of the Member States relating to turnover taxes — common system of value added tax to be applied to works of art, collectors' items, antiques and used goods (OJ 1978 C 26, p. 2). That proposal was subsequently amended but those amendments are not relevant in the present context (OJ 1979 C 136, p. 8).

18 See Article 3 of the Proposal referred to above, at footnote 17 (OJ 1978 C 26, p. 2).

19 Emphasis added.

20 See the suggested Article 2(4) of the proposal referred to above in footnote 17.

44. In another proposal [21] which eventually led to the adoption of Directive 94/5/EC, [22] the Commission suggested that objects made of gold or any other precious metals or containing precious stones, where the value of those materials did not exceed 50% of their selling price, would still benefit from the special arrangements applicable to, inter alia, second-hand goods. [23]

45. The Economic and Social Committee supported the introduction of the special arrangements and approved the exclusion of precious metals or precious stones. However, it disagreed that the scope of those special arrangements should depend on the value of the materials incorporated. It noted that '… the proposal to include objects containing precious stones and metals only when the value of the incorporated materials accounts for less than 50% of the selling price seems somewhat arbitrary. The difficulty of an objective valuation would probably give rise to numerous disputes or cases of fraud. It would perhaps have been more helpful to exclude items which are suitable for re-working'. [24]

46. The adopted version of Directive 94/5 inserted a new Article 26a [25] that provided for a simple exclusion of precious metals and precious stones, with no reference to the value that these elements represent within the entire object.

47. In the light of the above, the idea of the exclusion of goods *made of* precious metals or *containing* precious stones from the scheme as well as the idea of a 50% threshold appeared within the legislative process as elements relevant for the delimitation of the special arrangements for, inter alia, second-hand goods.

48. However, although instructive as to all the practical problems encountered on the way, the legislative history fails to reveal the precise reasons that led to the exclusion of precious metals and precious stones from the profit-margin scheme. In order to understand those reasons, one needs to turn to the (economic) logic inherent in goods made of precious metals or precious stones.

2. Economic logic and purpose

49. The nature of objects made of or containing precious metals or precious stones is specific. [26] Their function (and value) is twofold. Depending on the quality and condition of each specific good, they constitute not only a specifically crafted or produced object endowed with a certain functionality (functional value), but they also store the intrinsic value attributed by society to the precious metals or precious stones contained therein ('material' intrinsic value).

50. The practical problem demonstrated by the complex legislative history of Article 311(1)(1) of the VAT Directive is that in view of the vast range of objects made of or containing elements of precious metals or precious stones, it is difficult to devise an abstract criterion to generally assess the relative importance of each of those types of value.

21 Proposal for a Council Directive supplementing the common system of value added tax and amending Articles 32 and 28 of Directive 77/388/EEC — Special arrangements for second-hand goods, works of art, antiques and collectors' items, COM(88) 846 final (OJ 1989 C 76, p. 10).

22 Council Directive of 14 February 1994 supplementing the common system of value added tax and amending Directive 77/388/EEC — Special arrangements applicable to second-hand goods, works of art, collectors' items and antiques (OJ 1994 L 60, p. 16).

23 See Article 1 of Proposal for a Council Directive supplementing the common system of value added tax and amending Articles 32 and 28 of Directive 77/388/EEC — Special arrangements for second-hand goods, works of art, antiques and collectors' items, COM(88) 846 final (OJ 1989 C 76, p. 10).

24 Point 3.1 of the Opinion of 21 June 1989 on the proposal for a Council Directive supplementing the common system of value added tax and amending Articles 32 and 28 of Directive 77/388/EEC — Special arrangements for second-hand goods, works of art, antiques and collectors' items (OJ 1989 C 201, p. 6).

25 'A. …: (d) second-hand goods shall mean tangible movable property that is suitable for further use as it is or after repair, other than works of art, collectors' items or antiques and other than precious metals or precious stones as defined by the Member States.'

26 See, by analogy, concerning investment gold, judgment of 26 May 2016, *Envirotec Denmark* (C-550/14, EU:C:2016:354, paragraph 41).

51. On one side of the spectrum, I can certainly use a gold nugget as a paperweight. It can also be sold and reused as a paperweight. It is nonetheless very unlikely that the price of such a paperweight will be determined with regard to its undeniable efficiency in keeping a bunch of papers from flying away, even if there is a strong gust of wind. Instead, its price is likely to be determined on the basis of the current market price of gold. In such a scenario, the price of the item will be the price of raw material it is composed of.

52. On the other side, one may imagine a complex and expensive medical device that is made of, amongst other things, several precious metals or even (a) precious stone(s). The value of the precious metals or precious stones in the device might in itself be considerable, but it is likely that the functional value of the device, if it is resold while fully operational, would be much higher than the value of the precious materials it is composed of.

53. However, intriguing examples aside, it is quite clear that for the purposes of the application of Article 311(1)(1) of the VAT Directive, it is the first scenario that is likely to be relevant. There are a variety of objects made of or containing precious metals whose value, as objects endowed with certain functionality, is far from obvious. But those objects are still traded because of their precious material content. In the present case, that appears to concern, in particular, dental material, pieces of broken cutlery or broken jewellery.

54. It is thus clear that objects made of precious metals or precious stones have a 'stored value' which is independent of whether the initial functionality of the concrete object is also maintained or not. This is why the metals and stones concerned are called *precious* after all, why wars have been waged over their ownership, and why the discovery of a hidden treasure containing coins, rings and jewellery of an unknown queen makes the lucky finder a rich woman,[27] although she might still prefer lighter modern jewels for daily use.

55. In view of this economic logic, it would thus appear that the precious metals or precious stones exception aims at situations in which, simply put, the original functionality of the second-hand goods is lost, or in the context of the transaction in question, does not matter. Such goods are no longer resold because of their functionality, but because of the inherent value of the raw material of which they are composed. Consequently, such goods leave the specific economic cycle of second-hand goods. Instead, they enter a new economic cycle of 'raw' material, effectively serving as input for the production of new items made of precious metals or precious stones.

56. Finally, as a point of broader, systemic analogy, it ought to be noted that similar considerations led the EU legislature to exempt investment gold from VAT altogether.[28] In the relevant proposal introducing the special scheme for gold, the Commission noted the problem of residual tax and double taxation that constitutes 'the very justification of the special scheme proposed … for second-hand goods, works of arts, antiques and collector's items. … By contrast, gold, as an object of investment, can be the subject of an unlimited number of transactions. … Any system of taxing the margin minimises but does not completely eliminate the effects of residual tax: it will continue to grow the longer the economic cycle simply because tax on the margin is incorporated into the price and cannot be deducted by the subsequent buyer. The particularly high value of gold and the large number of successive transactions to which it may be subject would amplify this phenomenon'.[29]

27 Subject, of course, to the relevant national legislation.

28 See Article 346 of the VAT Directive. Article 344 of the VAT Directive defines 'investment gold'.

29 Proposal for a Council directive supplementing the common system of value added tax and amending Directive 77/388/EEC — special scheme for gold (COM(92) 441 final, pp. 6 and 7). That proposal led to Council Directive 98/80/EC of 12 October 1998 supplementing the common system of value added tax and amending Directive 77/388/EEC — Special scheme for investment gold (OJ 1998 L 281, p. 31).

57. The exemption applicable to investment gold comes from the fact that it is considered to be 'inherently similar to other financial investments which are exempt from VAT'.[30] By contrast, the reasons for the exemption disappear if the investment gold is transformed, for example, into jewellery. It is still the same material but its function within the economic cycle is viewed differently.[31]

3. The Member States' discretion and its limits

58. Finally, Article 311(1)(1) of the VAT Directive states that precious metals and precious stones are to be *defined by the Member States*.

59. The considerable latitude that the Member States enjoy in setting up the conditions for the applicability of the precious metals or precious stones exception is, however, not unlimited. Two types of limits may be mentioned as a conclusion to this section: general and specific.

60. As far as the *general* limits applicable to exceptions in the VAT Directive are concerned, the Court has acknowledged that when implementing an exception, Member States must respect, in particular, the principles of equal treatment and fiscal neutrality,[32] taking into consideration the objective[33] pursued by the VAT Directive.

61. The *specific* limit flows from the concrete objective of the provision interpreted, that is Article 311(1)(1) of the VAT Directive in the present case. Again, it is clear that that provision leaves to the Member States considerable latitude as to the definition of the notion of 'precious metals or precious stones', in particular for the definition of the types of precious metals and precious stones, as well as the nature of the goods in question. However, the exercise of that discretion cannot deprive the notion of 'second-hand goods' of its proper content through an excessively narrow definition of what may constitute precious metals or precious stones. The consequence of that would be that any goods containing precious metals or precious stones would remain within the second-hand goods regime perpetually, irrespective of their continuing use and functionality.

62. In other words, the basic economic logic of the precious metals or precious stones exception must be respected. For an object to remain within the profit-margin scheme applicable to second-hand goods, there must be some preserved functionality of the object in question, in addition to the precious material content.[34]

30 Recital 53 of the VAT Directive.

31 As acknowledged in recital 27 of the VAT Directive. See also Article 82 of the VAT Directive. See further recital 4 of the Proposal for a Council Directive amending Directive 77/388/EEC as regards certain measures to simplify the procedure for charging VAT and to assist in countering tax evasion and avoidance, and repealing certain Decisions granting derogations (COM(2005) 89 final).

32 Concerning different notions of the VAT Directive (or its predecessors) whose definition is left to the Member States see, for instance, judgment of 26 May 2005, *Kingscrest Associates and Montecello* (C-498/03, EU:C:2005:322, paragraphs 51 to 54); of 27 April 2006, *Solleveld* (C-443/04, EU:C:2006:257, paragraphs 27 to 36); of 28 June 2007, *JP Morgan Fleming Claverhouse Investment Trust and The Association of Investment Trust Companies* (C-363/05, EU:C:2007:391, paragraphs 41 to 49); of 15 November 2012, *Zimmermann* (C-174/11, EU:C:2012:716, paragraphs 31 to 33); of 28 November 2013, *MDDP* (C-319/12, EU:C:2013:778, paragraphs 37 and 38); or of 13 March 2014, *ATP PensionService* (C-464/12, EU:C:2014:139, paragraph 42).

33 See, in this sense, judgments of 27 April 2006, *Solleveld* (C-443/04, EU:C:2006:257, paragraph 35); of 28 June 2007, *JP Morgan Fleming Claverhouse Investment Trust and The Association of Investment Trust Companies* (C-363/05, EU:C:2007:391, paragraph 43); and of 13 March 2014, *ATP PensionService* (C-464/12, EU:C:2014:139, paragraph 42).

34 See also Capaccioli, S., 'VAT Taxation of Gold in the European Union', *EC Tax Review 2014*, pp. 85 to 101, at p. 100: 'the margin scheme is applicable to used jewellery only if the transaction has a "margin" over the precious metals contained, meaning that added value over the metal exists. If the transaction has the substance of reworking or recovering the gold, used jewellery is deemed gold material'.

C. Assessing a transaction

63. The key criterion for deciding whether an item falls under the second-hand goods profit-margin scheme or whether it reverts (through the precious metals or precious stones exception) back to the general VAT regime is the *maintained functionality* (use) of the goods considered. The overall logic is the prevention of double taxation and distortion of competition in the context of goods that are reintroduced into the economic cycle without bringing any new, added economic value.

64. As this case demonstrates, however, the devil is in the detail. How is that general rule to be applied in complex factual situations of apparently mixed items sold in bulk? The guidance provided in this section with regard to such situations is bound to be limited for two reasons: first, every assessment conducted in a similar context will be heavy on the facts, and is for the national court to make. Second, that factual assessment will be further framed by the national rules that are implementing Article 311(1)(1) of the VAT Directive and which, provided they respect the limits set by EU law, may allow for quite some differentiation, in particular in borderline cases.

65. With those caveats in mind, the final section of this Opinion will first set out the criterion for carrying out such an evaluation (1) before turning to the concrete factors that might be taken into account when making such an assessment (2).

1. The criterion: the maintained functionality (use) of the goods considered

66. As already noted, the key question to be asked is whether the functionality of the goods at issue is preserved and whether that functionality is there in addition to the 'mere' precious metal of which that good is composed.

67. The discussion that unfolded at the hearing unveiled the complexity of factual scenarios that may in practice arise. To start with, there are certain scenarios which are clear.

68. First, there was a consensus that the precious metals or precious stones exception applies to goods when sold as *material*. I agree with that. In principle, that means that (unless another specific provision of the VAT Directive applies, such as the one for investment gold, collectors' items or antiquities), a golden nugget once kept as a souvenir and then given as a pledge in exchange for a loan would be classed as a precious metal within the meaning of Article 311(1)(1) of the VAT Directive. The exclusion from the profit-margin scheme appears logical because such goods are likely to be traded to be modified in some way.

69. Second, there will be objects made of precious metals or precious stones that will be sold taking into consideration the value of the material and *also* their individual function. Such objects are likely to be sold in an *individualised* way. That could be the case of, for example, a used gold necklace, the value of which is certainly assessed in the light of the purity of the material used, but also in the light of its condition, which includes whether the necklace is still suitable to be worn. The inclusion of such an item under the profit-margin scheme appears to be appropriate because such goods are not likely to be traded for reworking.

70. Apart from such clear-cut cases, which might be considered as forming the ends of a spectrum, there are a number of less clear scenarios in between.

71. On the one hand, there are objects that are, for economic reasons, sold by weight or in bulk, their functionality not only being maintained, but even taken into account. That can be the case of a mix of lower quality silver rings, priced and sold by the kilo. Similar to what was argued by the Appellant at the hearing, I consider that the fact that specific goods are priced and sold by the kilo, does not

necessarily prevent the possibility of considering those objects as second-hand goods, within the meaning of Article 311(1)(1) of the VAT Directive if the preserved functionality is indeed a relevant element of the transaction. Indeed, if their preserved functionality matters in order to ascertain their value, then such objects are not likely to be sold to be reworked.

72. On the other hand, however, a different conclusion is called for in the case of goods priced and sold in bulk regardless of their functionality. In such a situation, the disregard for their original functionality would also mean the absence of any individualisation of each single item. That would be the case, as discussed at the hearing and mentioned by the referring court, of dental material or damaged objects made of, or containing, precious metals or precious stones. If the functionality of the used goods at issue is no longer considered to be the relevant element of the whole transaction, the 'second-hand status' of the objects is lost. Indeed, if the functionality becomes irrelevant, it seems difficult to consider that those goods are the subject of transactions to be introduced and maintained as such in the economic cycle. The rationale of the profit-margin scheme then disappears.

73. Finally, within the last category, there might be the specific factual situation of a *mix within the mix*: in one bag, there might not only be mixed items (rings, spoons, bracelets, pendants), but also a mix in the way that some items might objectively be suitable for reuse, should someone wish to take them from the bag and use them, while others might not.

74. How to classify such borderline situations is again deeply dependent on the facts of the case, together with the way a Member State has implemented the precious metals or precious stones exception of Article 311(1)(1) of the VAT Directive. Personally I would see a lot of sense if, as a rule of thumb, the *predominant* purpose of each transaction would lead to the line being drawn at around 50%: if the majority of the items sold in bulk is for reworking, sold as material, then the fact that somebody could still pick up individual items from a bag and use them is simply not relevant, because the overall purpose of the transaction was different. But since, as explained above,[35] attempts by the EU legislature to introduce such thresholds have been expressly discarded and the discretion was left to the Member States, it is necessary to honour that decision and to conclude that, within the limits for the Member States' discretion set out above,[36] it is for the Member States to set rules for such situations, including the applicable thresholds.

2. Evaluating a transaction: the factors

75. Which of the categories outlined above applies is a matter for the referring court to ascertain, subject to the specific national rules adopted for the transposition of Article 311(1)(1) of the VAT Directive. From what is stated in the order for reference and more specifically the wording of the first question referred, it appears to me that the referring court has already carried out such a factual assessment and concluded that the purpose of the transaction was for the precious metals or precious stones to be extracted and reused as raw material. If that is indeed the factual situation, I agree that the precious metals or precious stones exception should apply.

76. Without in any way questioning that factual assessment, but in order to provide general guidance, I shall briefly discuss some factors that might be of relevance in making such a factual assessment. It ought to be noted that the guidance offered forms a part of the response to the first preliminary question referred. It does not pertain to the second question which, given my response to the first, does not need to be addressed by the Court.

35 Above, points 44 to 46 of this Opinion. I certainly acknowledge the potential for fraud identified by the Economic and Social Committee in their opposition to the introduction of any clear threshold in this regard (above, point 45). I do wonder, however, how far that recognised problem is effectively being tackled by not having any threshold at all at EU level and leaving that problem to the Member States.

36 Above, points 58 to 62 of this Opinion.

77. It should be stated at the outset that any such assessment of a transaction has to be an *objective* one. It aims at ascertaining the purpose of the transaction as it would be perceived by an independent observer considering its objective circumstances. Making a generalisation with regard to the various factors discussed in the course of these proceedings, I suppose that they can be put into three different baskets.

78. First, there are the factors that are relevant and ought to be taken into account, such as the presentation of goods for resale; methods of the valuation of such goods and other sale conditions, such as the quantities of the goods sold together; and the fact that the purchaser is involved in a particular business, namely the processing of precious metals or precious stones.

79. Second, apart from such objective factors, there is also the extensively discussed element of subjective intent. In this regard, I entirely agree with the Latvian Government and the Commission that the intentions of one or the other party cannot be conclusive. Such intention cannot autonomously determine the purpose of the transaction and the applicable VAT regime.[37] That is also true concerning the knowledge that the Appellant had at the moment of the transaction as regards the intent of the respective buyers as to how the goods would be used, mentioned by the referring court.

80. That does not mean that the intention of the parties bears no relevance at all. It certainly does, but not as a determining factor. It is just one of the (objective) indications that may help to explain the true nature and purpose of the transaction to the external observer evaluating the transaction as a whole. That relates to the broader acknowledgement by the Court of the fact that 'consideration of economic and commercial realities is a fundamental criterion for the application of the common system of VAT'.[38]

81. Third, there are factors that, for the specific type of assessment in question, are simply irrelevant. This is the case of the legal status of the purchaser, as also stated by the Latvian Government and the Commission.

82. Finally, it is clear that all the relevant objective factors are to be considered and assessed as a whole. They should not be considered in isolation from each other. Thus, for instance, the fact that items containing precious metals or precious stones and which are sold by weight but maintain their functionality[39] can, in certain circumstances, still be considered as second-hand goods, makes it clear that the fact of selling goods by weight does not necessarily and in itself make the relevance of functionality of those goods disappear. The same applies to the method of valuation: while pricing the goods based on the value of the material may be an indication of the fact that the goods at issue are traded without consideration of their individual function, taking into account the value of the material is likely to be part of the price-setting for an individual gold ring as well. For that reason, and similar to what was observed by the Commission, I consider that the relevant objective circumstances of the transaction must be considered as a whole and in their mutual interplay.

37 See, by analogy, judgment of 6 July 2006, *Kittel and Recolta Recycling* (C-439/04 and C-440/04, EU:C:2006:446, paragraphs 41 and 42 and the case-law cited). See also, concerning the notion of 'supply of services', judgment of 20 June 2013, *Newey* (C-653/11, EU:C:2013:409, paragraph 41).

38 Judgment of 20 June 2013, *Newey* (C-653/11, EU:C:2013:409, paragraph 42 and the case-law cited).

39 Example mentioned above at point 71 of this Opinion.

V. Conclusion

83. In the light of the above, I suggest that the Court respond to the questions posed by Augstākā tiesa (Supreme Court, Latvia), as follows:

– Article 311(1)(1) of the Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax shall be interpreted as meaning that the notion of 'second-hand goods' does not cover used goods acquired by a trader that contain precious metals or precious stones such as the ones in the main proceedings which are resold principally for the extraction of those precious metals or precious stones, if it follows from the objective circumstances of the transaction that such goods are resold without consideration of the functionality of the goods concerned.

– Whether this is the case must be established on the basis of the objective circumstances of the transaction, considered as a whole. The elements to be taken into account include the presentation of goods for the purpose of their resale; methods of the valuation of such goods; the quantities of the goods sold together; and the fact that the purchaser is involved in a particular business, such as the processing of precious metals or precious stones.