



## Supreme Court Defines VAT- Recoverable Promotion Expenses

*by Marc Quaghebeur and Laurent Tainmont*

In an April 8 decision, the Belgian Supreme Court settled a long-running debate over the distinction between business entertainment expenses and business promotion expenses.

### Background

Under article 45, section 3 of the Belgian VAT Code, a taxpayer can recover the VAT on all business expenditures except business entertainment expenses. However, the distinction between business entertainment expenses and business promotion expenses has long been a gray area.

Tax authorities tend to look at the nature of the expenses rather than their purpose. That means expenses for items such as food and beverages offered to guests, flower arrangements, and entertainment are not deductible for VAT purposes.

In the case submitted to the Supreme Court, a publishing company had hired an event organizer to manage a launch party for a new magazine and to take charge of several concerts in connection with the elections of the "most deserving pop singer" and "Man and Woman of the Year." Tax authorities considered the publishing company's costs regarding those events as business entertainment expenses and denied the publisher the right to deduct the VAT on the invoices submitted by the event organizer.

The court of first instance and Court of Appeal characterized the expenses as business promotion expenses. In particular, the Antwerp Court of Ap-

peal<sup>1</sup> referred to article 17(6) of the EC Sixth VAT Directive,<sup>2</sup> which makes a distinction between "strictly business expenditure" and "luxuries, amusements or entertainment."

It concluded that the notion of business entertainment expenditure is limited to the costs of entertainment and amusement incurred for customers or guests for the sole purpose of creating a favorable atmosphere for the company. Those expenses are not deductible, it said.

However, the Court of Appeal said that expenditures incurred for the purpose of selling products directly, or for advertising specific products, do not fall within that definition. Those are promotional expenses, and therefore, are strictly business expenditure, it said. The purpose of the launch party clearly was to promote the sale of the new magazine by acquiring name recognition in the other media, and the concerts clearly helped to maintain the reputation of the publisher's other magazines, the Court said.

### The Supreme Court

In their appeal to the Supreme Court, the tax authorities argued against an interpretation of business promotion expenses based on the Sixth VAT Directive. They said it is not the purpose (promoting the business), but rather the nature of the expense

<sup>1</sup>Antwerp, March 15, 1999.

<sup>2</sup>Council Directive 77/388/EEC of May 17, 1977.

For example, a show, a cocktail party, and so on), that determines whether an expenditure qualifies as business entertainment or business promotion. In their view, the cost of entertaining third parties is always a form of business promotion, so the purpose of the expenditure is not a relevant consideration.

The Supreme Court rejected that argument and provided new definitions of business promotion and business entertainment expenses. It said business entertainment expenditures include all expenses, including those for entertainment, which are incurred to welcome and receive visitors from outside the company to confirm and reinforce the business relationship. Business promotion expenditures, however, are expenses that are mainly and directly aimed at informing the final purchaser of the existence and qualities of a product or service to promote the sale. The deduction of VAT on those expenses cannot be refused, the Court said.

The Supreme Court's interpretation is reminiscent of the definition used by the European Court of Justice in 1993<sup>3</sup> for "advertising services." The ECJ said "the concept of advertising necessarily entails the dissemination of a message intended to inform consumers of the existence and the qualities of a product or service, with a view to increasing sales."<sup>4</sup>

---

<sup>3</sup>*Commission of the European Communities v. French Republic* (C-68/92), November 17, 1993.

<sup>4</sup>Paragraph 16.

More specifically, the ECJ said it is "sufficient that a promotional activity, such as . . . the organization of a cocktail party or banquet, involves the dissemination of a message intended to inform the public of the existence and the qualities of the product or service which is the subject matter of the activity, with a view to increasing the sales of that product or service,"<sup>5</sup> for the activity to be characterized as an advertising service within the meaning of article 9(2)(e) of the Sixth VAT Directive.

Because article 45, section 3 of the VAT Code is an exception to the rule that all business expenses entail a right to deduct the VAT, it must be construed restrictively. In effect, that means that only expenses that strictly comply with the criteria of article 45, section 3 must be excluded from the VAT deduction. It goes without saying that this figured into the Supreme Court's decision to favor the purpose of an expenditure over its nature in determining whether it qualifies as a business promotion expense. Hopefully, the decision will put an end to a long line of contradictory decisions by the lower courts. ♦

♦ *Marc Quaghebeur and Laurent Tainmont,  
Vandendijk & Partners, Brussels*

---

<sup>5</sup>Paragraph 18.