TREATMENT OF CONSTRUCTION CONTRACTS VS. SALE OF GOODS TO BE INSTALLED

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Article 17, paragraph 6, point a) of Presidential Decree 633/1972, provides for the application of the VAT reverse charge mechanism for the supply of services made in the construction sector by subcontractors contracted by companies that carry out construction or restructuring of real estate property, or by general contractors or other subcontractors.

Reverse charge or ordinary VAT regime: following the introduction of this provision, several interpretation issues have arisen, of which the most debated has been the VAT treatment of service contracts, defined by VAT law as actual provision of services (thereby subject to the reverse charge) in case of construction contracts , but as supply of goods in case of sale of goods to be installed (thereby subject to the ordinary VAT regime).

Distinguishing between service contracts and supply of goods to be installed: by means of a **service contract**, the supplier agrees, based on his own organization of the necessary means and at his own risk, to perform a work or service for a cash consideration (art. 1655, Civil Code). In this case, the contractual intent is to produce a result different to merely the combination of goods installed.

The supply of goods to be installed is, on the other hand, a contract by which the supplier provides a particular good or a set of goods, and, as a strictly ancillary service, installs them. In essence, goods are supplied here, and not services. In this case, the installation is exclusively directed to adapt the goods to the needs of the customer without changing their nature.

In some cases, the difference between contract for the supply of goods to be installed and service contract is very thin and, consequently, it is necessary to perform an analysis of the underlying intent of the parties and the characteristics of the transaction.

Tax authorities interpretations over the years:
Circular. n. 37/E dated 22 December 2015, deriving some principles from European and Italian case law, has provided the following significant clarifications useful to distinguish the two above cases for VAT treatment purposes:

- it is necessary to verify whether the services provided by the supplier are just limited to the installation of goods without any alteration of them, or, if the goods are intended to be changed, if the alterations are directed to modify the nature of the goods and / or to adapt them to the specific needs of the customer;
- the relationship between the price of the goods and the services is an objective index which may be taken into account, but the cost of the goods and labour cost cannot, by itself, assume decisive importance;
- it is necessary to clearly identify the intent of the contract, considering the existing agreements between the parties, and it must be considered whether the parties intended to attribute major importance to the service or to the goods;
- when the main purrpose of the contract is the supply of goods, and the installation is exclusively directed to allow their use, without changing their nature, the contract can be qualified as a supply of goods to be installed;
- when the supply of goods changes their nature, the labour service is the essential purpose of the contract and the changes made to the goods generate significant added value in reaching the final result, then the contract can be qualified as a service contract.

- if the main object of the contract relates to the provision of services, then it will be necessary to apply the reverse charge regime. The supplier should issue a "not subject to VAT" invoice, and the customer should issue a self-invoice with the application of 22% VAT;
- if, however, the main object of the contract is the supply of goods, and the installation service is just of an auxiliary nature, then the supplier will apply VAT in the ordinary way.

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