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SECOND REPORT FROM THE COMMISSION

on the application of the common system of value added tax,
submitted in accordance with Article 34 of the Sixth Directive
(77/388/EEC) of 17 May 1977)

(Situation as at 30 June 1987)

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INTRODUCTION

The First Report on the application of the common system of value added tax (1) was presented to the Council on 22 September 1983 and then transmitted to Parliament.

All Member States now apply VAT. Portugal is well on the way to setting in place the common VAT system, having replaced its turnover tax arrangements, which applied only at the wholesale stage, with a VAT system very similar to the Community system.

The common VAT system was introduced in Spain and Greece on 1 January 1986 and 1 January 1987 respectively.

On its accession to the Community, Greece was not required to introduce the system until 1 January 1984. Two successive deferments meant that the deadline was put back to 1 January 1987 (2).

The Act of Accession of Spain and Portugal specified 1 January 1986 and 1 January 1989 as the respective dates for the systems' introduction in the two Member States. A joint declaration attached to the Act of Accession provides that, throughout the period of application of the temporary derogation enabling Portugal to postpone the introduction of the common system of VAT, this Member State is to be treated as a third country for the purposes of applying the First, Sixth, Eighth and Tenth VAT Directives.

(1) COM(83)426 final

(2) Fifteenth Directive (83/648/EEC) of 19 December 1983 (OJ n°L 360 of 23 December 1983, p. 49) and Twenty-first Directive (86/247/EEC) of 16 June 1986 (OJ n°L 164 of 20 June 1986, p. 27)

The First Report discussed the difficulties encountered in most Member States in meeting the deadline of 1 January 1978 laid down in the Sixth Directive for incorporating the VAT system into their legislation and the need for a Ninth Directive (of 26 June 1978) to authorize certain Member States to defer application of the system until 1 January 1979.

The decisions by the Court of Justice regarding the direct rights that may be invoked by taxable persons during the period from 1 January 1979 to the date on which national legislation is brought into line with the Sixth Directive (1) has been followed by a decision in Case 70/83 (2), which concerned a reference to the Court for a preliminary ruling on the interpretation of Article 13(B)(d)(1) of the Sixth Directive and of Article 1 of the Ninth Directive.

In its decision, the Court ruled that, in the absence of the implementation of the Sixth Directive, it was possible for the provision concerning the exemption from tax contained in Article 13(B)(d)(1) of the Sixth Directive to be relied upon by a credit negotiator in relation to transactions carried out between 1 January and 30 June 1978 where he had refrained from passing that tax on to persons following him in the chain of supply. It thus took the view that the Ninth Directive extending the time limit for the entry into force of the Sixth Directive did not have retroactive effect in respect of transactions carried out by economic operators prior to its entry into force.

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(1) See introduction to the First Report.

(2) [1984] ECR 1075.

This report will examine in particular the system's internal difficulties, distinguishing between those stemming from the divergences between national laws that the Sixth Directive expressly left untouched (Part I) and those to do with the interpretation of the Directive (Part II). Part III will look at the main directives proposed or adopted during the review period on the basis of the Sixth Directive.

The situation described is that obtaining as at 30 June 1987.

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PART 1DIVERGENCES NOT REMOVED BY THE DIRECTIVE

For the reasons mentioned in the First Report, a number of divergences have been left untouched by the Sixth Directive.

These can be classified into two groups :

- divergences arising from certain imperfections in the present system or from certain optional provisions permitted by the Directive (Chapter I) ;
- divergences arising from the rights of option for taxation authorized by the Directive (Chapter II).

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Chapter I

Divergences stemming from certain imperfections or from certain optional provisions permitted

In the First Report, the Commission noted that certain imperfections in the application of the common VAT system could be rectified without too much difficulty by clarifying some aspects of the Sixth Directive and even by amending it in some places in a way that would not affect the general disposition of the system.

The proposal for a Nineteenth Directive (1), sent to the Council on 5 December 1984, is a step in this direction since it represents a continuation of the efforts to establish a uniform common system of VAT while, at the same time, permitting more uniform application of the system for collecting own resources.

The Economic and Social Committee and Parliament gave their opinions on the proposal on 3 July 1985 and 6 April 1987 respectively (2). However, the optional provisions have not been removed from the Sixth Directive. Only those which have been the subject of proposed amendments or to which Member States have had frequent recourse during the review period will be mentioned.

(1) OJ n°C 347 of 19 December 1984, p. 1.

(2) For details concerning these opinions and the proposed amendment, see Chapter III below.

A. Power to derogate from the definition of taxable person (second subparagraph of Article 4(4))

The United Kingdom consulted the VAT Committee pursuant to the second subparagraph of Article 4(4) with a view to including in its national legislation the right to "treat as a single taxable person persons established in the territory of the country who, while legally independent, are closely bound to one another by financial, economic and organizational links".

The United Kingdom is faced with a growing fragmentation of businesses, that is to say, the practice whereby a person artificially subdivides a single activity into a number of independent entities so as not to register for VAT some or even all of those entities.

To combat such tax avoidance, the United Kingdom has incorporated into its national legislation measures whereby a number of such entities may be treated as a single taxable person for the purposes of registration and payment of VAT.

It had already consulted the VAT Committee, pursuant to Article 4(4), on the matter of the application of a legislative provision concerning groups of two or more legal persons. At the time, Germany, Denmark, Ireland and the Netherlands had also consulted the VAT Committee on the matter and the Commission had instituted infringement proceedings against Germany on the basis of Article 169 of the Treaty (1). This Member State meanwhile brought its national legislation into line with the Sixth Directive and, as a result, the infringement proceedings were not pursued further.

(1) See First Report, Part I, Chapter I, Point A.

B. Power to derogate from the definition of taxable amount upon importation (Article 11(B)(2))

The power to adopt as the taxable amount upon importation from another Member State the value defined in the customs rules, as provided for in Article 11(B)(2) of the Sixth Directive, is no longer compatible with the degree of integration achieved by the Community or with the objective of establishing the internal market. The real consideration must be taken into account in a VAT system while, given the prospect of a single market, steps must be taken to ensure that, in determining the taxable amount, a single criterion is applicable to intra-Community transactions and transactions carried out within the territory of the country. The power in question could, however, be retained in respect of imports from third countries. Accordingly, the proposal for a Nineteenth Directive provides for an amendment to the Sixth Directive along these lines by restricting the power to opt for the customs value solely to imports from third countries.

On 22 March 1982 the Commission brought an action before the Court of Justice following the failure of one Member State to comply with the rules laid down in the Sixth Directive for determining the taxable amount in the case of valuable racehorses (Case 95/82). The Member State in question having meanwhile complied with Community rules, the action no longer served any useful purpose and was removed from the Court Register.

C. Powers in connection with the special scheme for small undertakings (Article 24)

1. The First Report pointed out that the broad latitude Member States were allowed had led to marked divergences between Member States' administrative arrangements for small undertakings. It added that those divergences should be ironed out by the end of the transitional period by means of a common simplified scheme and a common system of exemptions.

In accordance with Article 24(8), the Commission drew up a separate report analyzing the different exemption, tax-relief and flat-rate schemes in force in Member States (1).

(1) COM(83)748 final of 15 December 1983.

As the follow-up to that report, the Commission on 9 October 1986 sent to the Council a proposal for a Directive amending Article 24 (1). The purpose of the proposal is to make for easier management, both for administrations and for taxable persons themselves, as well as to facilitate the control and collection of tax while preserving the economic neutrality of the specific schemes for small businesses and the fundamental rules on tax collection.

The proposal is also consistent with the wishes of the European Council, which expressly called for removal of obstacles to the establishment and growth of small and medium-sized businesses and for simplification of the tax and administrative environment for such businesses. This proposal forms part of the Community action programme for small and medium sized enterprises (SME), approved by the Council Resolution of 3 November 1986 (2).

(1) OJ n°C 272 of 28 October 1986.

(2) OJ n°C 287 of 14 November 1986, p. 1

2. Italy consulted the VAT Committee under Article 24(1) of the Sixth Directive on the introduction for each of the financial years 1985, 1986 and 1987 of measures to assist small and medium-sized businesses whose turnover in 1984 had not exceeded LIT 780 million (equivalent at the time to some 570 000 ECU or BFR 26 million) and taxable persons carrying on an artistic or professional activity.

The measures on which the VAT Committee was consulted included the system of deductions and the method of determining turnover.

As regards deductions, the businesses concerned may opt for a flat-rate scheme under which the amount of tax for which they are liable is calculated by deducting from the tax chargeable on taxable transactions flat-rate percentages fixed for each sector of activity. In addition, businesses whose turnover in 1984 did not exceed LIT 18 million (equivalent at the time to some 13 000 ECU or BFR 600 000) are exempt from certain invoicing and accounting requirements.

As regards determination of turnover, the tax administration is authorized, subject to certain conditions, to correct tax returns sent in by the taxable persons concerned on the basis of a presumption linked to the nature of the business and to other particulars such as the size and location of the premises, the number of workers, the amount of goods bought in, and energy consumption.

D. Power to retain or introduce simplification procedures that derogate from the Sixth Directive

1. A list of the derogations notified to the Commission under Article 27(5) is annexed to the First Report. The derogations in question had been in force in Member States before 1 January 1977.

In that report, the Commission had stated that it attached particular importance to compliance with the substantive rules set out in Article 27(1) and that it thus reserved its position on certain of those measures.

In one of the infringement procedures initiated in respect of several of those measures, the Court of Justice ruled on 10 April 1984 in Case 324/82 against Belgium (1) that, by retaining the catalogue price as the basis for charging VAT on cars, as a special measure derogating from Article 11 of the Sixth Directive, when the requirements laid down in Article 27(5) were not fulfilled, Belgium had failed to fulfil its obligations under the EEC Treaty.

Infringement proceedings against France in connection with the flat-rate determination of maximum taxable amounts for imports and supplies of valuable racehorses were terminated, France having brought its legislation into line with the Sixth Directive.

The Commission also decided to terminate the proceedings instituted against Luxembourg in connection with application of the flat-rate scheme for farmers to certain goods.

2. Since publication of the First Report, a number of new measures have been notified by Member States on the basis of Article 27(1) to (4). The measures were as follows :

- Germany and Luxembourg : a derogation to be introduced as part of a draft agreement between Germany and Luxembourg with a view to VAT being levied on all construction and maintenance work for a frontier bridge by the German authorities alone since Germany will assume responsibility for those operations (2);

(1) [1984] ECR 1861.

(2) Council Decision of 13 March 1983 (OJ n°L 181 of 6 July 1983, p. 25).

- Germany and Netherlands : a derogation whereby, under a draft agreement between Germany and the Netherlands, all the construction and maintenance work relating to the diversion of the Ems channel and the extension of the port of Emden would be subject to German VAT only, with Germany assuming responsibility for this work (1);
- France : a derogation whereby, for a period of four years, any deductible tax credit is not to be refunded in respect of automatic gaming machines but is to be set against tax due in subsequent tax periods (2).
- United Kingdom :
 - a) introduction of a special tax accounting scheme designed to avoid certain types of fraud or tax evasion on supplies of gold, gold coins and gold scrap between taxable persons (3);
 - b) introduction for a period of two years of a system for charging VAT designed to prevent tax evasion in cases where the marketing structure of certain firms is based on the sale of their products to unregistered resellers (4). This measure had been notified previously pursuant to Article 27(5) but was subsequently amended.

(1) Council Decision of 19 September 1984 (OJ n°L 264 of 5 October 1984, p. 26)

(2) Council Decision of 23 October 1984 (OJ n°L 268 of 30 October 1984, p. 17)

(3) Council Decision of 13 April 1985 (OJ n°L 264 of 5 October 1984, p. 27)

(4) Council Decision of 13 June 1985 (OJ n°L 199 of 31 July 1985, p. 60)

The measure authorized by the Council Decision of 13 June 1985 on the basis of Article 27(4) was extended for a further period of two years (1);

- c) application of flat-rate measures in respect of non-deductible VAT charged on fuel expenditure in the case of company cars (2);
- d) measures to simplify calculation of VAT in respect of long stays in hotels by assessing on a flat-rate basis the part of the service deemed to correspond to a letting of immovable property exempt under Article 13(B)(b)(1) of the Sixth Directive (3).

This measure replaces a wider-ranging provision based on Article 27(5);

- e) measures to combat tax avoidance designed to prevent taxable persons artificially reducing the price for supplies or imports of goods or for supplies of services to totally or partially exempt persons with whom they have certain family, legal or business ties specified in national legislation. In such circumstances, the free market price may be taken as the consideration for the transaction, irrespective of whether or not the latter is actually taxed, if there is a serious presumption of tax avoidance (4);

(1) Council Decision of 25 May 1987 (OJ n°L 188 of 8 July 1987, p. 52)

(2) Council Decision of 21 July 1986 (OJ n°L 212 of 2 August 1986, p. 35)

(3) Council Decision of 10 December 1986 (OJ n°L 359 of 19 December 1986, p. 59)

(4) Council Decision of 11 April 1987 (OJ n°L 132 of 21 May 1987, p. 22)

- f) derogation from Article 17(1) authorizing the United Kingdom to require firms with an annual turnover of less than 340 000 ECU to defer the right to deduct tax until it has been paid to the supplier. This measure, which is regarded as a simplification measure, forms part of an optional scheme for such firms based on the third subparagraph of Article 10(2) of the Sixth Directive (1);
- g) introduction for a two-year period of an anti-avoidance measure derogating from the Sixth Directive and aimed at preventing groups of businesses which are treated as a single taxable person, within the meaning of Article 4(4) of the Directive, and which are not entitled to deduct tax in full from being able to effect full deduction of the tax on certain acquisitions of capital assets by means of a company established and dissolved for that purpose (2).

(1) Pursuant to Council Decision of 23 July 1987 (OJ n°L 273 of 4 August 1987, p. 40), the authorization to introduce this measure applies only until 30 September 1990, with the possibility of an extension beyond that date on the basis of a report and, if appropriate, on a proposal from the Commission.

(2) Decision not published (deemed to have been adopted on 13 April 1987)

CHAPTER II

Divergences arising from the rights of option for taxation

A. Rights of option under Article 28

Article 28 allows Member States to apply for a transitional period a number of derogations from the normal arrangements of the common VAT system. This period was to last initially for five years as from the entry into force of the Sixth Directive. The Council undertook to determine, before its expiry, whether any or all of those derogations should be abolished.

On 17 January 1983 the Commission sent to the Council a report in which it discussed the application by Member States of those derogations and the difficulties that their abolition would cause (1). The report was examined by the Council's ad hoc working party on 30 March 1983.

Following that examination, the Commission concluded that most of the derogations under Article 28(3) of the Directive should be and could be abolished. To that end, it transmitted to the Council on 4 December 1984 a proposal for an Eighteenth Directive on the gradual abolition, in the light of their economic, social and budgetary impact of most of the derogations specified in that provision (2).

The Economic and Social Committee and Parliament delivered their opinions on the proposal on 3 July 1985 and 6 April 1987 (3).

The proposal is currently being examined within the Council.

(1) COM(82) 885

(2) OJ n°C 347 of 29 December 1984, p. 3.

(3) For details regarding these opinions and the proposed amendments, see Part III below.

In its report of 17 January 1983, the Commission also discussed the derogations under Article 28(2) authorizing Member States to maintain in force, subject to certain conditions and pending abolition of tax frontiers, the exemptions with refund of input taxes, commonly referred to as zero-rating, applicable on 31 December 1975. The report highlights in particular the drawbacks of zero-rating within the territory of the country, especially where it applies to a large proportion of domestic consumption.

B. Rights of option under Article 13(C)

Special attention was paid to these rights of option for taxation under Article 13(C) in the First Report, to which are annexed three tables giving an overall picture of the situation in the individual Member States as regards each of the transactions involved.

The proposal for a Nineteenth Directive provided for an addition to Article 13(C) whereby the right of option allowed for banking and financial transactions may not be granted in respect of "Services rendered by financial institutions in issuing or managing payment cards or other similar documents".

The reasons for this inclusion are set out in Part II, Chapter V : Questions of interpretation concerning exemptions, point F : Payment cards.

PART II

DIFFICULTIES CONNECTED WITH THE INTERPRETATION OF CERTAIN PROVISIONS IN THE DIRECTIVE

The VAT Committee continued its work on the basis of questions raised by Member States and by the Commission departments themselves concerning the application of Community VAT provisions, and in particular those of the Sixth Directive.

It held eight meetings between 1 January 1982 and 31 December 1986 and fifty-four working papers were discussed, seven of these under the consultation procedure.

A number of guidelines agreed by a majority of the Committee were the subject of proposals for improving the Sixth Directive sent by the Commission to the Council in the context of its aforementioned proposal for a Nineteenth Directive.

This report will also discuss the main implementing difficulties encountered during the review period, the guidelines agreed by the Committee and any improvements made or proposed. It will also mention the relevant case law, commenting briefly on certain decisions taken by the Court of Justice after the First Report had been published.

CHAPTER I

Application of Article 2 to certain transactions

In its decision of 28 February 1984 in Case 294/82, the Court of Justice ruled that Article 2 of the Sixth Directive must be interpreted as meaning that no import turnover tax arises upon the unlawful importation into the Community of drugs not confined within economic channels strictly controlled by the competent authorities for use for medical and scientific purposes (1).

The question as to the scope of this ruling and its consequences for the application of Article 2 of the Sixth Directive was put to the VAT Committee. By a large majority, the Committee felt that transactions carried out within the territory of the country and involving goods that were the subject of a prohibition on marketing fell outside the scope of VAT, subject to the conditions and within the limits that could be deducted from the ruling.

Two questions have meanwhile been referred to the Court of Justice for a preliminary ruling on the interpretation of Article 2 of the Sixth Directive in the light of the aforementioned decision with regard to the supply of narcotic drugs within the territory of a Member State (Case 289/86 Vereniging Happy Family, Amsterdam) and the supply of amphetamines within the national territory where such supply is forbidden by law but tolerated in practice (Case 269/86 W.J.R. Mol).

(1) [1984] ECR 1177

CHAPTER II

Liability to tax in respect of certain activities (Article 4(5))

1. Notaries and sheriffs' officers

The previous report discussed the difficulties arising in connection with the taxable position of certain professions whose members may authenticate acts in their capacity as public officers. They included inter alia notaries and sheriffs' officers in the Netherlands, whose public duties were not subject to VAT arrangements. The Commission took the view that persons carrying on such professions should be liable to VAT pursuant to Article 4 of the Sixth Directive since there could be no denying that they performed independently, that is to say, in the absence of any relationship of employer and employee, an economic activity taken to mean a permanent provision of services for consideration. It also felt that the underlying principle of VAT, namely a comprehensive tax on consumption, required Article 4(5) to be interpreted strictly; accordingly, that provision would apply only to activities performed by bodies governed by public law and related to the fundamental powers and duties of a public authority and not to activities that can be performed intrinsically by individuals in a profit-making capacity.

The Commission deployed these arguments among others when it brought an action before the Court of Justice under Article 169 of the Treaty.

In its decision of 26 March 1987 (Case 235/85), the Court upheld the Commission's position (1).

(1) Not yet published in the European Court Reports;
OJ n°C 108 of 23 April 1987, p. 5.

2. Supply of control and support services to air navigation

A question concerning the tax arrangements applicable to control and support services for air navigation, and in particular the tax status of suppliers, State bodies, semi-public bodies or local authorities supplying such services either direct or through a concessionary company, was submitted to the VAT Committee.

On the basis of an analysis by the Commission departments, guidelines were agreed for three categories of support services for air navigation. The Committee decided almost unanimously that suppliers of services in the airport zone (landing, parking, etc.) were liable to tax, with such services being taxed or exempted, as the case may be, on the basis of Article 15(9); moreover, a majority of the delegations took the view that suppliers of services in the approach and take-off zone (control of the air space in the vicinity of the airport by control towers) and suppliers of services in the upper and lower air spaces (control of en-route navigation) were not liable to tax on the basis of the first subparagraph of Article 4(5). The Committee decided unanimously that Eurocontrol was not liable to tax either in respect of en-route navigation control or in respect of the calculation and collection of fees charged to airlines and the sharing of the proceeds among the control bodies of the Member States overflown.

CHAPTER III

Place where services are supplied (Article 9)

A. Hiring out of movable tangible property

1. The First Report stressed that an excessively literal interpretation of Article 9(1) could, in certain cases, lead to non-taxation of the hiring out of movable tangible property in the country in which it should be taxed, that is to say, the country in which the hiring out occurs.

The Tenth Council Directive of 31 July 1984 (1) sets out to remedy this state of affairs by altering the place of taxation for the hiring out of such property, which is now the place where the customer is located (Article 9(2)(e)).

The hiring out of forms of transport was however excluded from the amendment and is still taxable, therefore, at the place at which the supplier is located, in accordance with the principle set out in Article 9(1).

2. The Commission departments were called upon to examine a number of problems raised by a Member State in connection with the application of the Sixth and Tenth Directives to certain international leasing transactions.

The problems related in particular to situations which had more to do with hiring out than with leasing proper and in which a leasing company purchases equipment in a country other than that in which it has its head office with a view to hiring it out to a taxable person in that country.

Under the circumstances, the leasing company is de facto carrying on an economic activity in the customer's country. Accordingly, an attempt must be made to apply in the first place the territoriality rule laid down in Article 9(1), and it is only if the supplier does not have a fixed establishment in the customer's country that the rule set out in Article 9(2)(e) is applicable in accordance with the Tenth Directive.

(1) OJ n°L 208 of 3 August 1984, p. 58

Questioned on this matter, the delegations to the VAT Committee concurred with this analysis but noted that, where Article 9(2)(e) was applicable, VAT charged on the purchase of equipment would be refunded under the procedure provided for in the Eighth and Thirteenth Directives, depending on whether the leasing company was established within the Community or in a third country.

The analysis remains the same in the case of forms of transport hired out under the same circumstances.

However, since such goods are excluded from the scope of the Tenth Directive, they are taxable in accordance with the general principle laid down in Article 9(1), that is to say, at the place where the supplier is located, and in the case in point this is the same as the place at which the customer is located; if the supplier does not designate a place of business or does not have a fixed establishment, the person liable to pay tax may be designated in accordance with Article 21(1)(a). A majority of the delegations to the VAT Committee held to the view, however, that the hiring out of forms of transport could be taxed in the country in which they were purchased and hired out by the supplier only if the latter had a place of business or a fixed establishment there. Where the supplier was established in a third country, the Committee was unanimous in the view that taxation must take place in the customer's country, with a large majority basing itself on Article 9(3)(b) and a minority on Article 9(1).

B. Treatment of pallets and containers as forms of transport

The First Report also recalled the need to confer an identical meaning in Member States on the concept of "forms of transport" in order to ensure that the place of taxation for certain items of property, and in particular those which are, by their very nature, liable to cross frontiers, does not vary depending on whether they rank as "forms of transport" or "movable tangible property".

Consequently, the Commission, with that need in mind and in order to take account of the view of the large majority of Member States, inserted in its proposal for a Nineteenth Directive a clarification in respect of Article 9 that reads as follows :

"The expression 'forms of transport' in this Article includes pallets and containers, and equipment and apparatus capable of being drawn or pushed in order to perform a contract for transport or towing".

C. Definition of the concept of "fixed establishment" in Article 9

1. Article 9(2)(e) lists a number of services for which the place of taxation is the place where the customer has established his business or has a fixed establishment to which the service is supplied.

Now, it emerged that the concept of fixed establishment was not the same in all Member States and that this gave rise to problems when it came to determining :

- i) the place of taxation for the transactions specified in Article 9(2)(e), and
- ii) the procedure for refunding tax on the basis of the Sixth or Eighth Directive.

The VAT Committee was asked for its views on the two possible interpretations of this concept : one according to which a fixed establishment was regarded as any fixed installation from which transactions (sales or supply of services) can be carried out; the other according to which this (potential) capacity to carry out transactions is unnecessary, a simple information office or a simple administrative office being sufficient. A large majority of the Committee considered that fixed establishment was to be defined, if anything, without reference to its capacity to effect taxable transactions.

The proposal for a Nineteenth Directive took account of this guideline by providing for an addition to Article 9 defining fixed establishment as "any fixed installation of a taxable person, even if no taxable transaction can be carried out there".

2. Article 9(1) lays down the general principle of the place of taxation for services, declaring it to be "the place where the supplier has established his business or has a fixed establishment from which the service is supplied...".

The concept of "fixed establishment" laid down in that provision was supplemented by the decision of 4 July 1985 by the Court of Justice in Case 168/84 *Berthold v Finanzamt Hamburg-Mitte-Altstadt* (1), in which the Court ruled in particular that an installation for carrying on a

(1) Not yet published in European Court Reports;
OJ n°C 191 of 31 July 1985, p. 8.

commercial activity on board a ship sailing on the high seas outside the national territory - the activity in question being the operation of gaming machines - may be regarded as a fixed establishment within the meaning of Article 9(1) only if the establishment entails the permanent presence of both the human and technical resources necessary for the provision of those services and it is not appropriate to deem those services to have been provided at the place where the supplier has established his business.

D. Application of Article 9(2)(e) to public broadcasting organizations

Article 9(2)(e) lists a number of services that are taxable at the place where the customer, provided he is a taxable person in a Member State, is established. In the case of such services, the customer's status thus determines the place of taxation.

It transpired that the tax status of broadcasting organizations was not the same in all Member States as regards their non-commercial activities. In some Member States they themselves are considered as non-taxable persons and their activities as falling outside the scope of the tax whereas in other Member States they rank as taxable persons, with the services they supply thus being exempt.

This situation is such as to create legal uncertainty and even double taxation or non-taxation, since the supplier of services is not necessarily aware of the status of the body to which he supplies his services.

The only way to resolve this problem is by applying Article 9(2)(e) uniformly to public broadcasting organizations in all Member States, irrespective of their tax status (exempt or excluded from the scope of VAT), in all cases where a service mentioned in that provision is supplied to such a body. When this question was put to it, the VAT Committee, in the interests of simplification, decided almost unanimously in favour of such a solution.

E. Telecommunications services

A number of questions were raised concerning the arrangements for certain telecommunications services since, in most cases, these were international in nature. The VAT Committee agreed on certain guidelines relating in particular to the place of supply of international telecommunications services (the country of the person paying for the communication in accordance with the criterion of the place where the supplier has established his business), telephone communications from vessels sailing on the high seas (outside the territorial scope of the tax), telecommunications services supplied to sea-going vessels and notably the use of coastal relay stations (regarded as services to meet the direct needs of such vessels and exempt within the limits laid down in Article 15(8)), and services supplied by public telecommunications authorities and involving use of their networks by other Member States (in favour of an exemption similar to that for transactions treated as exports).

CHAPTER IV

Questions of interpretation concerning the taxable amount (Article 11)

A. Minimum taxable amount

In March 1981, the Commission instituted infringement proceedings under Article 169 of the Treaty against Belgium for failure to bring its national VAT legislation governing calculation of the taxable amount for cars into line with Articles 11 and 27 of the Sixth Directive.

In its application to the Court of Justice, the Commission contended that the Belgian rules were not compatible with Article 11 since their effect was to tax systematically supplies or imports of new cars on the basis of a value generally higher than the consideration actually received by the suppliers or the price paid by the private importer. As regards supplies on the national market, the Belgian rules imposed VAT on the value of all price discounts or rebates, which is contrary to Article 11(A)(3)(b). As far as car imports were concerned, the Belgian rules did not take account of the price actually paid.

The Commission also took the view that the measures in question, which had been notified on the basis of Article 27 (5), were not covered by that provision because they were too general in character; in point of fact, they rendered the system laid down in Article 11 practically purposeless in the market sector in question and were therefore disproportionate to the aim in view. Lastly, the Commission disputed that the provisions at issue were justified by the desire to prevent tax evasion or avoidance or that they constituted genuine measures for simplifying the procedure for charging the tax.

In its decision of 10 April 1984 (Case 324/82) (1), the Court upheld the arguments put forward by the Commission.

(1) Loc. cit., see Part I, Chapter I, point D.1.

Following the Court's decision, Belgium amended its legislation so that VAT would in future be calculated on the basis of the value actually paid by the buyer.

At the same time, however, it envisaged applying a registration tax payable on the difference between the list price and the price invoiced at the same rate as the VAT rate.

Since the new measure did not seem to be in conformity either with the Court's decision, the Commission on 2 December 1985 instituted fresh proceedings under Article 169 (Case 391/85).

B. Supply of a new item with a used item taken in part-exchange

The legislation of Ireland and the Netherlands provides that, when a new item is supplied and the supplier takes a used item of the same kind in part-exchange, the taxable amount is to be reduced by the value of the used item. The Commission took the view that this arrangement constituted a derogation from Article 11 of the Sixth Directive that could not be justified by Article 32 of that Directive and brought two actions before the Court of Justice (Cases 16 and 17/84).

The Court did not accept the Commission's arguments, taking the view that the systems at issue were in principle covered, both as regards their object and their effects, by Article 32 of the Sixth Directive and that they did not infringe Article 11 of that Directive. Accordingly, it dismissed the Commission's applications in two decisions dated 10 July 1985 (1).

C. Subsidies

1. Article 11(A)(1)(a) stipulates that "subsidies directly linked to the price" must be included in the taxable amount. Furthermore, the second indent of Article 19(1) permits Member States who so wish to include in the denominator of the deductible proportion the amount of subsidies which are not directly linked to the price.

(1) Not yet published in the European Court Reports;
OJ n°C 195 of 3 August 1985, p. 4.

Following an analysis of the main difficulties of interpretation concerning the concept of subsidies as referred to in those provisions, the Commission considered that the whole problem needed to be thought out afresh (1).

In the course of this reappraisal, the Commission noted that the expression "subsidies directly linked to the price" of transactions carried out by a taxable person could be interpreted only in a strict and literal sense for the purposes of Article 11(A)(1)(a) and that a subsidy was to be included in the taxable amount only if three conditions were met :

- a) it constituted the consideration (or part of the consideration);
- b) it was paid to the supplier;
- c) it was paid to a third party.

A majority of the VAT Committee agreed with this interpretation.

2. A problem of interpretation also arose in connection with the tax arrangements applicable to Community subsidies paid out under the common organization of the market in milk and milk products. It is a known fact that the Community encourages the adoption of measures to promote sales, publicity and market research in respect of those products.

The question was put to the VAT Committee whether the Community's contribution to expenditure incurred in carrying out such measures was to be taxed as payment for a service that the "organizations concerned" (producers of, and traders, in milk products) were regarded as supplying to the Community through a "government agency" responsible for distributing Community aid. According to the Commission's departments, neither the Community nor the government agency could be regarded as a customer for any service whatsoever. The subsidy was designed solely to reimburse some of the expenditure incurred by the "organizations concerned" in respect of services purchased from other taxable persons (e.g. advertising agencies).

(1) Part Two, Chapter IV, point C of the First Report

Since, therefore, it was tantamount to a purchasing subsidy, the Commission departments took the view that one of the three conditions specified above was not met.

A large majority of the Committee agreed, since it considered that Community subsidies intended for the financing of publicity measures for milk products did not represent remuneration in respect of services supplied to the Commission and were not liable to VAT where they contributed to the payment of expenses incurred.

D. Incidental expenses to be included in the taxable amount

1. Collection commission charged by a carrier

In its decision of 12 June 1979 in Case 126/78 (1), the Court of Justice ruled that "if a carrier has undertaken, in addition to the transport of the goods, to collect the price of the goods before delivering them to the consignee (cash-on-delivery system) the collection of that price is a service ancillary to the transport within the meaning of Annex B, item 5, to the Second Directive of 11 April 1967" and that "for the purposes of the application of value added tax Member States are not empowered to treat an ancillary service such as the collection of the cash-on-delivery price separately from the service of the transport of goods".

The VAT Committee was asked whether the conclusions reached by the Court could be applied to Article 11(A)(2)(b) of the Sixth Directive and whether, therefore, the commission charged by a carrier for collecting on behalf of the seller the payment for goods carried was to be included in the taxable amount for the transport service as an incidental expense within the meaning of Article 11.

(1) [1979] ECR 2041

The VAT Committee considered that it was impossible merely to extend the Court judgment to the context of Article 11(A)(2)(b) and that only examination of the terms of the contract concluded between consignor and carrier would reveal whether or not this commission was an incidental expense.

2. Interest payable on hire-purchase sales

The First Report raised the matter of the arrangement to be applied to price supplements charged by a supplier in the case of a hire-purchase sale, the question being whether financing charges were to be exempted on the basis of Article 13(B)(d) or whether, on the contrary, the determining factor was that such financing charges were of the nature of incidental expenses and were, therefore, to be excluded from the exemption in respect of interest payments provided for in Article 13.

When the question was put to the VAT Committee, a majority of its members considered that, if there were no real loan agreement, the price supplement payable on a hire-purchase sale was to be included in the taxable amount for supplies of goods.

E. Importation of software

The problem of determining the taxable amount to be applied in respect of imports of software was referred to the VAT Committee.

In the case of "normalized" or generally used software, the Committee considered that there was a single import of goods the whole value of which was to be taxed.

In the case of specific software, it noted that there was both an import of goods (the physical support) and a supply of services (the data).

In intra-Community trade between taxable persons, the physical support will be treated as an accessory to the data and both supplies will be taxed within the Member State of the user as a single supply of services in accordance with the criteria laid down in the third indent of Article 9(2)(e). In order to avoid double taxation, the physical support will not be taxed upon importation.

The Committee has still to state its view on the tax arrangements for trade between third countries and individuals.

F. Carriage of passengers by sea or air between two places located in a single Member State, with the journey including passage through or above international waters or above foreign territory.

The Commission departments had encountered problems relating to the collection of VAT on transport operations carried out partly outside national territory. Some Member States considered that air or sea transport involving passage above or through international waters or the territory of another State no longer ranked as a journey within the territory of the country in respect of the distance covered outside the national territory. It was particularly important to know whether "own resources" could be collected in respect of that part of the price of the ticket relating to that distance.

When consulted about this problem the Committee considered, by a large majority, that, on the basis of the Sixth Directive, the whole of the journey in question should be considered as taking place entirely within the Member State concerned.

Accordingly, the Commission, in its proposal for a Nineteenth Directive, inserted into Article 9(2)(b) a new provision whereby "a journey by sea or air shall be deemed to take place entirely within a country when the place of departure and the place of arrival are in that country, provided there is no stop in another country".

In its decision of 4 July 1985 (Case 188/84 Berkholz v Finanzamt Hamburg-Mitte-Altstadt) (1) and 23 January 1986 (Case 263/84 Trans Tirreno Express v Ufficio Provinciale IVA) (2) the Court went some way towards endorsing the principles set out in the amendment proposed by the Commission. It ruled that Member States may charge VAT on transport services supplied on the high seas during journeys made either between two points in the same Member State or between two Member States.

(1) *Loc. cit.*

(2) Not yet published in the European Court Reports, OJ n°C 77 of 5 April 1986, p. 8

CHAPTER VQuestions of interpretation concerning exemptions (Articles 13, 14 and 15)A. Exemptions under Article 13(A)(1)

The First Report referred to implementing difficulties associated in many cases with the imprecise nature of certain provisions of Article 13(A)(1) concerning exemptions and to their repercussions both for application of the uniform basis of assessment and for own resources.

The proposal for a Nineteenth Directive dated 5 December 1984 attempted to improve the situation by incorporating the clarifications and amendments necessary to ensure better interpretation of the relevant texts. The VAT Committee agreed a number of guidelines for certain questions relating to application of the tax while the Court of Justice delivered a ruling in the case involving the exemption for transport services carried out on behalf of the Deutsche Bundespost.

a) Exemption relating to the supply of services by the public postal services

On 11 July 1985 the Court of Justice delivered its ruling in Case 107/84 (1). The First Report mentioned that the legislation of one Member State extended the exemption for the supply of services by the public postal services (Article 13(A)(1)(a)) to transport undertakings which carried mail on behalf of the public postal service. The Commission had taken the view that, like any other firm which was exempted, the public postal service should bear VAT on the inputs relating to its exempt activities and that it could not permit an extension of the exemption to the supply of services at issue. This view was endorsed by the Court.

(1) Not yet published in the European Court Reports;
OJ n°C 200 of 8 August 1985, p. 8

b) Exemption concerning hospital and medical care and closely related activities (Article 13(A)(1)(b))

In order to ensure that the differing assessments of the conditions governing eligibility for this exemption do not give rise to implementing difficulties, the Commission has included in its proposal for a Nineteenth Directive a provision extending the exemption to the entire hospital sector. A definitive exemption of this kind would render redundant the derogation based on Article 28(3)(b), read in conjunction with point 10 of Annex F, whereby hospital establishments not referred to in Article 13 as currently worded may continue to be exempt during the transitional period.

The expression "and closely related activities" contained in this provision also seemed to be interpreted in a fairly restrictive manner by Member States. This was confirmed when the matter was examined by the VAT Committee.

Nevertheless, a Community list of the transactions referred to was drawn up and accepted by a large majority of the delegations. It would seem, therefore, that the proposed amendment extending the exemption to the entire hospital sector could be supplemented by such a list.

c) Exemption for the provision of medical care in the exercise of the medical and paramedical professions

Two infringement procedures have been initiated under Article 169 of the Treaty against the United Kingdom and Ireland following an extension of the exemption to supplies of goods. The exemption in question applies to supplies of pairs of spectacles under a medical prescription.

In the case of the United Kingdom, an action was brought before the Court on 27 March 1985.

d) Exemptions concerning "certain services closely linked to sport" (Article 13(A)(1)(m))

The conditions governing the granting of this exemption were deemed to be strict enough for it to be proposed that the expression "certain services" be replaced by "services" without this creating any problem.

However, the wording of this provision gives rise to certain problems of interpretation since the Court of Justice was asked, in Case 273/86, to give a preliminary ruling on whether "... the supply of food and drink by a sports club to its members in a canteen run by the club (can) be regarded as a service closely linked to sport or physical education supplied to persons taking part in sport or physical education within the meaning of Article 13(A)(1)(m) of the Sixth Council Directive..."

The Commission proposed that the Court reply clearly in the negative to this question. Since the applicant subsequently withdrew his action, the Court removed the case from its Register on 8 April 1987.

e) Exemption for "certain cultural services" (Article 13(A)(1)(n))

In the proposal for a Nineteenth Directive, the imprecise term "certain" is replaced by a list of exempt services based on the corresponding lists applicable in a number of Member States.

f) Exemption for supplies of services by artists

Apart from the improvements to be made to this part of Article 13, the proposal for a Nineteenth Directive introduced two specific exemptions, one for works of art proper (supply of works of art by the artist who created them) and one for the supply of services by actors, authors, composers and writers.

However, in the opinions delivered by them, Parliament and the Economic and Social Committee opposed such exemptions, notably on the ground that preferential treatment for supplies of works of art and supplies of services by artists was not, in their view, justified.

The Commission took account of those opinions in its amended proposal for a Nineteenth Directive by proposing that the provisions at issue be deleted. As a compromise, the exemption for the supply of services by authors, artists and performers of works of art will be maintained on a transitional basis in accordance with Article 28(3)(b), taken together with point 2 of Annex F.

B. Exemptions under Article 13(B)

Three questions arise in connection with the application of Article 13(B). They concern the tax treatment of tourist assistance operations, the tax treatment of payment cards (this matter having already been dealt with in part in the First Report), and the application of Article 13(B)(d)(4) to "platinum nobles".

a) Tourist assistance operations

During examination within the Council of the Community texts relating to insurance, disparities came to light regarding the application of the Sixth Directive to tourist assistance activities, i.e. assistance to travellers.

When the matter was referred to it, the VAT Committee, on the basis of an analysis presented by the Commission departments, felt by a large majority that services consisting of the provision of cover in respect of the risks concerned (reimbursement of medical expenses; costs resulting from necessary extension of stay; repatriation of the insured on medical grounds and of an accompanying relative; travel expenses of the insured in the event of the death of a member of his family; repatriation of the remains of the insured; charges for towing or repatriating a vehicle; dispatch of spare parts) and supplied by an organization other than an automobile club should be regarded as insurance services coming under Article 13(B)(a) and that the contributions collected by these organizations by way of consideration for those services should be exempted on the basis of that provision.

However, in the case of assistance rendered by automobile clubs, the problem remains since the situation varies from one Member State to another : some Member States charge tax on the full membership fee while others apply an exemption on the basis of Article 13(A)(1)(1) but tax additional fees paid in exchange for special advantages; a number of Member States would prefer to see a standard breakdown of the fee into a taxable component and an exempt component.

The Committee also considered that services supplied by the "assister" to the insurer fell within the scope of the tax and could be exempted or taxed depending on their nature.

b) Payment cards

Under the proposal for a Nineteenth Directive, "services rendered by financial institutions in issuing or managing payment cards or other similar documents" will no longer qualify for the right of option allowed for financial and banking transactions.

The purpose of this exclusion from the right of option is to avoid any further disparities in the tax treatment of such transactions, particularly as regards the supply of services by the institution issuing the payment card to sellers of goods and services, by introducing an exemption in all Member States and thereby placing all taxable persons on an equal footing with regard to the non-deductibility of input tax charged on purchases connected with such transactions.

In the course of its work, the VAT Committee came out almost unanimously in favour of an exemption for services rendered by the issuer of the payment card to retailers on the basis of Article 13(B)(d), and in particular points 2 and 3, the main activity being essentially financial in nature. It transpired though that the right of option provided for in Article 13(C) could give rise to unavoidable distortions. Hence the proposal to exclude the services concerned from that right of option.

Since Italy continued to tax those transactions, the Commission, on 6 April 1987, instituted before the Court proceedings against that country under Article 169 of the Treaty.

c) Platinum nobles (Article 13(B)(d)(4))

Article 13(B)(d)(4) exempts transactions in respect of, among other things, coins used as legal tender, with the exception of collectors' items. It stipulates that "collectors' items" shall be taken to mean gold, silver or other metal coins or bank notes which are not normally used as legal tender or coins of numismatic interest;"

The question concerning the tax treatment of platinum nobles was raised for two reasons : they are recognized on the Isle of Man as legal tender, and they are recommended by banks as an investment and traded at a premium above the value of the pure metal. Since point 26 of Annex F cannot apply to such coins, the Commission departments felt they should be taxed immediately, irrespective of whether they were regarded as collectors' items (the conclusion to which the definition contained in Article 13 (B)(d)(4) leads) or as an investment medium. The deliberations of the VAT Committee endorsed this analysis.

C. Exemptions under Articles 14 and 15

a) Importation of official publications and importation of postage stamps

Difficulties have arisen concerning the importation of official publications and of unfranked postage stamps valid for use in their country of origin.

Some Member States take the view that Article 14 (1)(g) of the Sixth Directive does not make express provision for the exemption of official publications. A number of Member States also justify the taxation on importation of postage stamps valid for use for postal services in their country of origin on the ground that supplies of these stamps within the importing country cannot qualify for the exemption provided for in Article 13(B)(e) and that, accordingly, the exemption on importation provided for in Article 14(1)(a) would not be applicable.

The Commission considers that importation of official publications involves an exercise of official authority on the part of the institutions of the country of origin; as regards importation of the postage stamps mentioned above, it takes the view that to impose tax on them is likely to create discrimination in relation to supplies of stamps having the same function within the importing country, i.e. stamps issued by the postal authorities of that country and supplied direct by them.

The proposal for a Nineteenth Directive thus inserted two specific provisions into Article 14 that were aimed at expressly exempting the transactions in question. However, for reasons of expediency, these provisions were subsequently transferred to the proposal amending for the third time Directive 83/181/EEC determining the scope of Article (1)(d) of the Sixth Directive as regards exemption from VAT on the final importation of certain goods.

b) Vessels intended for breaking up

It emerged from the work of the VAT Committee that most Member States exempted supplies of sea-going vessels intended for breaking up, either under a broad interpretation of Article 15 or under other provisions of the Directive.

In order to remove this legal uncertainty, the Commission included in the proposal for a Nineteenth Directive two provisions incorporating into Article 15 two exemptions for vessels and aircraft intended for breaking up.

c) Interpretation of Articles 14(1)(i) and 15(13) as regards services in connection with goods transport

The question was raised as to whether the exemption, e.g. of transport, provided for in Article 14(1)(i) was applicable only where the importation of goods to which the transport related was effectively taxed or whether it was also applicable where goods were definitively imported with no VAT being charged (e.g. goods forming part of a removal operation).

The Commission departments consider that Article 14(1)(i) should apply only in the case where transport involves goods subject to VAT on importation. This provision is designed to avoid double taxation of certain services such as transport that would be taxed once in accordance with the territoriality rules laid down in Article 9 and then again pursuant to Article 11(B)(3)(b) by virtue of their inclusion in the taxable amount for the importation of goods.

The same logic should apply to Article 15(13) in regard to transport services linked to the exportation of goods. Accordingly, in order to be fully consistent, transport services rendered in the country of departure in the event of removal should also be taxed. However, as things stand, there would not seem to be any legal basis on which to tax transport carried out in the country of departure since Article 15(13) exempts the supply of transport services directly linked to the export of goods. Furthermore, on the basis of Article 9(2)(b), transport is taxed in each country concerned on the basis of the distances covered. Combined application of these two Articles means that the transport of goods exempt on importation would be taxed only in respect of the portion of the journey undertaken in the country of importation. This creates an inconsistency in relation to the treatment of the transport of goods taxed on importation.

At present, a very large majority of Member States exempt from taxation the portion of the journey undertaken in the country of departure for the purposes of an international removal of goods. In other words, Member States take Article 15(13) to mean that all transport services linked to the export of goods are exempt even where there is no remission of tax on goods leaving the country.

As for the situation in the importing country, most Member States, in line with the interpretation placed on Article 14(1)(i), exempt the portion of the journey undertaken there.

A majority of the Member States would be prepared, in the context of future harmonization, to alter the present arrangements so that the entire journey undertaken for the purposes of an intra-Community removal operation was taxed in the country of departure. This would ensure consistency with the taxation of passenger transport provided for in Article 28(5) of the Sixth Directive and in the proposal for a Directive now being drawn up.

However, it must be borne in mind that this solution, which can be applied without difficulty after 1992, would currently pose problems of application given that, at the time of departure, it is not possible to know with certainty if the transported goods will actually be exempted at importation.

CHAPTER VI

Questions of interpretation concerning deductions (Articles 17 to 20)

A. System of deductions

1. The Council Decision of 23 October 1984 authorizes France, pursuant to Article 27 of the Sixth Directive, to apply in respect of automatic gaming machines a measure derogating from Article 18 of that Directive. It stipulates that, for a period of four years, France need not refund in this connection any deductible tax credit but may provide for it to be set against tax due in subsequent tax periods. It further provides that the derogation does not apply to automatic gaming machines the receipts of which can be established with certainty.

France has failed to incorporate a four-year deadline into its legislation and applies a general derogation that would not permit any exception. Proceedings have been instituted under Article 169 of the Treaty.

2. Articles 17 to 20 of the Sixth Directive provide for full deduction of input taxes on goods and services used for taxed transactions.

French legislation appears to have departed from that principle by stipulating that undertakings are entitled to deduct, annually and for a period of fifteen years, only a fraction of the VAT charged on the purchase or construction of buildings if the annual income from letting is less than one fifteenth of the value of the buildings.

In this connection, an action was brought before the Court on 18 February 1987 under Article 169 of the Treaty.

3. As provided for in Article 17(7) of the Sixth Directive, Italy consulted the VAT Committee twice on the exclusion for cyclical economic reasons - up to 31 December 1985 in the first instance and then, following an extension, up to 31 December 1987 - of the right to deduct VAT in respect of the purchase or importation of motor vehicles of not more than 2000 cc (2500 cc where fitted with a diesel engine) and the purchase of fuels and lubricants for use therein.

B. Refund of VAT to taxable persons not established in the territory of the country

1. The aim of the Eighth Council Directive of 6 December 1979 (1) is to harmonize the arrangements for the refund of VAT to foreign taxable persons who are residents of the Community.

All the Member States - with the exception of Portugal (2), which is still treated as a non-member country for the purposes of this Directive - currently apply the refund procedure provided for in the Eighth Directive.

A report on the application of the Directive - drawn up in accordance with Article 12 - was transmitted to the Council in November 1985 (3). It discussed the functioning of the refund procedure and emphasized the difficulties encountered in obtaining tax refunds from the tax authorities in certain Member States.

In its conclusions, the report nevertheless stated that the refund procedure was operating in a fairly satisfactory manner in most Member States but that improvements were needed in those areas where obstacles, often of an administrative nature, still seemed to prevent the procedure from operating smoothly.

It also pointed out, however, that the common refund system remained incomplete in the absence of any Community provisions determining the items of expenditure not eligible for deduction of tax and laying down arrangements for the refund of tax to taxable persons established in third countries. More recently, the proposal for a Thirteenth Directive was adopted on 17 November 1986 (4). However, the Council has not yet reached agreement on the proposal for a Twelfth Directive, which contains a Community list of items of expenditure not eligible for deduction of tax.

(1) OJ n°L 331 of 27 December 1979, p. 11

(2) Since 1 January 1988 Portugal has introduced into its legislation the refund procedure envisaged in the 8th Directive

(3) COM(85)584 final

(4) OJ n°L 326 of 21 November 1986, p. 40

As a result, the exclusions from the right to deduct tax or from the right of refund in the case of taxable persons not established in the territory of the country still vary significantly and the drawbacks inherent in this lack of harmonization remain. The Commission would very much like the Council to act at last on this proposal, the harmonization of such exclusions also being essential in the context of removal of tax frontiers planned for 1992.

2. Finally, the report referred to certain difficulties encountered in obtaining tax refunds, particularly from the Italian tax authorities. For one thing, it took an abnormally long time to obtain refunds and, for another, the Italian authorities required foreign taxable persons to open bank accounts in Italy - a requirement not envisaged in the Eighth Directive.

The Commission's staff have approached the authorities in Italy on a number of occasions to urge them to settle outstanding refund claims. In view of the fact that refunds are frequently made quite some time after the six-month deadline laid down in the Eighth Directive and although that deadline has been incorporated into Italian legislation, the Commission decided to initiate proceedings against Italy under Article 169 of the Treaty.

More recently, the Italian authorities have let it be known that a new decree is to be adopted which will enable foreign taxable persons to obtain VAT refunds by way of direct payments to accounts opened in their country of residence. This decree should remove if not all the difficulties encountered by foreign taxable persons, then at least those stemming from the requirement that they open accounts in Italy. This information was furnished by Italy in response to the Commission's reasoned opinion.

The problems of delay in obtaining refunds have not however yet been resolved.

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CHAPTER VII.

Interpretation of Article 26 : Special regime for travel agents

A. Scope

Article 26 stipulates that Member States are to apply VAT to the operations of travel agents in accordance with its provisions where travel agents deal with customers in their own name and use the supplies and services of other taxable persons in the provision of travel facilities.

These two conditions, which must be met before Article 26 is applicable, viz. "where the travel agents deal in their own name" and "use the supplies and services of other taxable persons in the provision of travel facilities", have been the subject of questions regarding interpretation and of analyses carried out by the Commission departments.

With regards to the first condition, it has been argued that travel agents escape all liability in providing travel facilities and that it can therefore be concluded that they act almost always in the name of another party. This argument would not only render Article 26 inoperative but would also seem to be contradicted by practice. There are, in fact, many cases where the travel agent sells a package without the traveller needing to know who provided the various services. In such cases, the traveller deals solely with the travel agent, who makes out a bill or invoice in his own name. In this situation, the travel agent can be regarded as acting in his own name, regardless of who ultimately assumes the risk of the contract being improperly executed.

To be applicable, Article 26 also requires the travel agent to "use the supplies and services of other taxable persons in the provision of travel facilities". This second condition, which defines the scope of the first, was also examined to establish, firstly, whether this wording should be interpreted as requiring the use by the travel agent of several services of other taxable persons and, secondly, how the term "travel" should be defined. The VAT Committee felt that the use of at least one service supplied by another taxable person in respect of a journey was sufficient for the purposes of Article 26.

B. Calculation of the margin

- Block booking

Current practice in the travel agency and tour operator sector does not always permit strict application of Article 26(2) relating to the calculation of the travel agent's margin. Where, for example, a travel agent makes block bookings of hotel accommodation or airline tickets which he then supplies to different travellers, it is difficult to calculate the margin in relation to any given trip, since the "cost borne by the travel agent" covers all the block bookings for the season. When consulted on this question, the VAT Committee took the view that the method of calculation provided for in Article 26 did not preclude determination of the margin not for each transaction but for all transactions on the basis of the same formula during a specific period.

- Transactions to be regarded as for the direct benefit of the traveller

The question arose as to whether certain costs borne by the travel agent in providing travel facilities should be regarded as transactions which are "for the direct benefit of the traveller". The case in question was the following : a tour operator established in a Member State sells among other things, tours undertaken in that Member State. To sell those tours to tourists from other Member States, the operator uses the services of travel agents based there, paying them a percentage of the price of each tour sold. Should the agent's commission, which is taxed in the country in which he is established, be regarded as a transaction for the direct benefit of the traveller and be deducted, for the purpose of calculating the margin, from the total amount to be paid by that traveller, thereby reducing the taxable margin by a corresponding amount ? If not, should that tax be refunded to him on the basis of the Eighth Directive ?

Article 26(2) stipulates that the taxable margin is the difference between the total amount to be paid by the traveller, exclusive of VAT, and the actual cost to the travel agent of supplies and services provided by other taxable persons where these transactions are for the direct benefit of the traveller. Only a broad interpretation of Article 26 could, therefore, lend support to the view that the services rendered by an agency to a tour operator in prospecting for potential customers are for the direct benefit of the traveller and are accordingly to be deducted from the taxable amount.

Consulted on this matter, a majority of the Committee took the view that the agency's remuneration was not to be deducted for the purpose of calculating the tour operator's margin. Furthermore, it was not necessary to apply the Eighth Directive in this case, since the remuneration has to be exempted under Article 15(14).

- Package which includes a transaction carried out directly by the travel agent

The Committee considered that, where travel packages include amounts representing a remuneration for transactions in respect of which agents are to be taxed separately in another Member State (as hotel owners, for example), such amounts should not be taken into account in determining the margin.

C. Other problems relating to the application of Article 26

The VAT Committee also examined two special cases involving the application of Article 26 : the hiring of villas, and the organization of language-study trips.

D. Current proceedings under Article 169

Proceedings were instituted under Article 169 against three Member States in respect of the application of Article 26. They were concerned with :

- Failure to apply Article 16(2) (charging VAT on all supplies and not on the margin) and taxation of agencies which have neither their head office nor a permanent establishment within the territory of the Member State concerned;

- exemption of services supplied by travel agents in respect of transactions in Spain;
- the arrangements for the commission paid by a tour operator to travel agents in other Member States.

This last question was examined by the VAT Committee (see point B above : calculation of the margin - transactions to be regarded as for the direct benefit of the traveller).

PART III

DIRECTIVES PROPOSED OR ADOPTED ON THE BASIS OF THE SIXTH DIRECTIVE

A number of articles in the Sixth Directive provide that the Commission will lay before the Council proposals for resolving certain matters left in abeyance or for clarifying the implementing arrangements for certain provisions.

The First Report mentioned the proposals that were being drawn up or examined by the Council at the time of its publication. In the meantime, some of them have been transmitted to the Council while others have already been adopted. This part of the report will, therefore, look at how the situation has evolved in the period since publication of the First Report.

In the interests of clarity, the different proposals for directives have been divided into three categories :

1. Directives determining the scope of certain exemptions in respect of international transactions;
2. Directives aimed at abolishing double taxation;
3. Other directives amending or supplementing the Sixth Directive.

CHAPTER I

Directives determining the scope of certain exemptions in respect of international transactions

A number of directives have been adopted as regards exemptions in respect of international transactions. Some of them have been amended or are at present the subject of proposals for amendments.

1. Directive determining the scope of Article 14(1)(d)

In determining the scope of Article 14(1)(d) as regards exemption from VAT on the final importation of certain goods, the Directive (1), adopted on 28 March 1983, is closely linked to the Community arrangements for exemptions from customs duties instituted by Council Regulation (EEC) n°918/83 (2). It grants exemptions notably in respect of the importation of goods by persons moving from a third country, the importation of goods acquired by inheritance, school outfits, scholastic materials and other scholastic effects, and capital goods and other equipment imported on the transfer of activities. It was amended in 1985, with the quantity of fuel admitted tax-free in standard fuel tanks of passenger transport vehicles travelling within the Community being raised from 200 to 600 litres (3). A proposal was sent to the Council on 10 July 1986 likewise with a view to raising to 600 litres the quantity of fuel that could be admitted tax-free in fuel tanks of commercial motor vehicles which make trips between Member States for the carriage of goods (4). A proposal for a Directive (5) amending for the third time Directive 83/181/EEC was transmitted to the Council on 9 February 1987 in order to take account, among other things, of certain amendments to Regulation (EEC) n°918/83.

(1) Directive 83/181/EEC; OJ n°L 105 of 23 April 1983, p. 38

(2) OJ n°L 105 of 23 April 1983, p. 1

(3) Directive 85/346/EEC; OJ n°L 183 of 16 July 1985

(4) OJ n°C 183 of 22 July 1986, p. 8

(5) OJ n°C 53 of 28 February 1987, p. 9

2. Directive on tax exemptions within the Community for certain means of transport temporarily imported into one Member State from another

The purpose of this Directive, which was also adopted on 28 March 1983, is to eliminate the obstacles to the free movement of vehicles registered in a particular Member State (1). It failed though to tackle a number of constraints that individuals in the Community find difficult to accept. In order to improve the situation while, at the same time, responding to the conclusions of the Fontainebleau European Council and of the Adonnino Committee, the Commission on 4 February 1987 proposed amendments to the Directive in the following areas : re-hire of private vehicles, extension of the period of temporary importation in the case of business ties in another Member State, extension of the exemption to persons other than the person who has temporarily imported the vehicle, company cars, students (2), immobilization abroad, short-term hire, private vehicles which have been irretrievably damaged, infringements and sanctions, and arbitration. The proposed amendments are currently being examined within the Council.

3. Directive on tax exemptions applicable to permanent imports from a Member State of the personal property of individuals

This Directive (3), adopted on 28 March 1983, concerns, among other things, the importation of personal property :

- i) in connection with a transfer of residence from one Member State to another;
- ii) on marriage;
- iii) acquired by inheritance and
- iv) in connection with the furnishing of a secondary residence

When adopting the Directive, the Council undertook to adopt before 1 January 1986 provisions permitting a substantial relaxation of the formalities relating to the granting of the tax exemptions agreed on. A proposal along these lines (4), which is also in keeping with the conclusions of the ad hoc Committee on a People's Europe and with the White Paper action programme, was sent to the Council on 16 December 1986.

(1) Directive 83/182/EEC; OJ n°L 105 of 23 April 1983, p. 59

(2) The amendments are designed to clarify the previous text, in line with the judgment by the Court of Justice in Case 249/84 Profant

(3) Directive 83/183/EEC; OJ n°L 105 of 23 April 1983, p. 64

(4) OJ n°C 5 of 9 January 1987, p. 2

The proposal is designed to incorporate improvements as regards the periods of use prescribed by the Directive, certain obligations subsequent to importation, quantitative limits on certain goods subject to excise duties, the inventory of goods, proof of former residence, removals involving a number of operations, secondary residences, and presents given on the occasion of a marriage. It is currently under examination within the Council.

4. Seventeenth Directive concerning exemption from VAT on the temporary importation of goods other than means of transport

On the basis of Article 14(1)(c) of the Sixth Directive, this Directive, which was adopted by the Council on 16 July 1985, concerns the "importation of goods declared to be under temporary importation arrangements, which thereby qualify for exemption from customs duties, or which would so qualify if they were imported from a third country" (1). It covers, therefore, a wide range of goods that will now qualify for exemption when temporarily imported for a period of less than twenty-four months and provided they remain the property of a person established outside the Member State of importation.

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(1) OJ n° L 192 of 24 July 1985, p. 10

CHAPTER II

Directives aimed at abolishing double taxation

A. Taxable persons : Seventh Directive

This proposal for a Directive, which was sent to the Council on 11 January 1978 and amended in May 1979, sets out to establish a common system of value added tax to be applied to works of art, collector's items, antiques and used goods sold by taxable persons; the aim being to abolish any residual tax in intra-Community trade.

The First Report underscored the serious consequences from the jurisdictional point of view as well as for competition and tax harmonization that failure to agree on the proposal would have. In it, the Commission urged the Council to take a decision soon.

Budgetary obstacles in some Member States and political obstacles in others applying more favourable arrangements, notably to works of art, have so far prevented the proposal from being adopted (1).

B. Individuals : Sixteenth Directive

The proposal for a Sixteenth Directive, sent to the Council on 23 July 1984 (2) and amended on 25 March 1984 (3), is designed to do away with double taxation in the case of used or second-hand goods on which VAT has been finally paid and thereby to abolish the cases of double taxation still existing in intra-Community trade.

(1) The Commission withdrew this proposal on 11 November 1987. It plans to send a new proposal to the Council shortly.

(2) OJ L²⁶ 226 of 23 August 1984, p. 2.

(3) COM(86)163 final

The Commission amended its proposal extensively in line with Parliament's wish that its scope be widened and procedures simplified. The amended proposal provides for general exemption arrangements applicable to imports by individuals of goods on which Community VAT has been charged, except in exceptional cases that are spelt out (goods deemed to be new, valuable goods and vehicles not more than four years old). Frontier compensation arrangements are proposed for such goods, which are excluded from the exemption arrangements.

The proposal takes account of the judgment given by the Court of Justice on 5 May 1982 in case 15/81 Gaston Schul, which was referred to in the First Report (1).

Since then, other judgments by the Court have clarified, in line with the broad interpretation placed on it by the Commission, the principles set out in the first judgment :

- Case 134/83

In its judgment of 11 December 1984 in Case 134/83 Abbink (2), the Court ruled that the present stage of Community harmonization did not preclude a Member State from prohibiting one of its residents to use on its territory motor vehicles admitted under temporary importation arrangements. It has made it clear though that, if that Member State claimed VAT on such a vehicle, taxation must take place having due regard to the principles laid down in the Gaston Schul judgment;

- Case 47/84

In its judgment of 21 May 1985 in Case 47/84 Gaston Schul (3), the Court ruled that VAT charged by a Member State on the importation from another Member State of goods supplied by a private person when VAT was not charged on the supply by a private person within the territory of the Member State of importation must be calculated in such a way as to take account of the VAT paid in the Member State of exportation and still included in the value of the product on importation.

(1) See page 75 of the First Report

(2) [1984] ECR 4097

(3) Not yet published; OJ n°C 144 of 13 June 1985, p. 4

Again according to this judgment, that amount is equal, in cases in which the value of the goods has decreased between the date on which VAT was last charged in the Member State of exportation and the date of importation, to the amount of VAT actually paid in the Member State of exportation, less a percentage representing the proportion by which the goods have depreciated; in cases in which the value of the goods has increased over that same period, it is equal to the full amount of the VAT actually paid in the Member State of exportation;

- Case 39/85

In its judgment of 23 January 1986 in Case 39/85 (1) the Court ruled that "for the purposes of applying Article 95 of the EEC Treaty where value added tax is levied on the importation of goods by a non-taxable person, no distinction should be made according to whether or not the transaction giving rise to the importation was effected for valuable consideration".

The Commission published in the Official Journal of the European Communities on 21 January 1986 (2) a communication about the Court's decisions of 5 May 1982 and 21 May 1985 (the Gaston Schul cases). In it, the Commission set out the conclusion which it had drawn from these cases and drew the public's attention to its policy in this matter. It also stressed that it was watching with particular attention to ensure that the Court's decisions in this field were applied by national administrations.

This ruling, derived from Article 95 of the Treaty, was not immediately implemented in most Member States and has still not been fully applied in some of them. Accordingly, the Commission has been obliged to initiate a certain number of procedures under Article 169.

(1) Not yet published in the European Court Reports;

OJ n° 77 of 5 April 1986, p. 8

(2) OJ n° 13 of 21 January 1986, p. 2

CHAPTER III

Other directives amending or supplementing the Sixth Directive

A. Directives adopted

1. Tenth Directive of 31 July 1984 : Application of VAT to the hiring out of movable tangible property.

As indicated in the previous chapter (Part II, Chapter III), the Tenth Directive (1) is intended to preclude non-taxation in the case of the hiring out of movable tangible property by providing that the place of taxation for such transactions is the Member State in which the customer is established. In accordance with the general principle laid down in Article 9(1), the means of transport excluded from the scope of the Directive are still to be taxed at the place at which the supplier is established.

2. Thirteenth Directive of 17 November 1986 : Refund of VAT to taxable persons in third countries (2)

Pursuant to this Directive, the principle of VAT refunds for taxable persons not established in the territory of the Community will become compulsory as from 1 January 1988. Member States will, however, still be free to determine the arrangements for submitting applications and for making refunds, although the latter may not be granted under conditions more favourable than those applied to Community taxable persons. In addition, Member States will be able to make refunds conditional on observance of the principle of reciprocity.

The proposal, which was sent to the Council on 19 July 1982 and amended in July 1983, was adopted only after lengthy discussions within the Council made necessary in particular by the fact that no agreement could be reached on a list of items of expenditure not eligible for a refund.

(1) OJ n°L 208 of 3 August 1984, p. 58

(2) OJ n°L 326 of 21 November 1986, p. 40

B. Proposals before the Council

1. Proposal for a Twelfth Directive on expenditure not eligible for deduction of VAT

This proposal, which was laid before the Council on 25 January 1983 (1) and amended on 20 February 1984 (2) has not yet been adopted by the Council. Some delegations feel that the exclusions provided for are too wide-ranging, while others are opposed to its very purpose in spite of the mandatory nature of Article 17(6) of the Sixth Directive.

2. Proposal for an Eighteenth Directive on the abolition of certain derogations provided for in Article 28(3) of the Sixth Directive

On 4 December 1984 the Commission sent to the Council a proposal for an Eighteenth VAT Directive on the abolition of certain derogations provided for in Article 28(3) of Directive 77/388/EEC (3).

The Economic and Social Committee endorsed the proposal on 3 July 1985 (4). While Parliament, which is amenable to the principle underlying the proposal, put forward a number of amendments in its opinion dated 6 April 1987 (5). In essence, the amendments consist of changes to the proposed timetable for abolishing the derogations and of the inclusion in the proposal of a number of derogations that Parliament feels should be discontinued with a view to the removal of tax frontiers by 31 December 1992.

(1) OJ n°C 37 of 10 February 1983, p. 8
(2) OJ n°C 56 of 29 February 1984, p. 7
(3) OJ n°C 347 of 29 December 1984, p. 3
(4) OJ n°C 218 of 29 August 1985, p. 11
(5) OJ n°C 125 of 11 May 1987, p. 15

Parliament also sought to retain the derogation provided for in Article 28(3)(e) given the lack of progress in adopting Community arrangements for works of art, collector's items, antiques and used goods.

The Commission incorporated most of the amendments sought into its amending proposal, which was transmitted to the Council on 25 June 1987 (1). As regards abolition of the derogation for transactions in gold other than gold for industrial use, the Commission, following the objections raised by Parliament, concluded that this question should be re-examined in greater depth. This derogation was, therefore, retained for the time being.

All the derogations will, in any event, have to be discontinued with a view to the removal of tax from lease by 31 December 1992.

3. Proposal for a Nineteenth Directive amending and making certain improvements to the common system of VAT

On 5 December 1984 the Commission transmitted to the Council its proposal for a Nineteenth Directive on the harmonization of the laws of the Member States relating to turnover taxes, amending Directive 77/388/EEC - common system of value added tax (2).

The Economic and Social Committee and Parliament endorsed the proposal on 3 July 1985 (3) and 6 April 1987 (4) respectively, subject to a number of amendments.

In its amending proposal, sent to the Council on 4 July 1987 (5), the Commission included one amendment that had been proposed by both the institutions consulted with a view to deleting from the text of the proposal the exemption provisions applying to artistic output, that is to say, deliveries of works of art by the artist who created them as well as the services of theatrical artists, authors, composers and writers. Accordingly, all these activities will, in principle, remain liable to VAT.

(1) COM(87)272 final

(2) OJ n°C 347 of 29 December 1984, p. 5

(3) OJ n°C 218 of 29 August 1985, p. 12

(4) OJ n°C 125 of 11 May 1987, p. 15

(5) COM(87)315 final

With regard to authors, artists and performers of works of art, the Commission agreed, by way of compromise, to retain the present text of point 2 in Annex F of the Sixth Directive, which allows a transitional derogation from the principle of taxation.

4. Proposal for a Directive on the special scheme applicable to small and medium-sized businesses

On the basis of the report it sent to the Council in November 1983 (1), the Commission proposed to the Council on 9 October 1986 a Directive aimed at simplifying and relaxing the arrangements for small and medium-sized businesses (2).

The proposal deals with two particular points, viz. the exemption arrangements and a simplified scheme.

The exemption arrangements provide for a compulsory exemption fixed at 10 000 ECU and an optional exemption of 35 000 ECU.

The proposal also allows small businesses likely to qualify for the exemption arrangements to opt for the simplified scheme.

The simplified scheme is concerned with the accounting procedures for small and medium-sized businesses with an annual turnover of less than 150 000 ECU. It includes simplification measures having a bearing on the chargeable event and the right to deduct, which it brings more closely into line with commercial practices regarding the charging of the price and the payment of suppliers, and on the frequency of returns, which are to be sent in annually with advance payments being made.

Under the simplified scheme, Member States may also introduce, for certain groups of taxable persons whose purchases are sufficiently homogenous in relation to their turnover, flat-rate percentages for calculating deductible VAT as a proportion of their turnover.

(1) COM(83)748 final

(2) OJ n°C 272 of 28 October 1986, p. 10

Member States may, however, retain the special schemes for small and medium-sized businesses in accordance with Article 14 provided these are more favourable than the proposed scheme and provided Member States receive Council authorization in accordance with a prescribed consultation procedure.

CONCLUSION

During the period covered by this report, the Commission has pressed ahead with its efforts to establish a more uniform VAT system.

Within the framework of the directives already adopted, the work of the VAT Committee has made for some measure of agreement on a number of matters relating in particular to the interpretation of the Sixth Directive and, as a result, has led to the adoption of majority guidelines on provisions as important as those concerning liability to tax in respect of certain services, the place of taxation for supplies of services, the taxable amount, the treatment of subsidies, exemptions, and the special scheme for travel agents.

The VAT Committee has also been consulted on a number of occasions by Member States under Article 29(4) of the Sixth Directive seeking derogations from certain provisions of that Directive relating in particular to the single-taxable-entity concept, exclusion from the right to deduct input tax for cyclical economic reasons, and the simplified scheme for small businesses.

The Commission is pleased to note that the number of such consultations has fallen appreciably compared with the period covered by the First Report. However, it takes the view that the work of the VAT Committee on the interpretation of Community VAT provisions should be stepped up in order to further promote the process of harmonizing the VAT base.

The Article 27 procedure, under which Member States may introduce special measures derogating from the Sixth Directive in order to simplify the procedure for charging VAT or to prevent certain types of tax evasion or avoidance, has been invoked as often as during the preceding period. Although some of the new measures authorized under this procedure have been limited over time, they still add to the number of derogations from the common VAT system. Consequently, the Commission would like to see Member States invoking this procedure less frequently, its preference being for a Community approach to resolving problems encountered by them.

A series of rulings given in accordance with Articles 169 and 177 of the Treaty have supplemented the case law established by the Court of Justice and have placed a Community interpretation on the instruments concerned, thereby helping to eliminate disparities due to the divergent application of the common VAT system.

The Commission is convinced that the divergences in implementation due to differing interpretations of the relevant Community instruments will be gradually remedied, in particular by pursuing and even intensifying the dialogue with Member States. However, it also firmly believes that the other divergences in implementation stemming, among other things, from the derogations provided for in the Sixth Directive should be eliminated in preparation for the dismantling of tax frontiers.

In addition, the Commission notes that some progress has been made towards harmonization through the adoption of a number of directives by the Council. These concern in particular the place of supply for the hiring out of movable tangible property, VAT refunds to taxable persons in third countries and certain exemptions on importation. Other proposals aimed at clarifying the provisions of the Sixth Directive, at abolishing derogations or at laying down a Community scheme for small and medium-sized businesses have in turn been sent to the Council, which has not yet acted on them. Aware of their importance for the objective to be achieved, the Commission has intentionally included them in its White Paper action programme for completing the internal market alongside the specific measures to be taken in the run-up to 1992.

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Since completion of this report, new proposals were presented to the Council on 7 August 1987. These proposals, along with those already being examined, set out all the measures which must be successfully implemented if the conditions necessary for completion of the internal market are to be met.

As regards VAT, the following proposals have been made :

- a proposal concerning the approximation of rates (1);
- a proposal instituting a process of convergence of rates (1)
- a proposal supplementing the common system of value added tax and amending the Sixth Directive (2).

A working document sent to the Council on the same date provides for the introduction of a VAT clearing mechanism for intra-Community sales (3). This mechanism is intended to ensure that Member States continue to receive the revenue to which they are entitled.

(1) OJ n°C 250 of 18 September 1987, p. 2 and 3

(2) OJ n°C 252 of 12 September 1987, p. 7

(3) COM(87)323 final 2

The proposal for a Directive on the VAT arrangements applicable to the transport of persons which was also provided for in the White Paper action programme, will be sent to the Council at a later date.

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The Commission takes the view that closer alignment of indirect tax rates, especially VAT rates, is a necessary prerequisite for dismantling internal frontiers within the Community and for establishing a Community-wide market that will operate as a genuine national market. It would stress that these objectives can, however, be achieved only if the proposals for Directives sent by it to the Council in August 1987 under its White Paper action programme for completing the internal market are adopted. It expects, therefore, to receive the support of all the Community institutions for the successful performance of this task, which is in response to the policy decisions taken by the Heads of State or Government of the Member States and to the ratification by national parliaments of the Single European Act, which entered into force on 1 July 1987.

Judgments delivered by the Court of Justice
up to 31 December 1988

Although the second report on the application of the Sixth VAT Directive covers only the period up to 30 June 1987, the Commission feels that it would be expedient to attach this brief summary of the recent judgments by the Court of Justice that have a bearing on the report.

In its judgment of 4 February 1988 in the Case 391/85 (1), the Court ruled that, by in practice retaining, under the Law of 31 July 1984, the list price as the basis for the taxation of new saloon cars and estate cars, the Kingdom of Belgium had failed to take the measures necessary to comply with the Court's judgment of 10 April 1984 (see pages 10 and 26 of the report).

In its judgment of 23 February 1988 in Case 353/85 (2), the Court held that, by exempting from VAT supplies of goods (e.g. corrective spectacles made by registered opticians) unless such goods were supplied as an integral part and included in the price of the service, the United Kingdom had failed to fulfil its obligations under Article 13(A)(1)(c) of the Sixth Directive (see page 32 of the report).

(1) O.J. No. C 63 of 8 March 1988, p. 5

(2) O.J. No. C 74 of 22 March 1988, p. 6

In its judgment of 25 February 1988 in Case 299/86 (reference for a preliminary ruling)(3), the Court made it clear that the Gaston Schul and ensuing judgments laid down the general principle that an individual should not have to suffer double taxation and were, therefore, also applicable even where goods had been acquired from a taxable person. It ruled that Article 95 of the EEC Treaty must be interpreted as meaning that, upon the importation of goods from another Member State by an individual which had not qualified for relief on exportation or for tax exemption in the importing Member State, the VAT charged on importation must take into account the residual amount of VAT paid in the exporting Member State and still included in the value of the goods at the time of importation, so as to ensure that the residual amount of such tax was not included in the basis of assessment and was deducted from the VAT payable upon importation (see pages 51 and 52 of the report).

As regards penalties, the Court also made the point that imports must be accorded the same treatment as similar transactions within the territory of the country and that, accordingly, national legislation which penalized more severely offences involving payment of VAT on domestic transactions was incompatible with Article 95 of the EEC Treaty in so far as that difference was disproportionate to the difference between the two categories of offences.

In its judgment of 3 March 1988 in Case 252/86 (reference for a preliminary ruling) (4), the Court held that Article 33 of the Sixth Directive was to be interpreted as meaning that, as from the introduction of the common system of VAT, Member States were no longer entitled to impose on the supply of goods, the provision of services or imports liable to VAT taxes, duties or charges which could be characterized as turnover taxes but that a charge which, although providing for different amounts according to the characteristics of the taxed article, is assessed exclusively on the basis of the placing thereof at the disposal of the public, without in fact taking account of the income which could be earned thereby, may not be regarded as a charge which can be characterized as a turnover tax.

(3) O.J. No. C 74 of 22.3.1988, p. 13

(4) O.J. No. C 78 of 25.3.1988, p. 4

In its judgment of 8 March 1988 in Case 102/86 (reference for a preliminary ruling) (5), the Court held that the exercise by the Apple and Pear development Council of its functions pursuant to Article 3 of the Apple and Pear Development Council Order 1980, S.I. No 623 (as amended by the Apple and Pear Development Council (Amendment) Order 1980, S.I. No 2001) and the imposition on growers pursuant to Article 9(1) of an annual charge for the purpose of enabling the Development Council to meet administrative and other expenses incurred or to be incurred in the exercise of such functions did not constitute "the supply of services effected for consideration" within the meaning of Article 2 of the Sixth Directive (see page 17 of the report).

In its judgment of 8 March 1988 in Case 165/86 (reference for a preliminary ruling) (6), the Court ruled that, where an employer who was subject to the rules on VAT, by agreement with one of his employees and another taxable person (a supplier), had goods supplied at his own expense to that employee who used them exclusively for the purposes of the employer's business and the employer received from the supplier invoices for those goods charging VAT on them, the provisions of Article 11(1)(a) of the Second Directive and of Article 17(2)(a) of the Sixth Directive must be interpreted as meaning that the employer could deduct the VAT thus charged to him from the VAT which he was liable to pay (see page 39 of the report).

In its judgment of 24 May 1988 in Case 122/87 (7), the Court ruled that, by exempting from VAT the services provided by veterinary surgeons in the exercise of their profession, the Italian Republic had failed to fulfil its obligations under the Sixth Directive (see pages 31 to 33 of the report).

(5) O.J. No. C 89 of 6 April 1988, p. 8

(6) O.J. No. C 90 of 7 April 1988, p. 5

(7) O.J. No. C 156 of 15 June 1988, p. 5

In its judgment of 21 June 1988 in Case 415/85 (8), the Court ruled that, by continuing to apply a zero rate of VAT to supplies of electricity included in item (xx)(a) of the Finance Act 1985 in so far as it was not supplied to final consumers, Ireland had contravened the provisions of the Sixth Directive.

In its judgement of 21 June 1988 in Case 416/85 (9), the Court held that, by continuing to apply a zero rate of VAT

- to supplies to industry of water and sewerage services (emptying of cesspools and septic tanks) including in Group 2 of Schedule 5 to the Value Added Tax Act 1983, in so far as they were not supplied to final consumers,
- to news services included in Group 6, in so far as they were not provided to final consumers,
- to supplies of fuel and power including in Group 7 and protective boots and helmets included in Group 17, in so far as they were not supplied to final consumers,
- to the provision of goods and services included in Group 8 in relation to the construction of industrial and commercial buildings and to community and civil engineering works, in so far as they were not provided to final consumers,

the United Kingdom had contravened the provisions of the Sixth Directive.

In a judgment of 21 June 1988 in Case 257/86 (10), the Court held that, by adopting and maintaining in force legislation under which exemption from VAT was not granted in respect of all imports of free samples of low value and which lacked clarity and precision with regard to the exemption of certain imports of such samples, the Italian Republic had failed to fulfil its obligations under Article 14 of the Sixth Directive (see pages 36 to 38 if the report).

(8) O.J. No. C 190 of 19 July 1988, p. 11

(9) O.J. No. C 190 of 19 July 1988, p. 11

(10) O.J. No. C 190 of 19 July 1988, p. 12

In its judgment of 28 June 1988 in Case 3/86 (11), the Court of Justice ruled that, by fixing in relation to VAT under the flat-rate scheme for farmers the flat-rate compensation percentages at 15 % and then 14 % for the beef, pigmeat and unconcentrated and unsugared fresh milk sectors from 1981 and 1983 respectively and by providing that flat-rate compensation percentages should apply to supplies and services intended for flat-rate farmers, the Italian Republic had failed to fulfil its obligations under the Treaty and Article 25(3), (5) and (8) of the Sixth Directive.

In its two judgments of 5 July 1988 in Cases 269/86 and 289/86 (references for preliminary rulings) (12), the Court ruled that Article 2 of the Sixth Directive had to be interpreted as meaning that no liability to VAT arose upon the unlawful supply of drugs effected for consideration within the country in so far as the products in question were not confined within economic channels strictly controlled by the competent authorities for use for medical and scientific purposes (see page 17 of the report).

In its judgment of 6 July 1988 in Case 127/86 (references for a preliminary ruling) (13), the Court ruled that the Sixth Directive prevented a Member State from levying VAT on a motor vehicle which was owned by an employer established in another Member State where VAT had been paid and which was used by a frontier-zone worker residing in the first Member State for the performance of his duties under his contract of employment and, secondarily, for leisure purposes (see pages 36 to 38 of the report).

(11) O.J. No. C 199 of 29 July 1988, p. 9

(12) O.J. No. C 211 of 11 August 1988, p. 4

(13) O.J. No. C 211 of 11 August 1988, p. 6

In its judgment of 12 July 1988 in Joined Cases 138 and 139/86 (reference for a preliminary ruling) (14), the court held that:

1. Article 27(1) of the Sixth Directive permitted the adoption of a measure derogating from the basic rule set out in Article 11 A.1(a) of that Directive even where the taxable person carried on business not with any intention of obtaining a tax advantage but for commercial reasons.
2. Article 27(1) of the Sixth Directive permitted the adoption of a derogating measure, such as that at issue in the main proceedings, which applied only to certain taxable persons amongst those selling goods to non-taxable resellers, on condition that the resultant difference in treatment was justified by objective circumstances (see page 11, point (b), of the report).

In its judgment of 14 July 1988 in Joined Cases 123/87 and 330/87 (reference for a preliminary ruling) (15), the Court ruled that Article 18(1)(a) and Article 22 (3) (a) and (b) of the Sixth Directive allowed Member States to make the exercise of the right to deduct dependent on the holding of an invoice which must contain certain particulars which were needed in order to secure the collection of VAT and the supervision thereof by the tax authorities. Such particulars must not, by reason of their number or technical nature, make it practically impossible or excessively difficult to actually exercise the right to deduct (see pages 39 and 40 of the report).

(14) O.J. No. C 205 of 6 August 1988, p. 5

(15) O.J. No. C 222 of 26 August 1988, p. 3

In its judgment of 21 September 1988 in Case 50/87 (16), the Court ruled that, by introducing and maintaining, in disregard of the provisions of the Sixth Directive, fiscal rules restricting the right of undertakings which let buildings that they had purchased or constructed to deduct the VAT paid on inputs where the return from those buildings was less than one fifteenth of their value, the French Republic had failed to fulfil its obligations under the Treaty (see page 39, point A 2, of the report).

On 27 October 1988, the Court removed from its register Case 103/87, Italy having amended its legislation so as to provide for exemption (see page 35, point (b), of the report).

(16) O.J. No. 269 of 18 October 1988, p. 8

