COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 16.3.2005
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2005/0019 (CNS)

Proposal for a

COUNCIL DIRECTIVE

amending Directive 77/388/EEC as regards certain measures to simplify the procedure for charging value added tax and to assist in countering tax evasion and avoidance, and repealing certain Decisions granting derogations

(presented by the Commission)

EXPLANATORY MEMORANDUM

Background

Under Article 27 of the Sixth VAT Directive, the Council, acting unanimously on a proposal from the Commission, may authorise any Member State to introduce special measures for derogation from the provisions of the Sixth VAT Directive, in order to simplify the procedure for charging the tax or to prevent certain types of tax evasion or avoidance.

Currently, Member States have been allowed to apply over 140 derogations. This number will grow in the near future, since Member States which joined the EU on the 1st of May 2004 are now introducing requests for derogations. In addition, in a relatively short timescale they will almost certainly come across other special measures in their legislation which will require a Community legal base.

In its communication of 7 June 2000 to the Council and the European Parliament on a strategy to improve the operation of the VAT system within the context of the internal market[1], the Commission undertook to rationalise some of the large number of derogations currently in force. The Commission's communication[2] of 20 October 2003, which reviewed and updated the strategy, reiterated this. It was envisaged that such a rationalisation would involve making certain individual derogations available to all Member States through an amendment to the Sixth VAT Directive[3]. These derogations would be those which had already proved themselves effective and which tackled problems which were shared by more than one Member State.

The number of derogations and the similar problems they tackle is indicative of the fact that in recent years VAT avoidance and fraud has become a very real issue. Both the national authorities of the Member States as well as business federations have pointed out that evading VAT has become so widespread in certain sectors that it puts honest traders under a competitive disadvantage. Charging VAT but not paying it over to the State results in not only a loss of revenue for the State but also enables dishonest traders to offer goods or services at lower prices than their compliant competitors.

In addition, Member States are more and more frequently confronted with artificial constructions – often involving a series of transactions - set up with the sole purpose of obtaining a VAT advantage either by lowering the final VAT charge or by increasing the recovery of VAT. While the artificial character of the chain of transactions is usually obvious, it is much more difficult to tackle them effectively or quickly from a legal point of view, especially since counter measures or court action inevitably take a long time. In the meantime, experience in Member States demonstrates that VAT avoidance schemes are worked out by specialists and successful ones subsequently marketed as a product to businesses. It is therefore questionable whether a piecemeal approach to tackling this problem where there is evidence of common problems is still appropriate.

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1 COM(2000) 348 final

2 COM(2003) 614 final

3 Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment (OJ L 145, 13.6.1977, p 1. Directive as last amended by Directive 2004/66/EC (OL L 168, 1.5.2004, p. 35)).

When Member States want to amend their national VAT legislation in order to counter these avoidance schemes, the question of the compatibility of the envisaged measures with Community law, and the Sixth VAT Directive in particular, arises. Especially in the area of avoidance, the mechanisms for artificially lowering the VAT charge are set up after a careful analysis of the strict wording of national VAT provisions and the Sixth VAT Directive. The principles of the common VAT system laid down in the Sixth VAT Directive seem designed first and foremost for genuine transactions. Very little, if anything, within the Sixth VAT Directive itself caters for cases where a taxable person tries to circumvent these principles. Only the abovementioned Article 27 provides a legal base whereby the Council, on the basis of an individual request from a Member State, can authorise the application of special measures which derogate from the normal rules. This, however, is a cumbersome route.

The Commission is therefore of the opinion that specific known schemes could be more effectively tackled through an amendment to the Directive to provide a permanent viable alternative to the standard treatment where it can be justified through evidence of avoidance or evasion activity.

The Proposal

The current proposal aims to amend the 6th Directive to provide Member States with the option of quickly adopting legally sound measures in order to counter avoidance and evasion in certain specific and targeted areas. This will not only be to the benefit of national treasuries but also to businesses who suffer from unfair competition because they do not wish to get involved in the setting up of avoidance schemes. In addition to measures to combat avoidance and evasion, the rationalisation proposal also includes some measures aimed at simplifying the application of the tax in certain circumstances where those liable to pay the tax are in financial difficulties. The rationalisation exercise, however, does not affect either specific measures designed to deal with a particular situation in a single Member State, or the ability of Member States to continue to request derogations under Article 27 of the Sixth Directive in the future where justified.

The material in the resultant proposal, therefore, introduces changes in some areas where there are proven difficulties with the operation of the sixth Directive and a demonstrable need to allow some limited flexibility more generally. In common with the derogations from which they spring, these measures represent an alternative to the normal rules and are only being made available to all Member States to help counter avoidance and evasion or to simplify the operation of the tax. The Commission is also of the view that in some areas, such as in relation to the taxation of waste and scrap material, it is preferable and more appropriate to have the permanency of an amended 6th Directive rather than being over-reliant on temporary derogations. To a large degree the proposed changes represent no more than a codification of what would, in any case, be available through a derogation under Article 27, and the proposed alternative treatments are similarly subject to the same restrictions. In addition, however, it does include an extension, in two areas, of a measure already found in the Directive (rather than in derogations) which has been of use to Member States in controlling the tax.

The measures (as befits legislation targeted towards specific problems) provide Member States with the option of using the alternative rule, rather than making their application mandatory. There is thus no obligation for a Member State to adopt the rule if there is no need for such a rule in that Member State. In addition, given the variety of mutations through which avoidance schemes pass in response to counter-measures, the proposal allows Member States some room to adapt the measures to their specific national situations. Thus, once

having opted to apply the rule, Member States are authorised to limit their application of the new rules in order to target their specific avoidance or evasion problem. Businesses, therefore, are not penalised by the mandatory application of inappropriate rules. Instead they should benefit from a selective, rather than a blanket, application which affects tax avoiders, not business generally. The Commission believes that this approach of setting the boundaries of the derogation and allowing flexibility of application within those boundaries is the most appropriate response to identified general problems which require individually tailored solutions.

Since one of the objectives of the proposal is to reduce the number of derogations, most particularly where there is duplication between Member States, the Directive also formally repeals a number of Council Decisions. Although a significant number of these have a limited life and would eventually run their course, some (for various reasons) are not time limited. Since the amended Directive 77/388/EEC will provide the legal base for the measures currently contained in the derogations, there is no need to confuse by maintaining a dual legal base. Accordingly, those derogations incorporated within the Directive will be repealed after a reasonable period for any necessary changes to be made to national legislation. The proposed time limit of a year will allow for any re-consultation with the VAT Committee, for example, that might be necessary and will also allow time for any necessary changes at national level to be completed.

The opportunity of this rationalisation is also being taken to formally identify derogations notified under article 27(5) of Directive 77/388/EC which are no longer used by the relevant Member State because they have lapsed or have been superseded. Since these derogations are defunct there is no need to repeal them through the proposed instrument.

An additional objective of the rationalisation is to improve transparency. This process started with amendments to Article 27 at the beginning of 2004, embodied in Directive 2004/7/EC. These eliminated the provision under which the Council was deemed to have tacitly approved a derogation if it did not object to the measure within two months of being notified. Under the revised procedure, the Commission has to respond to every request for special treatment introduced by a Member State either by presenting a proposal to the Council if the request is acceptable or by presenting its grounds for opposing the measure to the Council if it is not.

This objective has been further pursued as, linked to this proposal, the Commission has published a list on the TAXUD website giving references to all the measures which are still in force and which were authorised under Article 27(1) – (4) or notified under Article 27(5).

Specific contents

Article 1(1): Grouping and Article 1(2): Transfers of going concerns

Although not arising from existing derogations, in Article 1(1) and 1(2) the Commission is taking the opportunity to propose changes to strengthen areas which Member States find can be exploited to avoid VAT. In both the area of "grouping" in Article 4(4) of the Sixth Directive and in "transfers of going concerns" (Article 5(8)) the proposal allows for Member States to take steps to ensure that the operation of the rules does not allow an unfair result which would unjustifiably benefit or prejudice those concerned. Member States already have the discretion to set the circumstances in which the both of these rules can apply. The new rule, already applied to capital goods through Article 20(6), would help Member States prevent unfair results arising from the operation of the rules.

Article 1(3)(a): Deletion

This Article simply deletes the current definition of open market value in the 6th Directive, which only applies to Article 11(A)(1)(d). An amended definition is inserted later through the addition of new paragraph 8 to Article 11(A) in Article 1(3)(b) of the proposed Directive.

Article 1(3)(b): New Paragraph 5 - Investment Gold

Several Member States already apply a special measure on the basis of Article 27 to counter an arrangement which avoids the payment of VAT on untaxed investment gold used as a raw material for making consumer goods. It is now proposed to provide within the Sixth VAT Directive the means for all Member States to apply this measure. Article 1(3)(b) of the proposal introduces an optional rule derived from the existing derogations through the insertion of a new paragraph (5) to Article 11(A) of the 6th Directive.

Investment gold, held in the form of bars or wafers of a specified purity recognised by the bullion markets, or gold coins fulfilling the legal criteria, is exempt from VAT. When the gold is sold in a form in which it no longer qualifies as investment gold, VAT should be charged on the supply. This happens for example when a gold bar is worked into jewellery. The amount of tax payable can be minimised if a customer provides their own investment gold for working since the supply will only consist of the service of working the gold. Since there is no supply of the exempt gold, tax will not be accounted for even though it has lost its status as investment gold and it no longer qualifies for exemption. This is the abuse which the existing derogations seek to counteract. Similarly, where investment gold is provided by the customer and the jeweller works it into an item which also incorporates goods provided by the jeweller the value of the gold will not be included in the resultant supply of goods. This Article requires those working exempt gold to account for VAT on the value of the gold when it no longer qualifies as exempt gold.

Article 1(3)(b): New Paragraphs 6 – 8 Valuation of supplies

One of the vulnerable areas for avoidance relates to the valuation of supplies since that directly affects the amount of tax which is charged. The new paragraph (6) to Article 11(A) of the 6th Directive, to be found in Article 1(3)(b), introduces an optional rule which enables Member States to revalue certain supplies.

Since the valuation rule in Article 11 of the Sixth Directive is clear and forms one of the key tenets of the tax, any deviation needs to be carefully circumscribed. In particular, the proposals observe the principle that the tax authority should not interfere in the taxable value of a supply as a matter of course but only in specified circumstances, and even then not routinely. The Article therefore only allows re-valuation in the context of combating tax avoidance and evasion and in order to do so, a series of additional tests also need to be satisfied. The rule can only be applied when the parties are connected and that connection, rather than demonstrable commercial reasons, has led to a value other than the usual market value being placed on the supply. In addition re-valuation of a supply is only allowed in 3 circumstances: (in the case of an undervaluation) where VAT has been charged and the recipient of the supply is not entitled to a full right of deduction of VAT; or (in the case of an overvaluation) VAT has been charged and the supplier is not entitled to a full right of deduction of VAT. Where VAT has not been charged, the revaluation is only applicable where an exempt supply has been undervalued by a partly exempt person. Finally, the rule cannot apply if the difference between the open market value and the value of the supply is

not significant, or where it can be shown that the supply is available for the same consideration to others who are not connected under the definition.

Thus, the scope of the re-valuation measure is limited. It is envisaged that it will not be used in relation to normal everyday transactions but apply only to a very small number of transactions made within specific categories and in specific circumstances. The tests to be met mean that re-valuation will also not apply to such transactions as supplies of goods or services made below cost price as part of a promotion; a sale of damaged stock at a discount; or where there is a clearance sale for the end of a line, for example, or at the end of a season.

This measure aims to combat avoidance where a taxable supply is made at a low value to a purchaser who is not able to deduct all his VAT and thus the lower amount of tax represents a real and lasting loss to tax revenues. The consideration is only set at that level because links exist between the supplier and purchaser. In order to apply the rule, Member States will need to define the relevant connections between the parties. This definition must be within the categories set out in the Directive.

Similarly, the rule in relation to overvalued supplies is aimed at businesses who do not have full right of deduction, and who inflate their taxable supplies to a fully taxable business connected to them. The recipient is able to recover input tax in full, but by increasing the value the supplier manages to shift the balance between the value of taxable and non taxable supplies that they are making in order to engineer an increase in the proportion of deductible VAT. Businesses can achieve the same result by reducing the value of an exempt supply to decrease their exempt turnover relative to the value of their taxable supplies and thus increase their recovery rate.

Under this proposal the ability to re-value should only be applicable when the alteration of the value of a supply leads to a direct loss of tax either through increased recovery or because irrecoverable tax is reduced. There should be no tax loss where the supply is being made by a fully taxable person to another fully taxable person since the tax on the supply can simply be reclaimed and the valuation has no impact on the recovery of the supplier. These supplies have therefore been excluded from the alternative new rules. This is consistent with the fact that the optional rules are still a form of derogation from the normal rules which (in line with ECJ rulings) should be strictly limited to tackling the problem.

It is worth noting that acquisitions resulting from intra-EC trade as well as supplies within a Member State are covered by the rule since the proposal amends Article 11(A) of the 6th Directive which is the provision used under Article 28e to define the valuation of intra Community supplies.

The proposal allows for re-valuation of the supplies to the open market value (OMV). The proposed new paragraph (8) to Article 11(A) of the Sixth Directive adjusts and replaces the definition of OMV found in Article 11(A)(1)(d) to cater for this change. Of the two main options, re-valuing using the OMV or the cost price, the Commission feels that OMV is the most appropriate. The cost price would only have the effect of enabling Member States to neutralise the tax loss suffered through the low value whilst OMV allows the tax authorities the possibility to protect some of the tax on the value added. Neither the OMV nor the cost price are necessarily easily calculated on each supply but the OMV gives Member States the greatest scope to collect something approximating to the tax which would otherwise be due. To provide some additional protection for the taxpayer, the proposal re-affirms that the OMV

may be below the cost of making the supply, but also establishes that the OMV should normally be, as a minimum, the cost price.

The introduction of the measure together with the national legislation and rules governing it are subject to consultation with the VAT Committee, established by Article 29 of the 6th Directive. This is with a view to ensuring that the interpretation of the legislation is consistent throughout the Member States which opt to adopt the measure. It flows from this requirement to consult that Member States who currently have a derogation covered by this new rule will need to re-notify the details of their domestic legislation once the Community legal base changes.

Article 1(4) and (5): Reference changes

Both these paragraphs make consequential amendments to references to Article 21 in Articles 17 and 18 of the 6th VAT Directive. These cater for a new optional reverse charge rule added to Article 21(2) of the 6th VAT Directive by Article 1(7) of this Directive.

Article 1(6): Capital items

Article 20(2) and (3) of the Sixth VAT Directive lay down some specific rules for adjustment of deductions of input VAT on capital goods. Article 20(4) stipulates that Member States may define the concept of capital goods.

While it seems logical that services above a certain value, which are used for a longer period within a business, are treated in a similar fashion to goods this is not explicit within the Directive as it now stands. As a consequence, some Member States have refrained from applying Article 20(2) and (3) to services, although the Commission is aware that this approach has given rise to avoidance opportunities. The proposed amendment in Article 1(6) is intended to clarify that adjustment of deductions relating to capital items under Article 20 of the Sixth Directive may apply equally to services - provided that they are of a capital nature and are treated as such.

Article 1(7): Reverse charges

Article 1(7) extends the use of an optional reverse charge mechanism for specified supplies made to taxable persons. These are in sectors of the economy which have proved particularly difficult for Member States to police, for example because of the nature of the industry or its structure. Often substantial revenue losses arise from taxable persons invoicing for supplies prior to disappearing without accounting for the VAT on the invoice, whilst at the same time the recipient legitimately exercises his right to deduct.

The areas covered are services relating to buildings (including any, or all, of the services of construction, repair, cleaning and demolition); supplies of staff relating to building services; land and buildings on which the option to tax has been exercised; and supplies of waste, scrap and recyclable material together with some products resulting from their treatment and some treatment services. What is covered by the term "waste" is defined in a new annex containing a list covered by existing derogations. Although some Member States are currently empowered to apply an exemption by derogation to supplies of waste, a reverse charge offers the opportunity to recover tax; is easy to administer; has proved to work well where it has already been introduced; and ensures that hidden tax is not passed on to the purchaser through

the irrecoverable tax of the vendor. In addition, a new exemption, even if optional, would not sit well with the general need to limit extensions to the exemptions.

In addition, some Member States have a derogation which prevents tax losses arising in the following three circumstances: sales of immovable property in the course of judicial liquidation where the option to tax in Article 13(C) has been exercised; the sale of goods taken as security; and when goods are supplied following the cession of the reservation of ownership to an assignee and the exercise of the assignee's right. In all three scenarios the supply is usually made by a vendor who is in financial difficulties and who is unable to honour his debts, including his obligations to the tax authorities. The result is that either the tax is counted as proceeds from the sale and is retained by the creditor to offset the taxable person's debt, or (when it does reach the taxable person) the taxable person disappears without paying the tax to the authorities. Article 1(7) has the effect of making taxable persons who are the recipients of the supplies in these circumstances responsible for paying and accounting for the VAT on those supplies. This both simplifies and makes the system more efficient, with no impact in tax terms on the customer and with minimal additional compliance costs.

The second subparagraph identifies where Member States have the discretion (subject to the consultation process identified in the first sub paragraph) to apply limiting measures, and the nature of those measures.

Article 1(8): New Annex

The annex inserted by Article 1(8) identifies the types and forms of waste materials covered by the reverse charge.

Article 2: Repeals

This Article provides that Council Decisions under Article 27(1) and Article 27(4) (prior to amendment by Directive 2004/7/EC), are repealed when the contents come within the scope of the proposed Directive.

The date of repeal allows a year for those Member States needing to reflect the change of legal base and any changes of substance within their national measures to amend legislation. It also provides time for any required consultations with the VAT Committee.

In Annex I to this Explanatory Memorandum is a list of the Article 27(1) and (4) Decisions which, in the Commission's view, would be covered by Article 2 of the proposed Directive. Annex II identifies Decisions whose content matter is considered by the Commission to be covered by the terms of the proposal but which do not require repeal since the terms of the Decisions provide for expiry on a particular date or when alternative rules come into force, whichever is the earlier. The Commission will propose measures to ensure that derogations within this last category may be maintained after entry into force of the proposed Directive in cases where Article 29 consultation is required. The references used are to the original Decisions rather than to any subsequent renewals.

Finally Annex III to this Memorandum includes a list of the derogations notified to the Commission under Article 27(5) but which the Commission has been informed by Member States are no longer in use. In the Commission's view there is no need to formally withdraw the derogations listed, but there have been included here to assist transparency.

Article 3: Implementation, notification and references

Article 3 achieves two objectives. Paragraph 1 provides a time limit by which Member States have to makes changes to their domestic legislation to give effect to the parts of the Directive which have mandatory effect. The construction "necessary to comply" indicates that where a Member State does not choose to exercise an option introduced by the Directive then there is no requirement for national legislation. On the other hand, where existing options are amended through the proposed Directive, (for example the option for grouping in Article 4(4) of Directive 77/388), and where they have already been exercised by a Member State, that Member State will have to implement the changes. If the option is not currently used by a Member State then there will be no effect until the option is adopted.

The second sub paragraph and paragraph 2 establish that Member States adopting legislation under the Directive must notify the Commission, and that a reference to the Directive must be included either at publication or in the text.

Article 4: Entry into force and Article 5: recipients

Self explanatory.

ANNEX I

List of Decisions under article 27 considered by the Commission to be covered by the terms of the proposal, and therefore repealed by the Directive.

An unpublished Council Decision from 1979 regarding the valuation of supplies of goods or services effected by certain connected persons requested by the Federal Republic of Germany;

The Council Decision deemed to have been adopted on 11 April 1987 authorising the United Kingdom to apply a measure derogating from Article 11 of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.[4]

Council Decision 88/498/EEC of 19 July 1988 authorising the Kingdom of the Netherlands to apply a measure derogating from Article 21(1)(a) of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.[5]

A Council Decision deemed to be adopted on 18 February 1997 under the procedure contained in Article 27(4) of Directive 77/388/EEC in its version of 17 May 1977 authorising the Republic of France to apply a measure derogating from Articles 2 and 10 of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes. This decision follows notification of the request to Member States on 18 December 1996.

Council Decision 98/23/EEC of 19 December 1997 authorising the United Kingdom to apply a measure derogating from Article 28e(1) of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.[6]

Council Decision 2002/439/EC of 4 June 2002 authorising the Federal Republic of Germany to apply a measure derogating from Article 21 of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.[7]

Council Decision 2002/880/EC of 5 November 2002 authorising the Republic of Austria to apply a measure derogating from Article 21 of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.[8]

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4 OJ L 132, 21.5.87, p22
5 OJ L 269, 29.9.1988, p54
6 OJ L 8, 14.1.1998, p24
7 OJ L 151, 11.6.2002, p12
8 OJ L 306, 8.11.2002, p24

Council Decision 2004/290/EC of 30 March 2004 authorising the Federal Republic of Germany to apply a measure derogating from Article 21 of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.[9]

Council Decision 2004/736/EC of 21 October 2004 authorising the United Kingdom to apply a measure derogating from Article 11 of Directive 77/388/EEC on the harmonisation of the laws of Member States relating to turnover taxes.[10]

Council Decision 2004/758/EC of 2 November 2004 authorising the Republic of Austria to apply a measure derogating from Article 21 of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.[11]

[9] OJ L 94, 31.3.2004, p59
[10] OJ L 325, 28.10.2004, p58
[11] OJ L 336, 12.11.2004, p38

ANNEX II

List of Decisions under article 27 considered by the Commission to be covered by the terms of the proposal but not requiring repeal.

Council Decision 98/161/EC of 16 February 1998 authorising the Kingdom of the Netherlands to apply a measure derogating from Articles 2 and 28a(1) of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.[12]

Council Decision 2000/256 of 20 March 2000 authorising the Kingdom of the Netherlands to apply a measure derogating from Article 11 of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.[13]

Council Decision 2000/746/EC of 27 November 2000 authorising the Republic of France to apply a measure derogating from Article 11 of Directive 77/388/EC on the harmonisation of the laws of the Member States relating to turnover taxes. [14]

Council Decision 2001/865/EC of 6 November 2001 authorising the Kingdom of Spain to apply a measure derogating from Article 11 of Directive 77/388/EC on the harmonisation of the laws of the Member States relating to turnover taxes.[15]

Council Decision 2002/736/EC of 12 July 2002[16] authorising the Hellenic Republic to apply a measure derogating from Articles 2 and 28a of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.

Council Decision 2004/228/EC of 26 February 2004 authorising the Kingdom of Spain to apply a measure derogating from Article 21 of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes.[17]

Council Decision 2004/295/EC of 22 March 2004 authorising the Republic of Italy to apply a measure derogating from Article 21 of Directive 77/388/EEC on the harmonisation of the laws of the Member States relating to turnover taxes[18].

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12 OJ L 53, 24.2.1998, p19
13 OJ L 79, 30.3.2000, p36
14 OJ L 302,1.12.2000, p61
15 OJ L 323, 7.12.2001, p24
16 OJ L 233, 30.8.2002, p36
17 OJ L 70, 9.3.2004, p37
18 OJ L 97, 1.4.2004, p63

ANNEX III

List of article 27 (5) notifications identified by the relevant Member States to be redundant and therefore considered by the Commission to be repealed.

(1) Notifications for the Republic of France relating to

- Article 2 and 21 and the taxation of purchases from non-taxable persons;

- Article 11 and the flat rate determination of maximum taxable amounts for imports and supplies of horses of high value

- Article 11 and the taxation of the total amount of transactions effected by persons involved in the supply of products by non-taxable persons

(2) Notifications for the Federal Republic of Germany relating to

- Art 10 and the suspension of tax for certain supplies following importation.

- Art 17 and flat rate deductibility of VAT on travel expenses

(3) Notifications for the Grand Duchy of Luxembourg relating to

- Article 9 and the treatment of transport operations

- Article 11(C) and the conversion of values into Luxembourg Francs at the average rate for the month

- Article 13(A) and the exclusion from the scope of tax of activities carried out by non profit making associations for the benefit of their members in return for a subscription

- Article 21 and the appointment of a tax representative to account for VAT on sales made by suppliers of goods or services who are not established in Luxembourg.

(4) Notifications for the United Kingdom of Great Britain and Northern Ireland relating to:

- Articles 6, 11, 13 and special arrangements applied to the taxable amount for long stays in hotels

- Article 11 and the treatment of intermediaries involved in the sale of cosmetics

- Article 11 and the arrangements applied to discount stamps

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 93 thereof,

Having regard to the proposal from the Commission[19],

Having regard to the opinion of the European Parliament[20],

Having regard to the opinion of the European Economic and Social Committee[21],

Whereas:

(1) In order to combat tax avoidance and evasion and to simplify the procedure for charging value added tax, certain derogations applied for and granted in respect of individual Member States but covering similar problems should be made available to all Member States through incorporation in Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment[22]. Those measures should be proportionate and limited to countering the problem. Given that the Member States have different needs, that incorporation should be limited to extending the option of adopting the rules concerned to all Member States, as and when the need arises.

(2) Member States should be able to take action to ensure that facilitations provided for in Directive 77/388/EEC for the benefit of business relating to the taxable person and the transfer of a business as a going concern are not being exploited to avoid tax.

(3) It should be possible for Member States to intervene as regards the value of supplies in specific limited circumstances, to ensure that there is no loss of tax through the use of connected parties to derive tax benefits.

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19 OJ C , , p. .

20 OJ C , , p. .

21 OJ C , , p. .

22 OJ L 145, 13.6.1977, p. 1. Directive as last amended by Directive 2004/66/EC (OJ L 168, 1.5.2004, p. 35).

(4) It should be possible for Member States to include, within the taxable amount of a transaction, the value of investment gold used to make a finished product, where by virtue of being worked the gold loses its status of investment gold.

(5) It should be clearly established that certain services with the nature of capital items may be included in the scheme allowing for the adjustment of deductions for capital items over the lifetime of the asset, according to its actual use.

(6) Member States should be able, in specific cases, to designate the recipient of supplies as the person responsible for paying and accounting for value added tax. This should assist Member States in countering tax evasion and losses in identified sectors and on certain types of transactions.

(7) Directive 77/388/EEC should therefore be amended accordingly.

(8) Consequently, certain Council Decisions authorising individual derogations, pursuant to Article 27 of Directive 77/388/EEC should be repealed and Member States should not be able to avail themselves of those derogations under that article which are covered by the measures laid down in this Directive.

(9) In order that certain of the measures allowing Member States discretion of application and implementation may be applied consistently, their introduction should be subject to consultation in the Advisory Committee on value added tax established under Article 29 of Directive 77/388/EEC.

HAS ADOPTED THIS DIRECTIVE:

Article 1

Directive 77/388/EEC is amended as follows:

(1) In Article 4(4), the following subparagraph is added:

"Where a Member State exercises the option provided for in the second subparagraph, it shall ensure that the application of this option creates neither unjustifiable benefit nor unjustified disadvantage for taxable persons."

(2) In Article 5(8) the second sentence is replaced by the following:

"Where appropriate, Member States may, in cases where the recipient is not wholly liable to tax, take the necessary measures to prevent distortion of competition. They shall ensure that there is no unjustifiable benefit or unjustified disadvantage conferred."

(3) Article 11(A) is amended as follows:

(a) In paragraph (1)(d) the second subparagraph is deleted.

(b) The following paragraphs 5, 6, 7 and 8 are added:

"5. "Where a supply of goods or services involves the working of tax-exempt investment gold within the meaning of Article 26b(A) to the extent that it ceases to qualify as

such, Member States may provide that the taxable amount is to include the value of the gold contained in the finished product calculated on the basis of the current open market value of the investment gold.

6. Member States may, subject to the consultation provided for in Article 29, provide that the taxable amount of a supply of goods or services shall be the same as the open market value in any of the following circumstances:

(a) where the consideration is significantly lower than the open market value and the recipient of the supply does not have a full right of deduction under Article 17;

(b) where the consideration is significantly lower than the open market value and the supplier does not have a full right of deduction under Article 17 and the supply is subject to an exemption under Article 13;

(c) where the consideration is significantly higher than the open market value and the supplier does not have a full right of deduction under Article 17;

The option shall only be applied in order to prevent tax evasion and avoidance and when the consideration on which the taxable amount would otherwise be based has been influenced by family, management, ownership, financial or legal ties as defined by the Member State. For these purposes legal ties shall include the formal relationship between employer and employee.

7. The option provided for in paragraph 6 shall not apply in either of the following circumstances:

(a) where the supplier can demonstrate a commercial reason for the consideration charged for the goods or services

(b) where it can be shown that a similar consideration would be charged in the case of a person who has no ties with the supplier of the kind referred to in the second subparagraph of paragraph 6.

8. For the purposes of this Directive, ‘open market value’ shall mean the full amount that, in order to obtain the goods or services in question, a customer at the marketing stage at which the supply takes place would have to pay, at the time of the supply and under conditions of fair competition, to a supplier at arm's length within the Member State in which the supply is taxable. Unless justified by market conditions, the open market value shall not be less than the cost to the supplier of making the supply."

(4) Article 17(4), in the version set out in Article 28f(1), is amended as follows:

(a) In point (a) of the second subparagraph, the words "Article 21(1)(a) and (c)" are replaced by "Article 21(1)(a), (1)(c) or (2)(c) ";

(b) In point (b) of the second subparagraph the words "Article 21(1)(a)" are replaced by "Article 21(1)(a) or (2)(c);

(5) In Article 18(1)(d), in the version set out in Article 28f(2), the words "Article 21(1)" are replaced by "Article 21(1) or 21(2) (c)";

(6) In Article 20(4), the following subparagraph is added:

"Member States may also apply paragraphs 2 and 3 to services which have characteristics similar to those normally attributed to capital goods, including where those services are treated not as current expenditure but as having a continuing asset book value."

(7) In Article 21(2), in the version set out in Article 28g, the following point (c) is added:

"(c) where the following supplies are carried out Member States may, subject to the consultations provided for in Article 29, lay down that the person liable to pay tax is the taxable person to whom those supplies are made :

(i) the supply of construction, repair, cleaning, maintenance, alteration and demolition services in relation to immovable property;

(ii) the supply of staff engaged in activities covered by point (i) ;

(iii) the supply of immovable property, as referred to in Article 13(B)(g) and (h), where the supplier has opted for taxation of the supply pursuant to point (C)(b) of that Article;

(iv) the supply of used material, used material incapable of re-use in the same state, scrap, industrial and non-industrial waste, recyclable waste, part processed waste, and certain specified services listed in Annex M;

(v) the supply, outside a judicial liquidation procedure, of goods provided as security by one taxable person to another in execution of that security;

(vi) the supply of immovable property on which the option to tax under Article 13(C) has been exercised in the course of the judicial liquidation of the enterprise that owned the immovable property thus sold;

(vii) the supply of goods following the cession of the reservation of ownership to an assignee and the exercising of this right by the assignee.

For the purposes of the first subparagraph, Member States may specify the supplies covered by point (i) as well as the categories of suppliers or recipients to whom that point may apply. They may also limit the application of this measure to some of the supplies listed in point (iv) and in Annex M."

(8) Annex M set out in Annex I to this Directive is added.

Article 2

Any Decisions granting derogations pursuant to Article 27 of Directive 77/388/EEC that are covered by the provisions of this Directive are repealed with effect from [date – one year after entry into force].

Article 3

1. Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive on [one year after the entry into force] at the latest. They shall forthwith communicate to the Commission the text of those provisions.

   When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

2. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

Article 4

This Directive shall enter into force on the day following that of its publication in the *Official Journal of the European Union*.

Article 5

This Directive is addressed to the Member States.

Done at Brussels,

For the Council
The President

ANNEX I

"Annex M

List of supplies of used material referred to in Article 21(2)(c)(iv)

(a) the supply of ferrous and non ferrous waste, scrap, and used materials including that of semi-finished products resulting from the processing, manufacturing or melting down of non-ferrous metals;

(b) the supply of ferrous and non-ferrous semi-processed products and certain associated processing services

(c) the supply of residues and other recyclable materials consisting of ferrous and non-ferrous metals, their alloys, slag, ash, scale and industrial residues containing metals or their alloys and the supply of selection, cutting, fragmenting and pressing services for these products;

(d) the supply of, and certain processing services relating to, ferrous waste as well as parings, scrap, waste and used and recyclable material consisting of cullet, glass, paper, paperboard and board, rags, bone, leather, composition leather, parchment, raw hides and skins, tendons and sinews, twine, cordage, rope, cables, rubber and plastic;

(e) the supply of the materials referred to in point (d) after processing in the form of cleaning, polishing, selection, cutting or casting into ingots;

(f) the supply of scrap and waste from the working of base materials."