COMMISSION OF THE EUROPEAN COMMUNITIES

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Proposal for a

COUNCIL DIRECTIVE

Amending Directive 77/388/EEC

as regards the rules governing the right to deduct
Value Added Tax

Proposal for a

COUNCIL REGULATION (EC)

on verification measures,
measures relating to the refund system
and administrative cooperation measures
necessary for the application of Directive 98/xxx/EC

(presented by the Commission)

EXPLANATORY MEMORANDUM

As a result of the changes made to the common VAT system by the transitional arrangements, it was possible to eliminate, on 1 January 1993, the checks and administrative procedures prior to or on crossing an internal border of the European Union, while safeguarding to the maximum the Member States' discretion for determining the national VAT system, in particular by retaining a large number of options and powers in the Directive.

The abolition of physical barriers nevertheless placed greater emphasis on the intangible obstacles to transnational activities faced by business.

The wide variety of rules for determining the place where a transaction is taxed and, consequently, the place where the tax is deducted or refunded, and the lack of uniformity in the way the present system of VAT is applied, means that the Single Market is segmented into fifteen tax areas, creating legal uncertainty for traders. Thus, traders have to know the law and the way it is applied in each Member State where they carry out taxable transactions and in the Member States where they incur VAT-bearing expenditure.

In addition, traders exploit these differences by using clever tax accounting, and this distorts any fairness of competition that might otherwise exist in the Single Market.

In July 1996 the Commission presented a work programme accompanied by a timetable of proposals for the introduction of a genuine common system of VAT which will be suited to the demands of the Single Market. Under this programme, Community action will be based on three pillars: more uniform application of the tax, modernisation of the tax and a change in the taxation system (place of taxation).

However, independently of the move to a system of taxation at the place of origin, it is now an urgent necessity to modernise the general provisions of the present system and to achieve more uniform application. This phase has become the absolute priority of the work programme.

In a working paper dated 14 May 1997, the Commission also indicated that VAT obligations should be one of the sectors to be covered in the second phase of the SLIM initiative (Simpler Legislation for the Internal Market). The Commission felt that there was a need for immediate examination of simplification measures which would reduce the burdens on business in the short term, and at the same time pave the way for the introduction of the new system of VAT.

The working party set up to examine the subject identified the VAT refund procedure laid down by the Eighth VAT Directive as one of the subjects which is in urgent need of simplification.

Following the work of this group, the Commission report on the SLIM initiative, approved by the Internal Market Council on 27 November 1997, recommends a study of how to achieve a radical reform of the existing refund procedures in the Eighth Directive.

The first section of the present proposal is the outcome of this study. The objective of the proposed measures is to simplify the procedures enabling taxable persons established in the Community to recover the tax in a Member State where they are not established.

The second section of the present proposal concerns expenditure not eligible for a full deduction of VAT. This section forms part of the exercise of modernising the present system and ensuring its more uniform application. The objective of the proposed measures is to approximate the national rules that are currently very divergent in this area.

The two sections of the proposal, at first sight independent of one another, are in fact inseparable if the neutrality of the tax is to be ensured.

First of all, if the rules concerning the refund/deduction of the tax paid in a Member State where the taxable person is not established were amended without approximating the right to deduct, this would provide a solution to existing situations of distortion of competition, but would create new distortions, in particular for suppliers of services, who are in direct competition on the market of a given Member State, and who would be subject to different deduction rules.

Example: the services of three accountants, established in three different Member States (A, B and C), supplied to a taxable person established in Member State D, must all be taxed in Member State D. However, under the proposed system, the VAT paid in Member State D on expenditure on accommodation, food, petrol, etc. incurred when visiting their clients is deductible in their Member State of establishment within the limits applied by that Member State (provided that the accountants have no VAT identification in Member State D for other activities). Since the non-deductible VAT forms part of the cost of a service, an excessively wide divergence in the deduction rules leads to distortions of competition.

Secondly, since VAT is not fully deductible under the proposed expenditure rules, they still leave the Member States a margin of discretion. The change in the refund procedure prevents traders from exploiting any differences that might still result from this margin of discretion, so as not to create situations of unfair competition.

The two sections of the proposal are described in detail below.

1. DEDUCTION OF THE VAT PAID IN A MEMBER STATE WHERE THE TAXABLE PERSON IS NOT ESTABLISHED

Introduction

The Sixth VAT Directive establishes the principle that every taxable person is entitled to the deduction or refund of VAT, whatever the Member State where he has incurred VAT-bearing expenditure. However, as Community law stands at present, the taxable person can exercise this entitlement to deduction or refund only in the Member State where the transaction was taxed.

The Eighth VAT Directive harmonised, throughout the Community, the arrangements for the refund of VAT to taxable persons established in a Member State other than that making the refund. The main objective of that Directive is to place taxable persons who are not established in the Member State where they pay VAT on a similar footing to the taxable persons of that Member State who exercise their right to deduct by directly setting off the tax on their periodic returns.

The difficulties connected with the application of the Eighth Directive

In practice, the operation of the Eighth Directive refund procedure poses considerable problems for both traders and the national administrations of the Member States.

First, the procedure has given rise to complaints, from traders, and in particular that:

- administrative formalities are burdensome (requests must be made in an official language of the country of refund, documents must be presented by fixed time limits, etc.). In practice, traders are frequently obliged to use local advisers to complete these formalities;

- more and more Member States are failing to respect the time limit for refunds laid down by the Directive. Thus traders are compelled to pay the tax in advance and shoulder the cost over long periods: this can represent a considerable financial burden. Uncertainty as to when the refund will be made and, consequently, as to the size of the financial burden to be borne creates uncertainty for traders as to the costs to pass on to their customers;

- national administrations apply the provisions of the Eighth Directive extremely literally, so that requests are frequently rejected because of failure to respect the formalities and traders are given the impression that national administrations wish to discourage the use of the refund procedure.

The burden and the cost of the administrative formalities and the refund period mean that taxable persons who are entitled to a refund of VAT are discouraged from exercising that right.

As a result, the difficulties which taxable persons face in practice undermine the very principle of the deductibility of the tax and therefore the neutrality of the tax irrespective of the Member State of supply.

Secondly, the refund procedure causes considerable problems for the competent national administrations, since it has proved more difficult than expected to operate. Each refund request requires a physical intervention (in particular, every invoice and import document presented must be stamped and returned within one month) by the administration of the Member State of refund. The Member States must consequently allocate a significant number of officers to the completion of tasks considered to be unproductive; the purpose of which is to refund a tax collected on the national territory to taxable persons from other countries.

Even more important is the lack of effective verification as to whether an application for refund and the amount to be refunded are justified, since the administration possesses very little information with which to assess the right to refund.

The information available allows it to verify only:

- the applicant's status as a taxable person (on the basis of certification by the Member State in which he is established);

- the conformity of the invoice or the import document;

- the correct application of the limits to the right to deduct which are in force in the Member State of refund (where the tax was paid).

However, the Member State of refund has no information as to how the expenditure is actually divided between activities which are taxed, exempt or outside the scope of VAT and as to how the right to deduct is exercised (according to the proportion deductible or the actual attribution). Thus, the Member State is unable to take account of the taxable person's overall tax situation and is obliged to take decisions on the basis of incomplete information.

The Member States are well aware of this situation: in 1993 the complexity and cost of the procedure led 11 of the then 12 Member States to ask for a derogation on the basis of Article 27 which would enable them to introduce special measures for taxing certain work on movable tangible property and transport services located in the territory of the country but directly linked to the intra-Community transport of goods, so that traders did not have to have to use the Eighth Directive as a matter of course.

These derogations, authorised by Council Decisions, were justified by the fact that the increasing use of the refund procedures could impede the development of intra-Community trade in certain services.

The Council also amended the fifteen Commission proposals for a Decision on special measures for the taxation of telecommunications services, with a view to simplifying collection of the tax, so that operators did not have to use the Eighth Directive procedure.

In view of the foregoing, it was not unexpected for the SLIM initiative to make a recommendation on the Eighth Directive refund procedure, which was supported by both representatives of the national administrations and business.

The Commission's reaction to the SLIM recommendation

It is first of all important to stress that the above difficulties will be definitively solved by the introduction of the new common system of VAT, as set out in the work programme adopted by the Commission in July 1996.

Under this new system, based on the principle of a single place of taxation and deduction, every taxable person will be able to deduct the input VAT in one place, even if the transaction was taxed in another Member State. Consequently, the Eighth Directive procedure will become redundant.

The Commission has, however, decided to react promptly to the SLIM recommendation, while bearing in mind that any legislative initiative in this area can only have a temporary nature, pending the entry into force of the new common system of VAT.

The objective of the present proposal is therefore to improve the operation of the existing system of VAT in the short term, by simplifying a procedure which in the view of business impedes the operation of the Internal Market, while not undermining the continuation of the work envisaged by the work programme for the new common system.

Consequently, certain parts of the proposal will be revised as and when proposals for the introduction of the future system are presented.

The Commission is proposing additional verification measures, the justification and need for which will be regularly reviewed, with the sole object of immediately permitting adequate monitoring of the deduction in the absence of satisfactory cooperation between Member States in the area of verification.

Another consequence is that, were the Council not to adopt the present proposal within a reasonable period, the Commission would be obliged to withdraw it so that the Council did not have to go on discussing a proposal which could not achieve its objective - the rapid simplification of existing procedures - and which, if adopted belatedly, could therefore jeopardise the transition to the new common system.

The principles of the proposed system

A right to deduct

The Commission takes the view that the only change which can in fact significantly simplify the common system of VAT in general, and the refund procedure in particular, is to authorise the taxable person to deduct the VAT paid in a Member State where he is not established, by setting it off in his periodic return against the amount of VAT for which he is liable in a Member State where he carries out taxable transactions, for which the VAT-bearing goods and services are used.

The purpose of the present proposal is to introduce this right to deduct into Article 17 of the Sixth Directive, with the result that the special refund procedure for taxable persons established in the Union (i.e. the procedure laid down by the Eighth Directive) will disappear.

In substance, the proposed measures, which take the legal form of an amendment to paragraph 3 and the inclusion of paragraph 3a in Article 17, achieve the following result, as regards taxable persons established in the European Community:

- the taxable person is identified in a single Member State:

  the VAT is deducted in that Member State, irrespective of the Member State where he incurred the VAT-bearing expenditure;

- the taxable person is identified in several Member States:

  (a) he is identified in the Member State where he has incurred the VAT-bearing expenditure:

  the VAT is deducted in that Member State (no change as compared with the present situation).

  (b) he is not identified in the Member State where he has incurred the VAT-bearing expenditure:

  the VAT is deducted in the Member State where he supplies goods or services for which the expenditure is used.

It follows logically from this amendment of Article 17 that the amount of VAT eligible for deduction will now be determined according to the rules of the Member State of

establishment, and no longer according to the rules of the Member State which collected the tax, as is the case at present.

In terms of formalities, this proposal requires taxable persons to present a specific document, to be attached to their periodic return, on which they enter the VAT amounts paid in other Member States for which they are exercising their right to deduct. These amounts are to be broken down by Member State. A copy of the invoices or import documents is to be attached to this specific document in order to provide proof.

A bilateral refund and compensation system for debts

This document contains the information required to operate a refund system between the Member States, so that the Member State in which the deduction is made (Member State of deduction) can obtain a refund thereof from the Member State where it was paid (Member State of purchase). The attached proposal for a Regulation deals with this debt refund and compensation system, and with the verification measures to be established by the Member States.

The proposal for a Regulation provides for the introduction of a debt compensation and refund system which operates bilaterally between the Member States. For this purpose, each Member State will, every six months, inform each of the other Member States of the amount of VAT deducted during the past half year which the Member State of purchase is required to refund.

The amount to be notified represents the amount of VAT actually deducted, i.e. after application of the proportion when the taxable person is engaged both in activities in respect of which VAT is deductible and activities in respect of which VAT is not deductible, and after the limits on the right to deduct which are in force in the Member State of deduction have been applied.

In this way, any Member State can establish the balance payable to or receivable from the other Member States. These balances are actually paid at a later date, because they may still be adjusted as a result of the verifications laid down by the Regulation. However, there is provision for the Member States, by bilateral agreements, to derogate from the deadline laid down by the Regulation by setting other deadlines or, in certain circumstances, by allowing the balance to be carried over until the following period.

Verification measures

Under the present VAT system, each Member State is responsible for applying, monitoring and collecting the tax, which goes directly into its national budget. One of the basic principles of this system is that the VAT is deducted in the Member State where the tax was due and/or paid. A single Member State is therefore responsible for verifying payment and deducting the tax.

The purpose of the present proposal is to introduce a derogation from the above principle for the cases today covered by the Eighth Directive.

As a result, for the transactions concerned, the Member State of purchase will be responsible for verifying that the VAT has been paid, whereas the Member State of deduction will be responsible for monitoring the deduction of that tax.

Like any other verification, this should be based on the knowledge which the tax administrations have of their taxable persons, on how their reliability is assessed, the fraud risk that these taxable persons represent and on thorough and efficient cooperation with the administrations of the other Member States. Effective control in the Internal Market requires the establishment of common criteria for assessing the fraud risk that a taxable person represents, rather than the routine forwarding of copies of invoices which constitutes an additional burden for both taxable persons and administrations. The cases which, on the basis of these common criteria, are identified as requiring more thorough monitoring, would be of interest to all the administrations concerned. This would enable them, as a result of their mutual interest in effective cooperation, to exploit to the full the information and experience they possess.

Directive 77/799/EEC on mutual assistance enables the Member States concerned to exchange any information they consider necessary in order to exercise their respective powers of inspection. Past experience demonstrates, however, that the Member States are not yet making full use of the opportunities provided by this Community instrument.

In view of this experience, and of the special nature of the proposed system, which seeks to improve the operation of the present VAT system, the Commission is obliged to provide for additional verification measures to accompany its introduction.

These additional measures reduce the simplifying effects of changing the deduction system and are only acceptable in the short term. The length of time for which they are applied must be strictly limited to the time required to improve cooperation between the Member States.

The Commission will regularly examine the use of these measures and their practical results for the Member States. For this purpose, the Member States are required to provide the Commission with the necessary information. The Commission will present to the Council, by the end of the second year in which these measures are applied, a report on whether they are justified and necessary as part of its monitoring of the cooperation between the Member States on verification, where necessary accompanied by proposals repealing the said measures.

As regards the verification measures laid down by the present proposal, it is important to bear in mind the nature of most of the expenditure for which refund requests are now made under the Eighth Directive procedure.

Because of the rules for the location of transactions, most of these requests relate to general costs, such as hotel and restaurant costs, costs connected with taking part in fairs and the vehicle and motor fuel costs of international road transport operators.

It is therefore unlikely that the proposed system, under which these amounts will be set off against the tax owed by the taxable person, will substantially increase the situations in which operators are entitled to high tax credits, which usually require more monitoring by the administration.

Consequently, it is necessary to ensure that the verification measures proposed specifically for operating the deduction system are not disproportionate to the risks of tax losses for the Member States.

The measures provided for by the Regulation result in several-stage verification and for each of the stages establish the financial responsibilities of the Member States concerned.

This phased verification has a great advantage over the present system, since it does not require the administration to take an "immediate and virtually final" decision, as is the case today.

First, the administration of the Member State of deduction carries out an initial verification when it receives the periodic return, the specific document and its annexes. Unlike the administration of the Member State of refund under the present system, the competent administration will already possess more precise data concerning the tax situation of the taxable person.

Clearly, the amount corresponding to the adjustments that are necessary following this initial verification is not included in the amount of VAT which the Member State of deduction requires the Member State of purchase to refund.

Next, the Member State of deduction provides the Member State of purchase with information, normally in electronic form, concerning certain transactions for which a deduction under Article 17(3a) is made.

When the Member State of purchase detects irregularities relating to the transactions for which the deduction has been made, it must inform the Member State of deduction thereof within three months of receiving the information. In addition, the Member State of purchase is not required to refund the amount of VAT in question to the Member State of deduction.

It is up to the Member State of deduction to take the recovery measures it considers appropriate, particularly in the light of the tax situation of the taxable person in question (filing of periodic returns, payment of the tax due, other existing tax debts).

In addition, irrespective of the place where the VAT was paid, the Member State of deduction examines whether the deduction made is justified, as part of the scheduled inspection of all the taxable person's activities.

Lastly, under the verification procedure laid down by this proposal there is nothing to prevent the administrations from requesting information by utilising the mutual assistance Directive procedure.

Also, the Commission is well aware of the fact that the non-harmonisation of information that has to appear on invoices is liable to pose problems. However, this problem already exists in normal intra-Community trade (supplies/intra-Community acquisitions, intra-Community transport, etc.) the only difference being, in the present case, that VAT is actually invoiced in the Member State of purchase. The SLIM report also contains a recommendation to study this problem. The Commission will not fail to act on this recommendation.

Pending the outcome of such work, the operation of the proposed system requires a minimum of flexibility from the Member States. They have to ensure that a taxable person in possession of an invoice, which mentions at least the information required by the Sixth Directive, is not prevented from exercising his right to deduct.

Nevertheless, an administration has the right to request from the taxable person a translation of the invoice entries in cases where it is unable to assess the business nature of the expenditure.

Conclusion

Introducing the requirement to present a specific document is justified because it enables all the present obligations laid down by the Eighth Directive to be abolished.

It can be concluded that the present proposal considerably simplifies recovery of the tax paid in a Member State where a taxable person is not established and, as a result, puts an end to a real obstacle to transnational activities. It also simplifies administrative management for the Member States by providing better opportunities for verification at Community level.

In legal terms, this change in the system requires:

- an amendment to Article 17 of the Sixth Directive, to include the right to deduct the VAT paid in a Member State where the taxable person is not established, and to Article 22 of the Directive, as regards the requirement to file a specific document and its annexes;

- the bringing into force of a Regulation which manages relations between the Member States as regards the bilateral compensation and refund system and the verification measures;

- the repeal of the Eighth Directive.

2. EXPENDITURE WHICH IS NOT ELIGIBLE FOR FULL DEDUCTION

Introduction

As regards the rules for the deduction of VAT, Article 17(6) states that:

"Before a period of four years at the latest has elapsed from the date of entry into force of this Directive, the Council, acting unanimously on a proposal from the Commission, shall decide what expenditure shall not be eligible for a deduction of value added tax. Value added tax shall in no circumstances be deductible on expenditure that is not strictly business expenditure, such as that on luxuries, amusements or entertainment.

Until the above rules come into force, Member States may retain all the exclusions provided for under their national laws when this Directive comes into force."

The provision refers to expenditure which, even when incurred as part of the normal running of a business, is often also intended to meet private needs, because it has the characteristics of private consumption. In these cases, it is not always easy to apportion such expenditure between business element and private element, with the result that there can be a risk of abuse or tax evasion, giving rise to distortions of competition.

The Member States have solved the problem in different ways:

Most countries (B, DK, EL, E, F, IRL, I, AU, P, FI, S, UK) exclude or limit the right to deduct so as to eliminate or substantially simplify cases where a distinction has to be made between expenditure relating to the private needs of the taxable person and others, and expenditure connected with the economic activities of the taxable person: according to the Member States concerned, this has advantages for the administration and prevents or limits tax fraud.

The other countries (D, L, NL) grant the right to full deduction, in accordance with Article 17(2), for the expenditure in question or for the most important categories of such expenditure, the only exclusion being that which has no business characteristic.

A proposal for a Directive on this subject was presented to the Council on 25 January 1983.[1] However, even though an amending proposal[2] was presented to take account of Parliament's amendments, it was not possible to reach a consensus on this proposal. Since the Council was unable to take a unanimous decision on this proposal, the Commission finally decided to withdraw it on 21 November 1996.[3] Withdrawal is also the logical consequence of the Commission's adoption in July 1996 of the work programme for the introduction of a common system of VAT, suited to the demands of the Single Market.

The difficulties in the present situation

The present situation does not meet the essential requirements of uniformity of the basis of assessment and tax neutrality.

The taxable persons of a Member State which authorises the full deduction of the tax for all expenditure, except that which has no business characteristics, enjoy an advantage compared with the taxable persons of a Member State where some categories of expenditure are excluded from the right to deduct. This difference in treatment can lead to distortions of competition in international trade in goods and services in so far as its effects are indirectly passed on to the price of goods and services.

Although the existence of this diverse treatment is not a new problem, the establishment of the Internal Market on 1 January 1993 highlighted these differences far more sharply by bringing national laws and the way they are applied by the Member States into more direct competition.

The Commission therefore feels it necessary to act on the mandate laid down in Article 17(6) of the Sixth Directive, and to resume the approximation of the different national rules which exist at present, while leaving Member States some margin of discretion to take account of the specific situation in their country.

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1 OJ C 37, 10.2.1983, p.8.

2 OJ C 56, 29.2.1984, p.7.

3 OJ C 2, 4.1.1997, p.2.

The principles of the proposed system

It should not be forgotten that the right to deduct is a basic feature of the value added tax system. Consequently, any exclusion from this right is an exception to the rule, which is unacceptable unless it is specifically justified.

Clearly, therefore, the proposal must be confined to categories of expenditure which, even when incurred as part of the normal running of a business, usually contain some element of private and final consumption at the same time. In general, moreover, there can be no real verification of how such expenditure is apportioned between business element and private element, so that risks of abuse or tax fraud are created.

Such expenditure is that particularly relating to passenger cars, expenditure on accommodation, food and drink, and expenditure on luxuries, amusements or entertainment.

Expenditure relating to passenger cars must be considered to refer to capital goods, the non-business use of which cannot be ruled out, and which above all cannot be easily verified.

Although expenditure on accommodation, food and drink can be incurred in certain places and according to certain rules because of the business activity exercised, there is no doubt that it also has private characteristics, since it is expenditure which satisfies primary needs.

Lastly, it should be remembered that the basic principle that the tax charged on goods and services used for the purposes of taxed transactions is deductible means that the deduction does not apply to expenditure which is not of a strictly business nature, such as expenditure on luxuries, amusements or entertainment, in accordance with the present version of Article 17(6).

Various systems have been established to take account of the specific nature of such expenditure as part of the activity of taxable persons.

Expenditure on passenger cars

As a rule, the normal deduction rules apply to the VAT on expenditure relating to passenger cars.

However, if difficulties in verifying the non-business use of these goods are so great that they prevent a Member State from applying the normal deduction rules in practice, an optional system for limiting the deduction has been established, enabling the Member States which so wish to measure the non-business use of passenger cars in a simplified fashion.

A Member State that makes use of this option may set a maximum percentage for deduction which may not be lower than 50% of the input tax, this amount corresponding to the maximum business use which, it is assumed, has been made of the passenger cars.

By utilising this option, the administration has no need to monitor the way in which a substantial majority of taxable persons apportion the private and business use of their passenger cars in their accounts.

However, where the percentage of business use is not as high as the percentage of the ceiling for deductible VAT set by the Member State of the deduction, the deduction is made according to the normal rules.

Application of a maximum deductible percentage enables a simplified distinction to be drawn between the input tax:

- linked to the non-business use of cars, i.e. private use but also use for transactions outside the scope of VAT;

- linked to the business use of cars, i.e. for transactions within the scope of VAT, both transactions in respect of which VAT is deductible and exempt transactions in respect of which VAT is not deductible.

Consequently, when the taxable person carries out both transactions in respect of which VAT is deductible and transactions in respect of which VAT is not deductible, the proportion of input VAT linked to the business use of passenger cars still has to be broken down to determine the VAT attributable to the former and the latter transactions.

Lastly, when the business use of the goods considered is negligible, the time spent by the administrations on verification will not be justified by the result. This is why the proposal provides for total exclusion from the right to deduct if the business use is less than 10%.

Special consideration is given to taxable persons whose activity consists in the operation of passenger cars or who rely on such goods to engage in their activity (e.g. taxable persons whose economic activity consists of the sale or hire of passenger cars, or who operate taxis, driving schools, etc.). In this case, the normal deduction rules are applied, but only if any non-business use is negligible, i.e. less than 10%.

Other expenditure

As regards expenditure on accommodation, food and drink, their characteristic of final consumption may justify exclusion from the right to deduct. However, such expenditure may be caused by the needs of the activity, e.g. because it is incurred during business travel. This is why a flat-rate limit on the deduction was considered fair, with the flat-rate percentage for deduction being set at 50% of the value added tax charged on expenditure on accommodation, food and drink.

However, deduction continues to be entirely ruled out for expenditure that is not directly and strictly linked with the needs of the taxed transactions, i.e. for expenditure on luxuries, amusements or entertainment.

3. PRESENTATION OF EACH OF THE PROVISIONS OF ARTICLE 1 OF THE DIRECTIVE

Ad point 1

Article 17(6) is repealed.

5. FISHING ZONES

The vessels referred to in Article 1 of the Protocol shall be authorised to engage in fishing activities in the waters beyond twelve nautical miles from the base lines.

6. ENTERING AND LEAVING THE ZONE

Vessels shall notify the Gabonese Ministry responsible for fisheries of their intention to enter or leave Gabon's fishing zone at least 24 hours in advance. When notifying their departure, all vessels shall also notify the estimated catches taken during the time they have spent in Gabon's fishing zone. This information should preferably be communicated by fax or, for vessels not equipped with a fax, by radio.

A vessel found to be fishing without having informed the Gabonese Ministry responsible for fisheries shall be regarded as a vessel without a licence.

Vessels shall be informed of the relevant fax number and radio frequency when the fishing licence is issued.

The Gabonese Ministry responsible for fisheries and the shipowners shall keep a copy of fax communications or a recording of radio communications until both parties have agreed to the final statement of fees due referred to in point 2.

7. ZONES CLOSED TO SHIPPING

The zones adjacent to oil extraction activities shall be closed to all shipping.

The Gabonese Ministry responsible for fisheries shall notify the coordinates of these zones to shipowners when the fishing licence is issued.

The zones closed to shipping shall also be notified for information purposes to the Delegation of the European Commission in the Gabonese Republic, as shall all changes to these zones, which must be announced at least two months before enforcement.

8. USE OF SERVICES

Community vessels shall, wherever possible, transship and procure the supplies and services they require in Gabonese ports.

Article 17b lays down provisions regarding exclusions from the right of deduction.

Article 17b(1)(a) provides that the VAT charged on expenditure relating to passenger cars is not deductible when their business use is less than 10%. In this case the difficulties in checking the breakdown between business and non-business use would be too great to justify the results. This provision is compulsory for all the Member States, therefore irrespective of whether or not a Member State has decided to use the option in the first subparagraph.

Since this exclusion concerns transactions in respect of which VAT is generally deductible, the taxable person may adjust the deduction when, in the subsequent year or years, the business use of the passenger car exceeds 10%, since the condition on which the exclusion is based no longer exists.

This is an exclusion laid down with a view to simplifying the administrative management of the VAT system. Consequently, when the business use of a car becomes too great, there is clearly no justification for retaining the effects of this exclusion.

Article 17b(1)(b) excludes any right to deduct for expenditure on luxuries, amusements or entertainment.

It would not seem appropriate to attempt a precise definition of what is meant by "expenditure on luxuries, amusement or entertainment" under the terms on this Directive.

It would instead be preferable to ensure a consistent interpretation on the basis of implementing measures. The Commission would refer, in this respect, to its proposal to amend the rules of procedure of the VAT Committee so as to transform it into a regulatory committee.

Only a few general indications of what might be covered by these terms should be given at the present stage.

"Expenditure on luxuries" might include expenditure which, by its nature and amount, can no longer be considered normal operating expenditure, e.g. the purchase by an accountant of an ECU 50 000 oriental carpet to decorate his office.

"Expenditure on amusement and entertainment" would cover expenditure designed to give (potential) clients a positive image of the taxable person and his business and expenditure defrayed solely to encourage clients to do business and employees to perform their duties, e.g. the purchase of 100 tickets to a football match for distribution free of charge.

Article 17c, introducing transitional provisions, establishes that the new system for limiting the deduction relating to passenger cars and to expenditure on accommodation, food and drink, and the exclusion from the right to deduct for expenditure on luxuries, amusements or entertainment, does not apply to situations arising when the previous legislation was in force (i.e. the exclusion from deduction), but only to transactions effected after the new system was introduced.

The right to deduct for capital goods arises when the taxable person acquires them, but, under Article 20 of the Sixth Directive, it is adjusted every year during the adjustment period. Thus, if the law were changed to introduce a right to deduct, even partial, in the case of capital goods the deduction would have to be adjusted on the basis of the years

remaining until the end of the adjustment period: this could have very significant budgetary effects for the Member States which did not grant a right to deduct.

Ad point 3

The purpose of extending the application of Article 20(3) is to deal with the eventuality of double taxation where a passenger car which has been eligible for a limited deduction in accordance with Article 17a is resold.

However, in order to avert the risks of tax avoidance, the amount of the adjustment can not exceed the amount of tax obtained by applying the rate of tax in force for passenger cars to the taxable amount of the resale.

Without this measure, tax could be avoided where a business car was resold to a private individual at an artificially low price, after only a few months' use. This measure limits the adjustment amount to the amount of tax due at the time of the resale, or, insofar as the resale is exempt (e.g. intra-Community supply), to the amount of tax which would be due if the resale was not exempt.

Ad point 4

Point 4 provides for modifications to Article 28f.

Ad point 4 a)

The purpose of this amendment is to exclude from Article 17(3), as amended by Article 28f, the principle of the right to a refund of the VAT paid in a Member State where the taxable person is not established, in so far as the taxable person is established in the Community.

Ad point 4 b)

New paragraphs 3a, 3b and 3c are inserted into Article 17, as amended by Article 28f: this entitles taxable persons established in the Community to deduct the VAT paid in a Member State where they are not established.

The first subparagraph of paragraph 3a provides for the principle of deduction.

The second subparagraph of paragraph 3a specifies the Member State where the taxable person can deduct the VAT, when he is identified for VAT purposes in several Member States. Clearly, this provision is only important if it is in fact the same person (the same legal entity) that is identified for value added tax in several Member States.

Example: a taxable person has the seat of his activity in Member State A. He also has fixed establishments from which taxable transactions are effected in Member States B and C. The VAT paid in Member State D, charged on the hotel costs of staff of the fixed establishment in Member State B, is deductible in Member State B according to the rules in force in that Member State.

The first subparagraph of paragraph 3b contains the definition of a non-established taxable person. This definition is the one laid down by Article 1 of the Eighth Directive supplemented by the rule that Directive 92/111/EEC added to Article 17(4).

The second subparagraph of paragraph 3b contains a provision concerning the exchange rate to be used to calculate the deductible VAT. Clearly, this provision applies only where either the amount of VAT paid is indicated in the currency of a country which does not use the Euro as national currency (VAT invoiced in dollars), or the Member State where the deduction is made has not introduced the Euro as its national currency.

Since the use of Community provisions on customs value is a principle familiar to the common system of VAT, the most appropriate solution seems to be to use these provisions for the application of paragraph 3a.

Lastly, the third subparagraph of paragraph 3b contains a provision which is meant to ensure that the non-harmonisation at Community level of the information to be mentioned on invoices shall not prevent a taxable person from exercising the right to deduct.

A taxable person who holds an invoice drawn up according to the rules applicable in the Member State of purchase cannot be prevented from exercising his right to deduct on the grounds that this invoice does not contain all the entries required by the law of the Member State of deduction.

Pending the examination of this matter in line with the SLIM recommendation made on this subject, the Member States must take the necessary measures to ensure that the administration of the Member State of deduction agrees that a taxable person should exercise his right to deduct when he is in possession of an invoice which mentions at least the information referred to in Article 22(3)(b).

Paragraph 3c lays down that the Council will adopt measures on the refund system and the administrative-cooperation measures necessary to ensure that the deduction arrangements of paragraphs 3a and 3b function properly.

These measures are dealt with in the proposal for a Regulation presented at the same time as this proposal for a Directive.

Ad point 4 c)

Article 17(4) of the Sixth Directive, as amended by Article 28f thereof, is amended to contain only references to the refund procedure laid down by the Thirteenth Directive, since any reference to the Eighth Directive procedure has become redundant.

Ad point 5

The introduction of a right to deduct the VAT paid in a Member State where the taxable person is not established requires the introduction of a new obligation in Article 22 of the Sixth Directive, as amended by Article 28h thereof.

In order to operate the refund system between the Member States, and for verification reasons, point (d) is added to Article 22(4). It requires the taxable person who exercises a right to deduct the VAT paid in a Member State where he is not established to attach a specific document to his periodic return.

In this document, the taxable person indicates, for each Member State, the deductible amount of tax. A copy of the invoices or the import documents must be attached to this specific document to provide evidence of these amounts.

The use of a specific document for these transactions means that an unnecessary extension of the periodical return forms can be avoided in all cases where the taxable person has not, during the tax period, incurred expenditure in the Member States where he is not established.

For verification reasons, the document must also contain a statement in writing by the taxable person certifying that he is not identified for VAT purposes in each of the Member States where he has paid the VAT for which he is exercising his right to deduct by means of the document in question.

4. INDIVIDUAL PRESENTATION OF THE REGULATION'S PROVISIONS

Ad Article 1

This Article defines the Regulation's scope.

Ad Article 2

Paragraph 1 defines some of the terms used in the Regulation.

Paragraph 2 requires Member States to determine the authority or authorities responsible for applying this Regulation and to provide the other Member States and the Commission with a list thereof.

Ad Article 3

Article 3 sets out the verification measures to be taken on submission of the periodic return in which the deduction is made.

Any irregularity detected when this verification is carried out must be corrected by the Member State of deduction.

In addition to this correction, where the verification reveals that taxable transactions have occurred on the territory of another Member State, the Member State of deduction must also inform the Member State concerned thereof. In such a case, the conditions governing deduction under Article 17(3a) of the Sixth Directive are not met and the taxable person in question is no longer considered to be a taxable person not established in the Member State of purchase.

Carrying out this verification as soon as the return is submitted allows tax administrations to react promptly to any irregularities detected and immediately to exclude the VAT on these transactions from the system of refund between Member States.

Ad Article 4

The first paragraph lays down the principle that the Member State of deduction is to obtain, from the Member State of purchase, a refund of the amount of VAT deductible pursuant to Article 17(3a).

Any adjustments carried out as a result of irregularities detected during the verification referred to in Article 3 are obviously excluded from the refund amounts.

The second paragraph lays down that, every six months, each Member State must inform all the other Member States of the amount, in Euro, of tax to which it is entitled by way of a refund under the first paragraph.

The information is to be expressed in Euro so that the refund amount to which a given Member State is entitled can be offset against the amount it is required to refund to the other Member State.

The third paragraph lays down that, as regards those Member States which have not introduced the Euro as their national currency, the amount of VAT, in national currency, which a Member State may obtain as a refund must be converted into Euro in accordance with the Community provisions in force for calculating customs value since the use of these provisions is a principle familiar to the common system of VAT.

Ad Article 5

The information referred to in Article 4 allows the calculation, bilaterally, of a balance between the Member States.

However, this balance is provisional since it can still be corrected as a result of applying the procedure laid down in Articles 6, 7 and 8.

Ad Article 6

The first paragraph lays down the principle that the Member State of deduction must inform the Member State of purchase of certain transactions in respect of which the right to deduct, pursuant to Article 17(3a), is exercised, namely those transactions which are likely to present a risk of tax evasion.

In order to enable the Member State of purchase to act quickly, the information must be sent by the 15th day of the month following the month in which the periodic return, together with the specific document and copies of invoices or import documents, is submitted.

To ensure that verification is effective, it is made clear that traders should not know the criteria used to determine the transactions which should be notified, and that these criteria may be amended by means of a quick and flexible procedure when the Member States' practical experience reveals that this is necessary.

For these reasons, the second paragraph of Article 6 lays down that responsibility in this area lies with the Standing Committee on Administrative Cooperation in the field of Indirect Taxation which, in this instance, acts as a "regulatory committee".

The third paragraph entitles Member States to lay down additional criteria on the basis of bilateral agreements.

The fourth paragraph requires Member States to supply the Commission with any information concerning the use of exchanged information which the Commission might deem necessary for drawing up the report referred to in Article 12.

Ad Article 7

When the information received pursuant to Article 6 allows the Member State of purchase to establish an irregularity in the transaction which has given rise to a deduction pursuant to Article 17(3a), that Member State must inform the Member State of deduction thereof within three months of receiving the relevant information.

This provision is more particularly concerned with instances in which the Member State of purchase discovers that the transaction in question is fictitious (e.g. fictitious taxable person, taxable person who exists, but where the transaction does not correspond to his economic activity), or that the taxable person in question is carrying out taxable transactions on its territory. In the latter case, deduction pursuant to Article 17(3a) must be refused, even if the expenditure in question was incurred as part of the taxable person's economic activity. Refusing deduction is an effective means for the Member State of purchase of compelling the taxable person in question to complete the formalities relating to identification, submitting returns and paying the tax.

By contrast, the mere finding that the tax due on a given transaction has not been paid to the Treasury is not enough to cast doubt on the regularity of the transaction giving rise to deduction of the tax in another Member State.

Ad Article 8

Where the Member State of purchase informs the Member State of deduction of any irregularities within the stipulated three months, the amount in question will not be refunded by the Member State of purchase to the Member State of deduction.

This means in practice that the financial burden of non-recovery of the amount in question falls on the Member State of deduction.

However, once the three-month period has elapsed, the Member State of purchase is no longer authorised to reduce the amount of tax, for which the Member State of deduction is requesting a refund, by setting off the tax connected with irregular transactions.

Ad Article 9

The first paragraph lays down the dates on which the final balance between Member States is determined.

If the provisional balance has not yet been fixed when the Member State of purchase, within the required deadline, informs the Member State of deduction of an irregularity, the amount of tax in question will not be included in the provisional balance.

However, if the provisional balance has already been fixed when the Member State of purchase, within the required deadline, informs the Member State of deduction of an irregularity, the provisional balance must be adjusted accordingly.

This is why provision is made for the balance to be determined on 30 April and 31 October, so leaving four months between the end of the period during which returns are submitted and calculation of the final balance.

The second paragraph lays down the date on which the balance must be paid, i.e. 15 days after the final balance has been calculated.

The third paragraph stipulates that payment be made in Euro, since the balance has already been calculated in that currency.

The fourth paragraph allows Member States to agree on other deadlines. For example, two Member States for which the refund amounts are small might wish to simplify the administrative procedure by, for example, carrying the balance forward until such time as it reaches a certain threshold.

Ad Article 10

This Article introduces new powers for the Standing Committee on Administrative Cooperation in the field of Indirect Taxation set up by Article 10 of Council Regulation (EEC) No 218/92 of 27 January 1992.

All the measures necessary for the implementation of the Regulation will be discussed by this Committee, which will serve as a regulatory committee for this purpose. It is already stipulated in Article 10(3) and (4) of Regulation No 218/92/EEC that the Committee may act as a regulatory committee on certain matters relating to the implementation of the Regulation.

Ad Article 11

This Article lays down that, if Member States enter into bilateral agreements under Articles 6 and 9 of the Regulation, they must inform the Commission thereof.

Ad Article 12

This Article lays down that, before the end of the second year of application of the additional verification measures, the Commission will present a report to the Council on whether they are justified or necessary and on the development of cooperation between Member States in the area of verification, where appropriate accompanied by proposals repealing the additional measures.

Ad Article 13

This Article specifies 1 January 1999 as the date on which the Regulation will enter into force.

Proposal for a
COUNCIL DIRECTIVE
amending Directive 77/388/EEC
as regards the rules governing the right to deduct
Value Added Tax

98/0209 (CNS)

THE COUNCIL OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular Article 99 thereof,

Having regard to the proposal from the Commission,[1]

Having regard to the opinion of the European Parliament,[2]

Having regard to the opinion of the Economic and Social Committee,[3]

Whereas the arrangements for the refund of tax to non-established taxable persons laid down by the Eighth Council VAT Directive (79/1072/EEC) of 6 December 1979[4], as last amended by the Act concerning the conditions of accession of the Kingdom of Norway, the Republic of Austria, the Republic of Finland and the Kingdom of Sweden and the adjustments to the Treaties on which the European Union is founded, in practice pose considerable problems for both business and the national administrations of Member States;

Whereas the Commission's report on the second phase of the SLIM initiative recommends examination of methods of radically reforming the arrangements for refund now laid down by the Eighth Directive;

Whereas the only change which can effectively make a major simplification to the common system of VAT in general, and to the refund procedure in particular, is to authorise the taxable person to deduct the VAT paid in a Member State where he is not established, by directly setting it off against the amount of VAT for which he is liable in a Member State where he carries out transactions eligible for a deduction;

Whereas in order to provide for every taxable person established in the Community the right to deduct the VAT paid in a Member State where he is not established, it is necessary in particular to amend Article 17 of the Sixth Council Directive (77/388/EEC)

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1 OJ C

2 OJ C

3 OJ C

4 OJ L 331, 27.12.1979, p.11.

of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes - Common system of value added tax: uniform basis of assessment;[5]

Whereas such amendment requires the introduction of a system of refund between the Member States, so that the Member State where the taxable person is established can recover the amount of VAT deducted from the Member State where this VAT has been paid;

Whereas, for the requirements of the refund and verification system, it is appropriate to require taxable persons to present a specific document to be attached to their periodic returns, on which they enter, for each Member State, the amounts of VAT paid in other Member States for which they are exercising their right to deduct and to require them to attach a copy of the invoices or import documents to this specific return;

Whereas, on the other hand, all the administrative formalities laid down by the Eighth Directive become redundant and therefore this new requirement does not undermine the objective of simplifying the entire procedure nor the opportunity to repeal the current 8th Directive;

Whereas the steps to be taken by traders to recover the VAT in a Member State where they are not established are considerably simplified;

Whereas in addition administrative management is simplified while providing the best opportunities for verification;

Whereas these changes are nevertheless only temporary, since they will become redundant when the new common system of VAT, based on the principle of a single place of taxation and deduction, is introduced;

Whereas, with a view to respecting the neutrality of the tax, it is appropriate for the procedure for recovering the tax paid in another Member State where the taxable person is not established to be simplified at the same time as the rules for limiting the right to deduct are approximated;

Whereas the recommendation made in the Commission's report on the SLIM initiative also makes the link between these two subjects;

Whereas certain items of expenditure, even when incurred in connection with the normal operation of a business, are often also liable to meet private needs and therefore have the characteristics of final consumption;

Whereas the apportionment of such expenditure between business and private use cannot always be accurately verified, so presenting the risk of abuse or fraud;

Whereas, in the present situation, the existing exclusions from, and limitations to the right to deduct in the Member States are very dissimilar, and this may be a source of distortions of competition;

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5 OJ L 145, 13.6.1977 p.1, as last amended by Directive 96/95/EC (OJ L 338, 28.12.1996, p.89).

Whereas this diversity is not a new problem, but whereas the operation of the Single Market since 1993 has made it more obvious that diversity can lead to distortions of competition in international trade insofar as its effects are passed on to the price of goods and services;

Whereas the problem of the dual business and private nature of expenditure and the resulting difficulties of verification exist in particular for expenditure on passenger cars, accommodation, food or drink, and that on luxuries, amusements or entertainment;

Whereas, in taking into account the different possibilities of intended use for business needs and the verification difficulties, a variety of arrangements must be established for the above categories of expenditure, but the normal deduction rules must apply for all expenditure for which this Directive does not provide specific rules;

Whereas, as regards expenditure relating to passenger cars, it is appropriate to provide for an optional arrangement, so that Member States which so wish can determine that the part of the non-business use of passenger cars in a simplified manner, while leaving a certain margin of discretion under this optional arrangement;

Whereas, as regards expenditure on accommodation, food and drink, a flat-rate limit to the right to deduction has been considered the most appropriate to take account of the dual business and private nature which such expenditure has;

Whereas, expenditure on luxuries, amusements and entertainment should be excluded from the right of deduction, given that this expenditure is not strictly business expenditure;

Whereas the purpose of approximating national laws on the expenditure referred to in this Directive is to confirm the general rules governing the right to deduct resulting from the Sixth Directive (77/388/EEC), by limiting all exceptions to those rules solely to the cases explicitly considered;

HAS ADOPTED THIS DIRECTIVE:

Article 1

Directive 77/388/EEC is hereby amended as follows:

(1) Article 17(6) is repealed.

(2) The following Articles 17a, 17b and 17c are inserted:

"Article 17a

Limitations of the right of deduction

1. As regards expenditure relating to passenger cars which cars which are not used solely for business purposes, Member States may provide that the deduction of the value added tax charged on such expenditure shall be calculated within the limit of a ceiling to be set by the Member States at not less than 50% of the said tax.

The provisions contained in the above subparagraph shall not apply to passenger cars which constitute the taxable person's stock in trade nor to those which are strictly necessary for the exercise of the business activity, nor to the goods and services connected with these cars, where their non-business use is less than 10%.

"Passenger car" means any road vehicle (including any trailer) other than one which, by its design and equipment, is intended solely for the transport of goods or is intended for industrial or agricultural use or has a seating capacity of more than nine persons including the driver.

"Expenditure relating to passenger cars" means expenditure on the purchase, including under contracts to make up work and the like, manufacture, importation, leasing or hire, use, modification, repair or maintenance, and expenditure on supplies for or services performed in relation to such vehicles.

2. Value added tax charged on expenditure on accommodation, food or drink, other than that incurred by a taxable person in relation to the supply for consideration by that taxable person of accommodation, food or drink shall be deductible at the rate of 50%.

3. The provisions of paragraphs 1 and 2 shall apply without prejudice to Article 17(5).

Article 17b

Exclusions from the right of deduction

1. The following expenditure is excluded from the right of deduction:

a) expenditure relating to passenger cars as defined in Article 17a(1) in respect of which the business use is less than 10%.

(b) expenditure on luxuries, amusements or entertainment.

Article 17c

Transitional provision

The provisions referred to in Articles 17a and 17b apply only to the value added tax which became chargeable after the said provisions entered into force in that Member State.

(3) The following third and fourth subparagraph are added to Article 20(3):

"The adjustment referred to in the first subparagraph shall also be applied in the case of the resale of a passenger car in respect of which the purchase, manufacture or importation had been subject to Value Added Tax which the taxable person was authorised to deduct in accordance with the first subparagraph of Article 17a(1).

The adjustment referred to in the previous subparagraph may in no circumstances exceed the amount of the tax obtained by applying the rate of tax in force for passenger cars to the taxable amount of the resale."

(4) Article 28f is modified as follows:

a) The opening sentence of Article 17(3) is replaced by the following:

"Subject to paragraph 3a, Member States shall also grant every taxable person the right to the deduction or refund of the value added tax referred to in paragraph 2 in so far as the goods and services are used for the purposes of:"

b) Paragraphs 3a, 3b and 3c are inserted in Article 17:

"3a In so far as the goods and services are used to make taxed transactions or transactions referred to in paragraph 3, Member States shall also grant every taxable person the right to deduct:

(a) value added tax due or paid in a Member State where that taxable person is not established in respect of goods or services supplied or to be supplied to him by another taxable person;

(b) value added tax due or paid in respect of goods imported goods into a Member State where that taxable person is not established;

When the taxable person is identified for VAT purposes in several Member States, the right to the deduction shall be granted in the Member State where the taxable transactions or the transactions referred to in paragraph 3 for which the goods or services are used are carried out. In so far as the goods and services are used in the general framework of the taxable person's economic activities and it is not possible to attribute them to taxable transactions or transactions referred to in paragraph 3, the right to deduct shall be granted in the Member State where the taxable person has established the seat of his economic activity.

3b For the purposes of applying the previous provision, 'a taxable person not established in the territory of country' shall mean a taxable person who has had in that country neither the seat of his economic activity nor a fixed establishment from which the goods or services are supplied nor, if no such seat or fixed establishment exists, his domicile or normal place of residence, and who has supplied no goods or services deemed to have been supplied in that country, with the exception of:

a) transport services and services ancillary thereto exempted pursuant to Article 14(1)(i), Article 15 or Article 16(1) B, C and D;

b) supplies of goods and services to a person who has been designated as the person liable to pay the tax in accordance with Article 21(1)(a);

c) supplies of services in cases where the tax is due solely by the person to whom the services are supplied in accordance with Article 21(1)(b).

When the VAT which the taxable person is authorised to deduct pursuant to paragraph 3a is expressed in a currency other than that of the Member State where the right to deduct arises, and provided that one of the two States issuing these currencies does not use the Euro as national currency, the exchange rate shall be determined, at the time when the chargeable event takes place, according to the Community provisions in force for calculating the customs value.

For the purposes of applying paragraph 3a and the first and second subparagraphs of this paragraph, Member States shall ensure that a taxable person is not prevented from exercising his right to deduct when he holds an invoice which contains at least all the information listed in Article 22(3)(b)."

3c: The Council, acting in accordance with the procedure provided for in Article 99 of the Treaty, shall adopt measures on the refund system and the administrative-cooperation measures necessary to ensure that the deduction arrangements of paragraphs 3a and 3b function properly."

(c) Article 17(4) is replaced by the following:

"4. The refund of value added tax referred to in paragraph 3 shall be effected to taxable persons who are not established within the territory of the Community, in accordance with the detailed implementing rules laid down in Directive 86/560/EEC.

The taxable persons referred to in Article 1 of Directive 86/560/EEC shall also be considered for the purposes of applying the said Directive as taxable persons who are not established in the Community when, inside the territory of the country, they have only carried out supplies of goods or services to a person who has been designated as the person liable to pay the tax in accordance with Article 21(1)(a).

Directive 86/560/EEC shall not apply to supplies of goods which are, or may be, exempted under Article 28c(A) when the goods supplied are dispatched or transported by the acquirer or for his account."

(5) Article 28h is modified as follows:

The following point (d) is added to Article 22(4):

"(d) In so far as the taxable person exercises a right to deduct which arose under Article 17(3a), the taxable person shall supplement the declaration by a specific document which must show the amount of deductions to be made, broken down by Member State.

The taxable person shall attach a copy of the invoices or import documents to the specific document in order to provide proof of these amounts.

The taxable person shall certify in the specific document provided for in the first subparagraph that he has no value added tax identification number in the Member State where the VAT deductible under Article 17(3a) is due or paid."

Article 2

Directive 79/1072/EEC is repealed with effect from 1 January 1999.

Article 3

1. Member States shall bring into force the necessary laws, regulations and administrative provisions in order to comply with this Directive on 1 January 1999. They shall forthwith inform the Commission thereof.

When Member States adopt these measures, they shall contain a reference to this Directive or shall be accompanied by such reference on the occasion of their official publication. The methods of making such reference shall be laid down by Member States.

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

Article 4

This Directive shall enter into force on the 20th day following its publication in the *Official Journal of the European Communities*.

Article 5

This Directive is addressed to the Member States.

Done at Brussels, 1998

For the Council
The President

Proposal for a
COUNCIL REGULATION (EC)
on verification measures, measures relating
to the refund system and administrative cooperation measures
necessary for the application of Directive 98/xxx/EC

98/0210 (CNS)

(presented by the Commission)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 99 thereof,

Having regard to the proposal from the Commission,[1]

Having regard to the opinion of the European Parliament,[2]

Having regard to the opinion of the Economic and Social Committee,[3]

Whereas amending the Sixth Directive in such a way as to enable a taxable person to deduct the VAT due or paid in a Member State in which he is not established requires the introduction of a bilateral refund and compensation system in respect of debts between Member States in order to allow the Member State in which, pursuant to Article 17(3a) of the Sixth Directive, deduction is carried out to request a refund of the amount in question from the Member State in which VAT was due or paid;

Whereas the practical operation of such a debt refund and compensation system requires the application of common rules, in particular with regard to exchange rates, the date on which the balance between two Member States is to be determined and the date on which the balance has to be paid to each other;

Whereas Member States may enter into bilateral agreements laying down special provisions between contracting Member States which derogate from these rules as regards the deadline for payment of the balance and the volume of documents to be transmitted for verification purposes;

Whereas cooperation between Member States in the area of control has not yet reached the quality or extent needed to permit an effective verification of the deduction made pursuant to Article 17(3a) of the Sixth VAT Directive (77/388/EEC); whereas temporary provision for additional verification procedures is therefore necessary;

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1 OJ C

2 OJ C

3 OJ C

Whereas these additional procedures reduce the simplification effect resulting from the amendment, by Council Directive 98/xxx/EC of xx/xx/1998, of the rules governing the right to deduct the VAT paid in a Member State where the taxable person is not established; a regular review of the procedures must take place to assess their need and justification;

Whereas the Commission will present to the Council before the end of the second year in which these procedures are applied a report on the need and justification for them and on the development of cooperation between Member States in the area of verification, where appropriate accompanied by proposals rescinding the additional procedures; whereas, to this end, Member States will supply the Commission with the necessary information;

Whereas the Commission, assisted by the Standing Committee on Administrative Cooperation in the field of Indirect Taxation, set up by Article 10 of Council Regulation (EEC) No 218/92 of 27 January 1992, should be given the power to adopt measures implementing this Regulation;

HAS ADOPTED THIS REGULATION:

Article 1

Purpose

This Regulation establishes the verification procedures, the rules and procedures relating to the refund system and the administrative cooperation procedures necessary for the application of Directive 98/xxx/EC.

Article 2

Definitions

1. For the purposes of this Directive:

- "Member State of deduction" means the Member State in which a taxable person exercises his right to deduct pursuant to Article 17(3a) of the Sixth Directive;

- "Member State of purchase" means the Member State in which the VAT eligible for deduction pursuant to Article 17(3a) of the Sixth Directive was due or paid.

2. Each Member State shall notify the other Member States and the Commission of the authorities appointed for the purposes of applying this Regulation.

Article 3

Verification by the Member State of deduction

1. The Member State of deduction shall, at the time when the periodic return, together with the specific document and copies of invoices or import documents, is submitted, carry out an initial verification to ensure that the limits on the right to deduct and, where appropriate, the deductible proportion have been correctly applied. In addition, it shall check whether the nature and type of expenditure gives rise to the presumption that the taxable person is carrying out taxable transactions on the territory of the Member State of purchase for which he is liable to pay tax.

2. Where irregularities are detected, the Member State of deduction shall forthwith carry out the necessary adjustments.

3. Where the Member State of deduction considers that expenditure shown by the taxable person indicates that taxable transactions are being carried out on the territory of the Member State of purchase, the Member State of deduction shall immediately inform that Member State thereof.

Article 4

Compensation between Member States

1. The Member State of deduction has the right to obtain from the Member State of purchase a refund of the amount of VAT deducted, with due account being taken of the adjustments resulting from the verification referred to in Article 3.

2. Each Member State shall inform the other Member States of the total amount, in Euro, of the VAT to be refunded pursuant to paragraph 1. This shall be done not later than 31 July of each year in respect of VAT deducted in returns submitted during the first half of the year in question, and not later than 31 January of each year in respect of VAT deducted in returns submitted during the second half of the previous year.

3. The exchange rate shall be determined on 31 January and on 31 July of each year, as appropriate, in accordance with the Community provisions in force for calculating customs value.

Article 5

Provisional balance

On the basis of the information transmitted pursuant to Article 4(2), Member States shall, on 31 January and 31 July, bilaterally decide the provisional balance between refund amounts payable and refund amounts receivable.

Article 6

Exchange of information

1. The Member State of deduction shall inform the Member State of purchase of the taxable transactions that may present a risk of evasion in respect of which VAT is deducted pursuant to Article 17(3a) of the Sixth Directive. Such information shall be sent not later than the fifteenth day of the month following the month in which the periodic return, together with the specific document and copies of invoices or import documents, is submitted.

2. The criteria for selecting the transactions that have to be notified shall be laid down in accordance with the procedure provided for in Article 10.

3. However, Member States may agree bilaterally on additional criteria.

4. Member States shall supply the Commission with any information concerning the use made of information exchanged which the Commission deems necessary for drawing up the report provided for in Article 12 below.

Article 7

Verification by the Member State of purchase

Within three months of receiving the information referred to in Article 6, the Member State of purchase shall inform the Member State of deduction of the cases where it has detected irregularities as a result of which it has established either that the taxable transaction was fictitious or that the transaction was carried out as part of the taxable person's taxable activities on its territory.

In such situations, the taxable person may not exercise the right to deduct laid down by Article 17(3a) of the Sixth Directive.

Article 8

Time limit for modifying the provisional balance

1. Provided that the three-month deadline referred to in Article 7 is met, the VAT amount relating to transactions in respect of which the Member State of purchase has detected irregularities shall be excluded from the amount which the Member State of deduction can obtain as a refund pursuant to Article 4.

2. Once the three-month deadline referred to in Article 7 has passed, the Member State of deduction may no longer request a change in the amount to be refunded.

Article 9

Payment of the balance between Member States

1. The final balance shall be determined on 30 April and 31 October. Where the provisional balance has already been determined, it shall be adjusted by setting off against it the VAT relating to any irregularities detected on the basis of the procedure provided for in Articles 6 and 7.

2. The final balance that a Member State must refund to another Member State shall be paid not later than 15 May in respect of final balances determined on 30 April and not later than 15 November in respect of final balances determined on 31 October.

3. Payment of the balance shall be made in Euro.

4. However, Member States may, by bilateral agreement, derogate from this Article. They may, *inter alia*, agree on a different deadline for payment of the balance or allow payment of the balance to be carried forward in certain circumstances.

Article 10

Implementing measures

1. The measures necessary for the implementation of this Regulation shall be adopted by the Commission in accordance with the procedure provided for in Article 10(3) and (4) of Council Regulation (EEC) No 218/92 of 27 January 1992.

2. To this end, the Commission shall be assisted by the Standing Committee on Administrative Cooperation in the field of Indirect Taxation set up under Article 10(1) of that Regulation.

Article 11

Communication of bilateral measures

Member States shall inform the Commission of any bilateral agreements entered into in the fields of Articles 6 and 9.

Article 12

Report

The Commission shall present to the Council, before the end of the second year of application of the verification measures referred to in Article 6 and 7, a report on the need and justification for them and on the development of cooperation between Member States in the area of verification, where appropriate accompanied by proposals repealing the said measures.

Article 13

Final provisions

This Regulation shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Communities.

It shall apply from 1 January 1999.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, [date]

For the Council
The President

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