



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 03.04.1996
COM(96) 144 final

Proposal for a

COUNCIL DECISION

**authorizing the Netherlands to apply a measure derogating
from Article 11 of the Sixth Council Directive (77/388/EEC)
on the harmonization of the laws of the Member States relating
to turnover taxes**

(presented by the Commission)

EXPLANATORY MEMORANDUM

By registered letter sent to the Secretariat-General of the Commission on 13 August 1993, the Dutch Government, acting on the basis of Article 27 of the 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 assessment¹, requested authorization to apply, in respect of the letting of immovable property, a measure derogating from Articles 11 and 20 of that Directive.

In accordance with Article 27(3) of the Directive, the other Member States were informed of the Netherlands' request by letter dated 13 September 1993.

As part of its efforts to combat tax avoidance, the Dutch Government requested authorization to introduce the following arrangements into its legislation:

- the extension to 20 years of the adjustment period for the deduction of VAT in the case of immovable property, which is set at 10 years by Article 20(2) of the Sixth Directive;
- the introduction of a minimum taxable amount for the taxable letting of immovable property;
- the introduction of a minimum taxable amount for the establishment of limited rights in respect of immovable property.

The Commission took the view that these measures would constitute too absolute a derogation from what is a key provision of the common system of value added tax, namely Article 11 of the Sixth Directive, and would be disproportionate to the aim pursued.

Since it had serious objections to the measures, the Commission, acting under Article 27(4) of the Sixth Directive, requested on 11 November 1993 that the matter be raised by the Council.

The Council Working Party on Financial Questions began discussing the Dutch Government's request at its meeting of 13 October 1994.

The Dutch authorities subsequently indicated that they wished to amend their request for a derogation, retaining only the request relating to the introduction of a minimum taxable amount for the establishment of rights *in rem* in respect of buildings or parts thereof and the land on which they stand. In addition, the measure would apply only to cases where the party acquiring the rights *in rem* is a non-taxable legal person or a taxable person carrying on exempted activities that do not entitle him to deduct VAT. Private individuals and taxable persons carrying on activities which entitle them to deduct VAT would thus be excluded from the scope of the derogation.

¹ OJ No L 145, 13.6.1977, p.1. Directive as last amended by Directive 95/7/EC (OJ No L 102, 5.5.1995, p. 18).

It has been found in practice that tax devices for evading payment of some of the VAT normally due in respect of immovable property are being set up, chiefly for the benefit of non-taxable legal persons or taxable persons carrying on activities which do not entitle them to deduct VAT.

The practices that the Dutch authorities wish to combat by means of the special measure usually follow the pattern set out below. A non-taxable legal person (e.g. a municipality) or a taxable person engaged exclusively in activities which do not entitle him to deduct VAT (e.g. a school) intends to buy or build new premises. Where this person (referred to below as person "A") carries out the operation himself, he has to bear the full amount of the VAT due either on the purchase transaction or on the building works.

To avoid this tax burden, the building in question is acquired by another legal person (referred to below as person "B"). The only economic activity of B is to establish rights *in rem* in respect of the immovable property on behalf of A; B's activity entitles him to deduct all the VAT due on the purchase transaction or the building works.

Once the adjustment period for VAT deducted in respect of investments in immovable property has expired, B sells the building freehold to A. The sale then qualifies for exemption from VAT under Article 13(B)(g) of the Sixth Directive.

The tax avoidance therefore takes place when the contracting parties agree on an abnormally low price for the establishment of rights *in rem*, which attracts VAT, and compensation for this abnormally low price in the form of a high price for the freehold sale of the property, which is exempt from VAT. This enables A, the final purchaser, to have the use of a building and become the owner after a certain length of time while reducing the tax burden on the property considerably.

For the establishment of rights *in rem* in respect of buildings or parts thereof and the land on which they stand, such rights being regarded as tangible property in accordance with Article 5(3) of the Sixth Directive, the planned measure is therefore aimed at introducing a minimum taxable amount equal to the open market value of the rights. However, the VAT would be calculated on the basis of the minimum taxable amount only in cases where the administration could prove that the taxable amount determined in accordance with the normal rules laid down in the Directive (i.e. on the basis of the price agreed between the contracting parties) is abnormally low in comparison with the price that could be obtained for the property in a transaction between independent parties operating at arm's length.

But application of this measure cannot be restricted to cases in which rights *in rem* are established in respect of new buildings or parts thereof as referred to in Article 4(3)(a) of the Sixth Directive. This is because, availing itself of the possibility open to it under Article 13(C)(b) of the Directive, the Netherlands allows taxable persons to opt for taxation of the establishment of rights *in rem* in respect of buildings or parts thereof and the land on which they stand other than those referred to in Article 4(3)(a).

The Commission takes the view that the measure planned by the Netherlands is indeed a measure aimed at preventing tax avoidance within the meaning of Article 27 of the Directive. It also takes the view that, since the derogation should apply only in limited cases (where it is proven that the price agreed is abnormally low), it is proportionate to the aim pursued.

The Commission considers it appropriate for the Netherlands to be authorized to apply the planned special measure given its exceptional nature. Nevertheless, in order to enable the measure to be assessed once it has been applied for a certain period of time, the authorization should be granted only until 31 December 1998.

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community,

Having regard to the 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 assessment¹, and in particular Article 27 thereof,

Having regard to the proposal from the Commission,

Whereas, pursuant to Article 27(1) of the Sixth Directive, the Council, acting unanimously on a proposal from the Commission, may authorize any Member State to introduce special measures for derogation from that Directive, in order to simplify the procedure for charging the tax or to prevent certain types of tax evasion or avoidance;

Whereas, by registered letter to the Commission dated 13 August 1993, the Netherlands requested authorization to introduce a measure derogating from Articles 11 and 20 of the Sixth Directive;

Whereas, in accordance with Article 27(3) of the Sixth Directive, the other Member States were informed on 13 September 1993 of the request made by the Netherlands;

Whereas, since it had serious objections to the Dutch Government's request, the Commission, acting under Article 27(4) of the Sixth Directive, requested by letter dated 11 November 1993 that the matter be raised by the Council;

¹ OJ No L 145, 13.6.1977, p.1. Directive as last amended by Directive 95/7/EC (OJ No L 102, 5.5.1995, p. 18).

Whereas the Dutch Government subsequently amended its request, reducing considerably the scope of the special measures derogating from the common system of value added tax;

Whereas the request is confined to a measure introducing a minimum taxable amount for the establishment of rights *in rem* in respect of buildings or parts thereof and the land on which they stand where the party acquiring the rights is a non-taxable legal person or a taxable person carrying on exempted activities that do not entitle him to deduct VAT;

Whereas under Article 5(3) of the Sixth Directive the Netherlands considers the establishment of rights *in rem* to be a supply of goods;

Whereas, availing itself of the possibility open to it under Article 13(C)(b) of the Sixth Directive, the Netherlands allows taxable persons to opt for taxation of the establishment of rights *in rem* in respect of buildings or parts thereof and the land on which they stand other than those referred to in Article 4(3)(a) of the Directive; whereas the derogation therefore also relates to such transactions;

Whereas, by taking the open market value as the taxable amount for certain supplies, the proposed measure derogates from Article 11(A)(1)(a) of the Sixth Directive, which provides that the taxable amount for supplies of goods is to be everything which constitutes the consideration which has been or is to be obtained by the supplier from the purchaser or a third party for such supplies, including subsidies directly linked to the price of such supplies;

Whereas the derogation is aimed at preventing the tax avoidance which takes place when the contracting parties agree on an abnormally low price for the establishment of rights *in rem*, which attracts VAT, and compensation for this price in the form of a high price for the freehold sale of the property, which is exempt from VAT;

Whereas the special measure is to apply only in cases where the administration is able to prove that the taxable amount determined in accordance with Article 11(A)(1)(a) of the Directive is abnormally low; whereas the administration may not act on mere presumptions, and the parties concerned must be allowed to adduce evidence to the contrary where they dispute the level of the open market value established by the administration;

Whereas, given the limited scope of the derogation, the special measure is proportionate to the aim pursued;

Whereas the authorization is granted temporarily, thereby enabling the effects of the measure to be assessed once it has been applied for a certain period of time;

Whereas the derogation in question has no adverse impact on the European Community's own resources accruing from value added tax,

HAS ADOPTED THIS DECISION:

Article 1

By way of derogation from Article 11(A)(1)(a) of Directive 77/388/EEC, the Netherlands is hereby authorized to take the open market value, as defined in Article 11(A)(1)(d) of the Directive, as the taxable amount for the establishment of rights *in rem* in respect of buildings or parts thereof and the land on which they stand, considered to be tangible property in pursuance of Article 5(3) of the Directive, where the following two conditions are met:

- the taxable amount determined in accordance with Article 11(A)(1)(a) of the Directive is abnormally low in comparison with the price that could be obtained for the property in a transaction between independent parties operating at arm's length;
- the party acquiring the rights *in rem* is a non-taxable legal person or a taxable person carrying on exempted activities that do not entitle him to deduct VAT.

Article 2

This authorization is granted until 31 December 1998.

Article 3

This Decision is addressed to the Netherlands.

Done at Brussels,

For the Council
The President

ISSN 0254-1475

COM(96) 144 final

DOCUMENTS

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Catalogue number : CB-CO-96-148-EN-C

ISBN 92-78-02238-1

Office for Official Publications of the European Communities

L-2985 Luxembourg