CONSULTATION OF THE ECONOMIC AND SOCIAL COMMITTEE

on the proposal for a sixth Council Directive on the harmonization of the legislation of the Member States concerning turnover taxes— common system of value added tax : uniform basis of assessment

A. REQUEST FOR AN OPINION

At its 252nd meeting held on 23 and 24 July 1973, the Council decided, in accordance with the provisions of Article 100 of the Treaty establishing the European Economic Community, to consult the Economic and Social Committee on the above proposal for a Directive.

The request for an Opinion was sent by the President of the Council to the Chairman of the Economic and Social Committee on 25 July 1973.

B. TEXT WHICH WAS THE SUBJECT OF THE CONSULTATION

The text which was the subject of the consultation was published in *Official Journal of the European Communities* No C 80 of 5 October 1973.

C. OPINION OF THE ECONOMIC AND SOCIAL COMMITTEE

At its 117th plenary session held in Brussels on 31 January 1974 the Committee adopted its Opinion on the text referred to under B by a majority, with three dissenting votes and one abstention.

The text of the Opinion is as follows :

THE ECONOMIC AND SOCIAL COMMITTEE,

Having regard to the Treaty establishing the European Economic Community, and in particular Articles 99, 100 and 198 thereof ;

Having regard to the letter of 25 July 1973, in which the President of the Council of the European Communities requested an Opinion from the Economic and Social Committee on the proposal for a sixth Council Directive on the harmonization of legislation of Member States concerning turnover taxes — common system of value added tax : uniform basis of assessment ;

Having regard to its Rules of Procedure and in particular Article 22 thereof ;

Having regard to the Decision taken by its Bureau on 26 September 1973 entrusting the Section for Economic and Financial Questions in the first instance, and the Sections for Industry, Commerce, Crafts and Services, and Agriculture on a supplementary basis, with the preparation of an Opinion and a report on the matter ;

Having regard to the supplementary Opinions of the Sections for Industry, Commerce, Crafts and Services and Agriculture ;

Having regard to the Opinion delivered by the Section for Economic and Financial Questions at the ninth meeting on 8 January 1974 ;

Having regard to the report presented to the Section by Mr Peyromaure-Debord-Broca, Rapporteur, and Mr Fredersdorf, Co-rapporteur ;

Having regard to its discussions at its 117th plenary session on 30 and 31 January 1974, meeting of 30 January 1974,

HAS ADOPTED THE FOLLOWING OPINION

by a show of hands, under Article 45 of the Rules of Procedure, by a majority, with three dissenting votes and one abstention :

The committee records its satisfaction at being consulted and at being able to keep the progressive introduction of a unified Community VAT system under review.

I. GENERAL COMMENTS

Objectives

The committee has taken note of the objectives pursued by this Directive, namely:

1. to create a comparable base as between the States by harmonizing the assessment basis, in pursuance of the Council Decision of 21 April 1970 (Article 4), which provided for replacement of the financial contribution from each Member State by the Communities' own resources. These own resources include a tax component — a levy on each Member State calculated by applying a rate of not more than 1 % to a basis of assessment determined in a uniform manner for the Member States according to Community rules;

2. to advance towards economic integration which, in the field of indirect taxation, must lead, at a later date, to complete harmonization, including harmonization of rates;

3. to arrive thus at the abolition of intra-Community tax frontiers, this and the previous operation being necessarily concomitant.

Contents of the Directive

The committee recognizes that the Directive is designed to:

1. remove certain differences which exist between the laws of Member States: The first two Directives allowed a certain degree of flexibility in order to ease the establishment of VAT in all the Member States, which has now been completed in both the founding and the new Member States;

2. harmonize the fields of application;

3. standardize the lists of exemptions;

4. ensure that taxable amounts are identical;

5. ensure, whatever the rate may be (reduced rate), the possibility of deduction of tax already paid;

6. harmonize the special schemes for:
   - agriculture: the creation of a flat rate scheme for deduction of tax already paid,
   - small undertakings: exemption from tax and tax relief, simplified rules for applying the normal system,
   - second-hand goods;

7. Set up a Value Added Tax Committee responsible for examining the conditions of application of the tax, interpreting where necessary the rules which have been laid down, ascertaining any deficiencies and proposing solutions.

Nature of the contribution

Harmonization of the basis of assessment enabling the Community to obtain its own resources from each Member State on the basis of a levy amounting to a maximum of 1 % does in fact appear to be an equitable means of apportioning the contribution to the Community budget between the Member States.

In virtue of the Council's decisions to date (1970, 1971 and 1972), the present financial contribution paid by the Member States should be replaced by a contribution of a tax nature.

How will the Community tax contribution be funded in each Member State

The committee discussed the question whether the new levy would have to lead to a rise in the rates of taxation in each Member State, since there would otherwise be a corresponding loss of revenue. On this subject, the committee points out that while the principle of this contribution has been established by Council decision, the way in which the Community contribution is to be funded has evidently been left completely to the discretion of the Member States.

Examination of other formulae

It was also asked why the harmonization of VAT should not be extended by harmonizing the rates instead of the bases of assessment. The answer to this question is that harmonization of the rates before harmonization of the bases of assessment would present a lengthy problem of apportionment between direct and indirect taxes which could only be effected very gradually in the various States, let alone at Community level. Furthermore, absence of harmonization of rates is offset by the adoption of a single levy on a harmonized basis of assessment.

The committee wishes to point out that harmonization of rates before harmonization of the bases of assessment would be illogical, since, technically, harmonization of the bases of assessment must precede harmonization of the rates.

Special schemes

The scheme for small undertakings and the common flat rate scheme for farmers are dealt with in the annexed supplementary Opinions, the former being covered by the Opinion of the Section for Industry, Commerce, Crafts and Services, and the latter by the Opinion of the Section for Agriculture. (See the remarks on Articles 25 and 27 in the specific comments.)

II. SPECIFIC COMMENTS

Article 1

Article 1 provides that Member States must have modified their value added tax systems in accordance with the provisions of the sixth Directive by 1 January 1975.

The committee considers that the difficulties of implementing these provisions will certainly not allow such a brief time limit to be complied with.

For the deadline of 1 January 1975 to be met everything would have had to have been ready and adapted at European level by 31 December 1973, because of the constitutional and legislative requirements which have to be complied with in certain Member States. Moreover, the committee feels that the deadline must be extended to give undertakings a breathing space in view of the fact that (a) the introduction of VAT has entailed for the Member States a difficult information task and an arduous adaptation process which are not yet complete in the Member States that have only introduced VAT quite recently, and (b) small and medium-sized undertakings in particular have had considerable difficulty in getting accustomed to the new system.

Article 4

The problem of whether or not to include building land in the field of application of VAT led to very lengthy discussion within the committee. Both systems exist at present among the Member States and each State appears to be satisfied with the solution it has arrived at, for the reasons given in the report. One solution could be to allow the States freedom of choice. However, this solution is bound to create inequalities between the Member States in respect of the Community tax from which Community resources are obtained, in view of the fact that an important component of the assessment basis would not be harmonized. In the event of such an option being provided, the basis of assessment for the Community levy would therefore have to be re-established notionally in the case of those states which leave building land outside the scope of VAT.

Under Article 4 'each Member State may treat as a single taxable person, persons established in its national territory who are legally independent but bound to one another by financial, economic or organizational relationships'.

But according to this text the 'Organschaft' (single-entity relationship) existing in the Netherlands and Germany would only be maintained until tax frontiers were eliminated. The committee wonders why this time limit has been imposed on a system which is not contrary to tax neutrality.

In addition, the committee requests that the Directive permits Member States in which this system does not exist to use it according to common rules.

The committee asks that the concept of tax deferment, an operation which does not run contrary to tax neutrality, should be definitely accepted in cases to be determined.

The committee considers it essential that the concept of activities carried out by public authorities be defined in an identical manner in all the Member States. (See, for example the comments on Article 14 A (1) (k)).

Article 5

Article 5 defines and lists what should be understood by 'supply of goods'.

1. *Paragraph 1* states that 'all interests or shares giving the holder thereof *de jure* or *de facto* rights of ownership or possession over immoveable property or part thereof' are to be treated as property attracting VAT. The committee requests that this should only apply in the very rare cases where there is an undeniable relationship between the sale of shares and the property in question.

2. The committee opposes the treatment of leasing as a 'supply of goods' (*paragraph 2 (b)*). It feels that the Member States should be free to consider leasing either as a form of rental followed by transfer of a used item of property, or as a contract involving from the moment of its conclusion, a taxable 'supply'. The latter solution, which has been adopted in the proposal for a Directive, means that VAT will have to be paid as soon as supply occurs and cannot be spread over the whole duration of the contract.

The committee wonders why the Member States should not be allowed freedom to choose, since the effect of both formulae on the harmonized basis of assessment as a whole ought to be slight and equality should be ensured in the medium term.

3. If contracts under which commission is payable on purchase or sale (*paragraph 2 (c)*) and contracts to make up work from customers' material (*paragraph 2 (d)*) are treated as supplies, this will considerably extend the assessment basis for VAT in countries such as France, where such transactions are considered as a supply of services.

Such an extension of the basis of assessment should only be applied if the one-month time lag for deductions, where it exists, as in France, has been abolished beforehand in accordance with Article 18 (2) of the proposal for a Directive.

Article 12

Article 12 defines the taxable amount.

Paragraph A (1) (b) introduces the concept of 'open market value' of goods or services where the price expressed as a sum of money is not the sole consideration for the supply of goods or services (own consumption of goods and services, barter transactions etc.).

The committee unanimously recognized that the 'open market value' is a theoretical concept which is difficult to define, so that it will doubtless lead to disputes, especially in view of the particular difficulties involved in the self-supply of land (Article 5 (3)).

However, no alternative solution is suggested.

The committee proposes that the concept of 'open market value' should not be applied in all cases such as, for example, delay in payment where the price agreed upon by the interested parties is known.

Paragraph A (3) lists what the taxable amount is not to include.

The committee wonders whether it would not be possible to exclude from the basis of assessment the sums due as penalties for delays or other irregularities in the performance of the obligations of the seller or the party who placed the order.

The committee proposes that the sums paid out to gamblers by automatic machines also be excluded from the basis of assessment.

Paragraph C (1) leaves it to the Member States to lay down the rules to be applied in the case of goods or services which remain unpaid or are cancelled. This is regrettable, for some countries, such as France, have adopted provisions which in effect mean that unpaid transactions are partially taxed. The volume of operations of this kind, especially in periods of recession, should have warranted Community provisions binding on the Member States in keeping with the principle of neutrality on which value added tax is based.

Article 13

Article 13 sets out the principles applicable to value added tax rates and basically incorporates the provisions of Article 9 of the second Directive.

1. **The reduction of the number of rates**

On this matter it is regretted that, while harmonization of the rates is deferred and their amounts can be varied, no attempt has been made to reduce their number by, for example, prohibiting the creation of new rates after 1 August 1973.

On the other hand, it must be pointed out that one Member State, Denmark, only has one rate, whereas, according to the proposal for a Directive, it could have two or three. Denmark should not be forbidden to introduce new rates, as this would be contrary to a sound harmonization policy.

The committee notes that the Commission is making a study of proposals concerning the number of rates to be applied.

2. Article 13 (3) provides that each reduced rate 'shall be so fixed that the amount of value added tax resulting from the application thereof shall be such as in the normal way to permit the deduction therefrom of the whole of the value added tax deductible under Article 17'. This is an indirect way of ensuring the future elimination of the zero rating.

The committee believes that it would be premature at this stage to take a decision on whether zero-rating of certain goods and services should be allowed in the future. That decision should be made in the light of the circumstances at the time when the charging of tax on imports and the remitting of tax on exports in trade between Member States are abolished.

The committee furthermore regrets that the Directive is not more precise on the relationship which should exist between the standard rate and the reduced rate.

Article 14

Article 14 lists the exemptions within the territory of a country.

1. **Exemption of trade unions, professional organizations, churches, etc.**

The committee considers that it would be preferable to make provision for exemption of trade unions and professional organizations in so far as they do not engage in competitive operations — such as commercial transactions or the giving of advice involving

payments separate from the general contributions and varying according to the extent of the services rendered.

This exemption would be particularly appropriate as regards trade union contributions, since otherwise trade unions' income from contributions would be reduced by the amount of the tax without the members being able to deduct this tax, as they themselves are not taxable persons.

It is pointed out that trade unions and professional organizations ought to be able to renounce exemption by opting for VAT in order to recover VAT already paid (taxes on immoveables and office equipment).

The above remarks also apply to churches and equivalent institutions in so far as their activities are not governed by public law and they are not already exempted for that reason.

2. Exemption of invalids

The following provision should be added to Article 14 on exemptions within the territory of a country :

Member States shall exempt deliveries of motor vehicles imported or acquired for use as a means of personal transport for persons who are at least 50 % permanently disabled.

This exemption shall apply in the manner and within the limits laid down by each Member State, until uniform rules are adopted by the procedure laid down in Article 31.

Such exemption may take the form of reimbursement of the tax.

3. Exemption of bank transactions

The making of advances and the granting of credit are exempted under Article 14 B (j).

There are two schools of thought here :

— certain members propose that all bank transactions including the making of advances and the granting of credit should be taxable ;

— others consider that the making of advances and the granting of credit should be exempted.

The disadvantage of this second system for banks is that the possibilities of deduction of tax already paid are greatly limited.

Furthermore, in the context of the proposal for a Directive, all the members feel that it would be advisable for define the exact scope of the concepts contained in Article 14 B, and in particular subparagraphs (f), (h) and (j).

The committee is also agreed that it would like to see the disappearance of specific taxes on turnover in the banking sector where they still exist.

4. Other observations

Paragraph A (1)(a)

Telecommunications services and related services provided by public authorities should not be exempted.

Paragraph A (1) (k)

The committee wonders why state radio and television is not exempted from VAT when it engages in the same activities as theatres, cinema clubs, concerts and other entertainment, which are exempted. Logically, only the receipts from radio and television advertising should be taxed. Tax neutrality should at all events be respected at both sectoral and regional level.

Paragraph B (d) (2)

The committeee wonders why a lessor of agricultural property should not be allowed to opt for VAT if the lessee is a taxable person.

Article 16

The committee requests the Commission to make sure that paragraph 10 does, in fact, lead to the exemption of the transmission of 'know-how' and data-processing information, market surveys, checking, maintenance and inspection services as well as all other similar services.

As regards paragraph 12, the Committee wonders about the justification of such a comprehensive exemption for diplomatic and consular missions and international organizations recognized as such by the host Member State, since this is fundamentally incompatible with VAT's character of a general tax on consumption.

The phrase 'by sea or air' should be deleted from point 13 (c), leaving the following wording :

'(c) international passenger transport, subject to the time limit set in Article 28.'

In addition the committee feels that provision should be made for suspension of liability for payment of value added tax in the case of purchases made by undertakings which are mainly engaged in exporting.

Article 17

Article 17 defines the existence and scope of the right to deduct.

Paragraph 4

The Committee welcomes the fact that the Directive provides that each Member State will have to refund to taxable persons established in another country the VAT invoiced to them for goods and services supplied in the Member State.

However, some members would like it to be possible for applications to be made in respect of credits of 50 units of account and over, instead of 100.

In addition, the committee requests that the refunding procedure be standardized.

The committee draws the Commission's attention to the economic consequences of a practice whereby a supplier in a Member State would invoice that State's VAT to his customer in another Member State. In this case there would be cumulative taxation with all the consequences this may entail, especially for the consumer in the country of destination of the supplies.

Paragraph 6

The committee notes that, since VAT is a tax on consumption imposed on products and services with a view to avoiding double taxation, to achieve this goal it is necessary to allow deduction of the VAT levied on all elements of the cost price. Any restriction of the right to deduct prevents the tax from being neutral and creates distortions in competition.

Logically, the system of VAT deductions should be brought into line with the provisions governing industrial and commercial profits. In other words, the VAT imposed on all goods and services which are necessary for operations and qualify as deductions in respect of industrial and commercial profits (commercial vehicles, supplies to social services, transport, hotels, etc.) should be deductible.

The committee considers that the provisions governing the cases in which VAT is not to be deductible will present problems because of their complexity.

The committee deplores, moreover, the vagueness of the expressions 'expenditure on luxuries' and 'entertainment expenditure' used in the Directive, and trusts that the VAT Committee will define them more precisely, in so far as this is possible.

Article 18

Article 18 defines the rules for exercising the right to deduct.

Paragraph 2

The committee approves the principle of immediate deduction, which precludes the deduction time-lag found in some countries (e.g. France).

On the other hand, the committee regrets the fact that the right to deduct is to lapse on 31 December of the year following that in which the deduction should have been made and proposes that this period be extended.

It would be necessary in the case of checks for the taxpayer's right to deduct to be exercisable over the same period as the authorities' right to increase the tax.

Paragraph 3

As regards tax credit, the committee feels that the periods for refund should be shortened considerably.

Article 21

This Article defines persons liable for payment of tax.

In paragraph 1 (a), the agent of the taxable person should not be placed on the same footing as the taxable person himself, and the committee considers that the wording should be amended by replacing 'and agents' by 'and, where appropriate, agents'.

Article 22

Article 22 deals with assessment of the amount of tax to be paid and liability for payment of the tax.

The committee notes that there are problems in the translation of the different concepts in paragraphs 1 and 2. These concepts are clear in five languages but lead to confusion in the German text. In this text, the word 'Festsetzung' should always be used.

Article 23

Article 23 determines the obligations of persons liable for payment under the internal system.

Paragraph 3 (c) states that 'the invoice shall be issued within 30 days following the chargeable event'.

This obligation to invoice within a certain time limit, which does not exist in countries where the chargeable event and liability for tax coincide, derives precisely from the fact that these two factors are separated in the proposal for a sixth Directive.

The Committee agrees:

— that it is a normal thing to fix a time limit for invoicing;
— that this time limit should nonetheless be extended.

Article 25

In principle, the committee is able to accept the special scheme for small undertakings described in Article 25, since Member States after all retain the possibility of introducing special schemes adapted to the situation of small undertakings in their country.

The committee requests that the turnover criteria applied by the Commission be increased and agrees that the new figures adopted could be periodically adjusted in line with the trend in the cost of living. The objective is to allow small- and medium-sized undertakings to be progressively included in the general common VAT system.

Article 26

Article 26 proposes a novel system for taxing second-hand goods. This is approved by the committee ; it avoids the cumulative taxation of second-hand goods which still exists in many countries.

Article 27

The committee approves in principle the Commission's proposals the aim of which is to facilitate the progressive integration of the entire agricultural sector in the normal VAT system.

However, account should be taken of the situations in the various Member States and of the specific difficulties of the agricultural sector, which can only be solved over a long period. Farmers must be left the right of choice in view of the fact that changeover from the flat-rate to the normal scheme must be undertaken very gradually, within the framework of the progress of common policies in other sectors, and particularly of the achievement of economic and monetary union.

Flat-rate taxation must be neutral so on balance it must not work to the advantage or disadvantage of farmers.

In addition, the committee asks the Commission to amend paragraph 12 (a), first and second indents, to avoid the risk of distortions to the disadvantage of industrial undertakings processing farm products, which could be subject to the ordinary tax system, whereas farmers who carry out processing activities would be subject to the flat-rate system.

Article 28 (1)

The phrase 'by sea or air' should be deleted from the second subparagraph leaving the following wording :

'The Commission shall in due course make to the Council proposals concerning the tax scheme to be applied from 1 January 1977 to international passenger transport.'

Articles 29 to 31

Value Added Tax Committee.

Article 29

The committee has received the assurance that decisions will only be taken by the VAT Committee after consultation of the representatives of economic and social activities in accordance with a procedure which is still to be determined. Only under this condition does the committee agree with the setting-up, composition and terms of reference to the VAT Committee.

CONCLUSION

The committee recognizes the need to lay down rules for a Community basis of assessment, which is a necessary step towards a new phase in the harmonization of the Community VAT system.

The committee also recognizes the need for this measure, if it is desired to achieve neutral and balanced apportionment of the contribution to the Community budget through a tax levied on a harmonized assessment basis.

Both in its opinion and in the annexed report, the committee finds that although a major effort has been made to achieve such neutrality, the provisions are not yet ideal and ought therefore to be improved in this respect.

The committee recognizes that the Value Added Tax Committee can help here.

The committee stresses the need for the Directive to be adopted and applied as a whole, so as to avoid — in view of existing laws — significant distortions at Member State level resulting from the application of certain provisions but not all the measures which are a logical consequence thereof.

Done at Brussels, 31 January 1974.

The Chairman
of the Economic and Social Committee

Alfons LAPPAS