such a case the immediate use of the goods for taxable or exempt supplies does not in itself constitute a precondition for its application.

Whether, in a particular case, a taxable person has acquired goods for the purposes of his economic activity within the meaning of Article 4 of the Sixth Directive is a question of fact which must be determined in the light of all the circumstances of the case, including the nature of the goods concerned and the period between the acquisition of the goods and their use for the purposes of the taxable person's economic activity.

A taxable person who uses goods for the purposes of an economic activity has the right on the acquisition of those goods to deduct input tax in accordance with the rules laid down in Article 17 of the Sixth Directive, however small the proportion of business use. A rule or administrative practice imposing a general restriction on the right of deduction in cases where there is limited, but none the less genuine, business use constitutes a derogation from Article 17 of the directive and is valid only if the requirements of Article 27(1) or Article 27(5) of the directive are met.

REPORT FOR THE HEARING
in Case C-97/90 *

I — Legal framework of the main proceedings

Article 4 of the Sixth Directive, contained in Title IV (Taxable Persons), provides as follows:

'1. "Taxable person" shall mean any person who independently carries out in any place any economic activity specified in paragraph 2, whatever the purpose or results of that activity.'

With respect to taxable transactions, Article 6 makes the following provision:

'The following shall be treated as supplies of services for consideration:

(a) the use of goods forming part of the assets of a business for the private use of the taxable person or of his staff or more generally for purposes other than those of his business where the value added tax on such goods is wholly or partly deductible.'

* Language of the case: German.

Article 10(1) and (2), contained in Title VII (Chargeable event and chargeability of tax), is drafted in the following terms:

'1.

(a) "Chargeable event" shall mean the occurrence by virtue of which the legal conditions necessary for tax to become chargeable are fulfilled.

(b) The tax becomes "chargeable" when the tax authority becomes entitled under the law at a given moment to claim the tax from the person liable to pay, notwithstanding that the time of payment may be deferred.

2. The chargeable event shall occur and the tax shall become chargeable when the goods are delivered or the services are performed . . . '.

In Title XI, dealing with deductions, Article 17 (Origin and scope of the right to deduct) provides as follows:

'1. The right to deduct shall arise at the time when the deductible tax becomes chargeable.

2. In so far as the goods and services are used for the purposes of his taxable transactions, the taxable person shall be entitled to deduct from the tax which he is liable to pay:

(a) value added tax due or paid in respect of goods or services supplied or to be supplied to him by another taxable person;

. . .

5. As regards goods and services to be used by a taxable person both for transactions covered by paragraphs 2 and 3, in respect of which value added tax is deductible, and for transactions in respect of which value added tax is not deductible, only such proportion of the value added tax shall be deductible as is attributable to the former transactions.

This proportion shall be determined, in accordance with Article 19, for all the transactions carried out by the taxable person.'

The following provision is laid down in Article 18 (Rules governing the exercise of the right to deduct):

'1. To exercise his right to deduct, the taxable person must:

(a) in respect of deductions under Article 17(2)(a), hold an invoice, drawn up in accordance with Article 22(3);

. . .

2. The taxable person shall effect the deduction by subtracting from the total amount of value added tax due for a given tax period the total amount of the tax in respect of which, during the same period, the right to deduct has arisen and can be exercised under the provisions of paragraph 1.'

Article 19 (Calculation of the deductible proportion) contains the following provision:

'1. The proportion deductible under the first subparagraph of Article 17(5) shall be made up of a fraction having:

— as numerator, the total amount, exclusive of value added tax, of turnover per year attributable to transactions in respect of which value added tax is deductible under Article 17(2) and (3),

— as denominator, the total amount, exclusive of value added tax, of turnover per year attributable to transactions included in the numerator and to transactions in respect of which value added tax is not deductible. The Member States may also include in the denominator the amount of subsidies, other than those specified in Article 11A(1)(a).

The proportion shall be determined on an annual basis, fixed as a percentage and rounded up to a figure not exceeding the next unit.

2. By way of derogation from the provisions of paragraph 1, there shall be excluded from the calculation of the deductible proportion, amounts of turnover attributable to the supplies of capital goods used by the taxable person for the purposes of his business ... '.

Article 20 (Adjustments of deductions) is drafted in the following terms:

'1. The initial deduction shall be adjusted according to the procedures laid down by the Member States, in particular:

...

2. In the case of capital goods, adjustment shall be spread over five years including that in which the goods were acquired or manufactured. The annual adjustment shall be made only in respect of one-fifth of the tax imposed on the goods. The adjustment shall be made on the basis of the variations in the deduction entitlement in subsequent years in relation to that for the year in which the goods were acquired or manufactured.

By way of derogation from the preceding subparagraph, Member States may base the adjustment on a period of five full years starting from the time at which the goods are first used.

...

3. In the case of supply during the period of adjustment capital goods shall be regarded as if they had still been applied for business use by the taxable person until expiry of the period of adjustment. Such business activities are presumed to be fully taxed in cases where the delivery of the said goods is

taxed; they are presumed to be fully exempt where the delivery is exempt. The adjustment shall be made only once for the whole period of adjustment still to be covered.

However, in the latter case, Member States may waive the requirement for adjustment in so far as the purchaser is a taxable person using the capital goods in question solely for transactions in respect of which value added tax is deductible.

4. For the purposes of applying the provisions of paragraphs 2 and 3, Member States may:

— define the concept of capital goods,

— indicate the amount of the tax which is to be taken into consideration for adjustment,

— adopt any suitable measures with a view to ensuring that adjustment does not involve any unjustified advantage,

— permit administrative simplifications.

5. If in any Member State the practical effect of applying paragraphs 2 and 3 would be insignificant, that Member State may subject to the consultation provided for in Article 29 forego application of these paragraphs having regard to the need to avoid distortion of competition, the overall tax effect in the Member State concerned and the need for due economy of administration.

6. Where the taxable person transfers from being taxed in the normal way to a special scheme or vice versa, Member States may take all necessary measures to ensure that the taxable person neither benefits nor is prejudiced unjustifiably.'

Article 22, contained in Title XIII, concerning the obligations of persons liable for payment, reads as follows:

'1. Every taxable person shall state when his activity as a taxable person commences, changes or ceases.

2. Every taxable person shall keep accounts in sufficient detail to permit application of the value added tax and inspection by the tax authority.'

Finally, Article 27 of the directive permits the Council to permit the introduction by the Member States of special derogation measures:

'1. The Council, acting unanimously on a proposal from the Commission, may authorize any Member State to introduce special measures for derogation from the provisions of this directive, in order to simplify the procedure for charging the tax or to prevent certain types of tax evasion or avoidance. Measures intended to simplify the procedure for charging the tax, except to a negligible extent, may not affect the amount of tax due at the final consumption stage.

2. A Member State wishing to introduce the measures referred to in paragraph 1 shall inform the Commission of them and shall provide the Commission with all relevant information.

. . .'

II — Facts and written procedure

In 1985, the plaintiff in the main proceedings (hereinafter referred to as 'the plaintiff') purchased a car for DM 20 206.15 on which he paid VAT in the amount of DM 2 828.86. He used that vehicle in 1985 mainly for private purposes and only to the extent of about 8% for business purposes. When he started his own tax consultancy practice on 1 July 1986, the plaintiff brought the vehicle into the business.

On his 1986 declaration of income, he claimed a retrospective deduction of DM 292.98 under Paragraph 15a of the Umsatzsteuergesetz (Turnover Tax Law) (hereinafter referred to as 'the Law') on the acquisition of the vehicle, which he calculated at 6/60ths of the total VAT he had had to pay in respect of the car. The Finanzamt München III (hereinafter referred to as 'the Tax Office') refused to allow such a proportional deduction under Paragraph 15a of the Law. Following the dismissal of the objection lodged by the plaintiff against that decision, he brought an action before the Finanzgericht München (Finance Court, Munich).

The Finanzgericht considered that the prevailing interpretation of Paragraph 15a of the Law according to which capital goods which have been used by a trader, in the first place for his private purposes, then, in the following years, for the purposes of the undertaking has no right whatsoever to a VAT deduction, raises certain doubts in regard to the Sixth Directive, which does not exclude the right to make a deduction.

The national court therefore stayed the proceedings and referred the following questions to the Court of Justice for a preliminary ruling:

'(1) Is Article 20(2) of the Sixth Directive applicable to all capital goods which

(a) were supplied by one taxable person to another taxable person and at some point within a period of five years, including the year in which the goods were acquired, are used by the recipient for the purposes of his taxable transactions,

or is it also necessary for the capital goods in question to have been

(b) used from the time of acquisition for the purposes of the taxable or exempted transactions (business purposes) of the taxable person, or

(c) applied at the time of acquisition for the purposes of the business of the taxable person?

(2) If alternative (b) is correct:

Does the application of Article 20(2) of the Sixth Directive to capital goods which are used by a taxable person both for business purposes and for other, in particular private, purposes (mixed use) depend on their having been used to a specific minimum extent for business purposes in the year in which they were acquired and, if so, how is that minimum to be defined?

(3) If alternative (c) is correct:

Is the application of the capital goods a matter for the taxable person's discretion or does it presuppose that the taxable person

(a) acquires them with the intention of using them for business purposes and, if so, must that use be intended to begin

(i) immediately from the time of acquisition, or

(ii) from some point within the year of acquisition, or

(iii) from some point before the expiry of a period of five years, including the year of acquisition?

and/or

(b) actually uses the capital goods for business purposes and, if so, does it matter whether such use begins

(i) from the time of acquisition, or

(ii) within the year in which the capital goods were acquired, or

(iii) within the period of five years, including the year in which the goods were acquired?

As far as Questions 3(a) and (b) are concerned:

Where the capital goods are used for mixed purposes, must the intended use or actual use (or both) for business purposes attain a specific minimum proportion and, if so, how is that minimum to be defined?'

The order for reference was received at the Court Registry on 10 April 1990.

Pursuant to Article 20 of the Protocol on the Statute of the Court of Justice of the EEC, written observations were submitted by:

— the Government of the Federal Republic of Germany, represented by Ernst Röder and Joachim Karl, Ministerialrat in the Federal Ministry of Economic Affairs, acting as Agents,

— the Government of the French Republic, represented by Edwige Belliard, acting as Agent, and Gérard de Bergues, acting as Assistant Agent, of the Legal Affairs Directorate of the Ministry of Foreign Affairs,

— the United Kingdom, represented by John Collins, Treasury Solicitor, acting as Agent,

— the Commission of the European Communities, represented by its Legal Adviser, Henri Étienne, acting as Agent.

Upon hearing the report of the Judge-Rapporteur and the views of the Advocate General, the Court, by decision of 16 January 1991, decided to assign the case to the Sixth Chamber under Article 95 of the Rules of Procedure and to open the oral procedure without any preparatory inquiry.

III — Written Observations submitted to the Court

The *Government of the Federal Republic of Germany* considers that the provisions of the Sixth Directive concerning deductions must be examined in their general context. A buyer's right to deduct is subject to four fundamental conditions to be found in Article 17(2) and (3) of the directive. The buyer must be a taxable person within the meaning of Article 4. The goods must have been supplied to him in his capacity as a taxable person by another taxable person. The buyer must use the goods for the purposes of his taxable transactions or for transactions of the kind referred to in Article 17(3) and those conditions must be fulfilled at the date relevant for the deduction, in accordance with Article 17(1) and Article 10 of the directive.

Article 17(5) and Article 19 provide that input tax pertaining to the acquisition of goods may be apportioned only if the goods are used both for transactions giving rise to a right to deduct and for transactions not giving rise to such a right. A taxable person has a turnover only in regard to his business activities. The proportion deductible thus applies only if the goods are put to mixed use for activities linked to the undertaking. In so far as the goods are used for non-business purposes, the directive provides for different compensation machinery through the application of Article 6(2)(a) under which the deduction of VAT is ultimately annulled in the light of the subsequent actual use of the goods for private purposes.

On the other hand, if the buyer did not acquire the goods in his capacity as a taxable person, he has no right to deduct tax. In such cases, the private use referred to in Article 6(2)(a) is not taxed because the goods in question give no right to deduction of VAT.

In the German Government's view, where a taxable person uses the goods for business purposes to such an insignificant degree that the acquisition must be regarded from an economic point of view as having been made exclusively for private purposes, Article 17(2) does not permit him to make a deduction in the year in which he acquired the goods even if the taxable person allocates the goods to his business the following year and uses them for business purposes. A contribution of private property of that sort does not fulfil the conditions for a deduction because the condition that the goods should have been supplied by another taxable person is lacking.

Article 17(2) does not make it possible to deduce clearly the minimum proportion of private use of the goods which there must be in order to obtain a deduction of the whole of the VAT paid. In the German Government's view, if the proportion of business use — as a fraction of total use — is so insignificant that it is at most of minimal economic significance, it must be presumed that the acquisition was made exclusively for purposes not connected with the undertaking, with the consequence that no deduction will be possible. In keeping with the economic considerations which govern the VAT legislation, the consequence of minimal use for business purposes cannot, according to Article 17(2), be to permit a complete deduction. It is not possible to define a threshold of minimum use applicable in all cases, but the tax authorities in the Federal Republic of Germany generally work on the basis that an acquisition is exclusively for purposes not connected with the undertaking if the proportion of use for such purposes is equal to more than 90%.

According to the German Government, it is at the time of acquisition that the decisive question in regard to deduction, according to Article 17(2), must be decided, namely whether the goods have or have not been acquired for business purposes. That decision cannot be corrected by Article 20(2) of the directive. That provision must be regarded as being a corrective to Article 17(5) and is consequently applicable only when the purposes for which capital goods are used are changed within the undertaking.

It must be decided on the basis of objective considerations whether the conditions for more than a minimum use for business purposes are fulfilled. It is not possible to say on the basis of the provisions of the directive whether that classification depends on a subjective decision on the part of the taxable person to use the goods for business purposes.

Article 20 applies only to capital goods. There is no objective reason to treat capital goods differently from other kinds of goods. It must be concluded that the goods in respect of which it is proposed to rectify the deduction must already have been capital goods at the date of acquisition. Goods can constitute capital goods only if they are part of the undertaking's property.

With regard to the second question, Article 20(2) does not apply to goods which were used exclusively for private purposes during the year in which they were acquired. If the goods were used to a negligible extent for business purposes during the year in which they were acquired, economic considerations require that such use should be regarded as of no importance.

In the view of the German Government, the third question does not require an answer because it would not answer Question 1(c) in the affirmative.

With regard to the first question, the *French Government* considers that the plaintiff is not entitled to claim a refund of part of the VAT which he paid at the time he purchased his vehicle.

When applying Article 20(2) of the directive, the constituent elements and characteristics of the VAT system should be borne in mind, as set out by the Court in its judgment of 21 September 1988 (Case 50/87 *Commission* v *France* [1988] ECR 4797, paragraphs 13 to 15).

An individual who buys goods for his own consumption has no right to deduct because he is not a taxable person within the meaning of Article 4(1) of the directive.

If the same goods are purchased from the individual by an undertaking for the purposes of its taxable transactions, the undertaking will have no right to deduct because VAT could not have been charged to him by virtue of Article 18(1)(a) of the directive.

Thus, once a final consumer has been involved, the goods are outside economic channels. If the goods return to those channels, they will not be subject to VAT. The taxable person cannot therefore have any right to deduct VAT because none will have been paid.

According to the French Government, the same analysis applies if the goods bought by an individual for his private consumption are allocated the following year to his own undertaking. In the meantime, the goods have left the economic circuit. From that point of view, it makes no difference if the taxable person and the non-taxable person are one and the same.

On the other hand, if the goods were initially acquired from a taxable person and used by him for business purposes, there would in principle be a right of deduction under Article 17 of the directive if they were used in whole or in part for the purposes of taxable transactions. According to Article 6(2), the latter include the use of the goods for the private use of the taxable person, which is assimilated to the supply of services for consideration.

Subsequently, the deduction must be adjusted under Article 20(2) of the directive. However, that adjustment mechanism cannot legally be applied unless the capital goods were acquired by a taxable person acting as such.

That interpretation is supported by Article 17, which provides that the right to deduct arises at the time when the deductible tax becomes chargeable and by Article 18(2), which provides that the taxable person must hold an invoice drawn up in due form. However, Article 22(3) requires the issue of an invoice only if the buyer is a taxable person.

The French Government therefore proposes to answer the first question to the effect that Article 20(2) of the Sixth Directive applies to all capital goods supplied to a taxable person acting in that capacity by another taxable person on condition that they have been used for business purposes from the time of acquisition or manufacture.

Having regard to the answer set out above, the French Government does not consider it necessary to answer the second series of questions.

With regard to the third question, in accordance with Article 17(1), (2) and (5), the deduction of VAT must be permitted as from the date at which the capital goods were acquired by the taxable person in so far as they were allocated to the undertaking and are, for that reason, presumed to be used at least partially for business purposes. Deduction is permitted only for that proportion of the VAT corresponding to taxable transactions.

According to the French Government, even minimal use for business purposes is capable, in principle, of giving a right to a complete deduction, subject to tax being charged on the private use of the goods. However, full deduction causes technical difficulties and gives unjustified advantages if the goods are hardly used at all for business purposes.

It was for that reason that France obtained from the Council, by way of a simplification measure under Article 27(1) to (4) of the Sixth Directive, a decision [1] authorizing it until 31 December 1992 to refuse the right of deduction in respect of expenditure on goods and services in cases where private use of those goods and services accounts for more than 90% of their total use.

As regards Member States having such rules at the time that the directive entered into force, such an exclusion can be based either on Article 17(6) or Article 27(5) of the directive in order to simplify the obligations of undertakings and administrations.

However, the French Government considers that the right to deduct should not be refused if the goods are used subsequently for business purposes. Article 20(2) fixes no minimum for the initial deduction. Thus, the French rules give a right to deduct where

1 — Decision 89/488/EEC of 28 July 1989 authorizing the French Republic to apply a measure derogating from Article 17(2) of the Sixth Directive 77/388/EEC on the harmonization of the laws of the Member States relating to turnover taxes (OJ 1989 L 239, p. 22).

capital goods initially allocated to the undertaking but not used for the purposes of transactions giving a right to deduct are, within the adjustment period, used for the purposes of such transactions.

Thus, a right to deduct two-fifths of the VAT charged on capital goods, on the basis of one-fifth per annum over two years, arises where such goods are allocated to the undertaking for three years and used only after that period for the purposes of the undertaking; similarly, an exempt taxable person who becomes liable to tax in respect of capital goods during the time in which they are in use may have a right to deduct.

Subject to the consultation provided for in Article 29, such an adjustment might not be carried out, in accordance with Article 20(5), having regard to the overall effect of the taxation in the Member State concerned and the need for administrative simplicity, on condition that competition is not distorted.

In the light of the foregoing, the French Government proposes that the Court should answer Question 3(a) to the effect that the allocation of capital goods to an undertaking presupposes the purchase by the taxable person of the capital goods for the purposes of his taxable transactions and that use must be envisaged from the time of acquisition. The answer to Question 3(b) should be that the capital goods must actually be used for business purposes before the end of the five-year period, including the year during which they are acquired. In answer to both Question 3(a) and (b), the Court should rule that, if the intended use does not reach, during any of the five years, the minimum level provided for in national law for reasons of simplification, Article 20(2) of the Sixth Directive is not to be applied. The same is true if the use is such that the conditions for the application of Article 20(5) are fulfilled.

According to the *United Kingdom*, the directive does not contain any express provision dealing with the situation where goods and services are acquired partly for business purposes and partly for non-business purposes. It is implicit in Article 17 that the right to deduct arises only in relation to business activities. The United Kingdom does not wish to make further observations on this aspect of the case.

The United Kingdom submits that, in respect of the right to deduct tax, Article 17(1) of the directive sets out clearly and precisely that a taxable person's right to deduct tax arises at the time when the deductible tax becomes chargeable. Article 17(2) determines the tax which a taxable person can actually deduct, that is, the tax which he incurs on goods and services in so far as the goods and services are used for the purposes of his taxable transactions.

In the light of those provisions the tax authorities have to determine whether a person is entitled to deduct tax in relation to supplies made to him in the light of his circumstances at the time when the tax became chargeable on such supplies to him. If at that time all the criteria set out in Article 17(2) are not met, no entitlement to deduct arises. The fact that the criteria in relation to the supply are subsequently met cannot affect the question of whether or not the right to deduct arose at the time the supply was made.

Accordingly, tax became chargeable under Article 10 of the directive on the supply of the motor car to the plaintiff in 1985. At that time in so far as the car was not used to make taxable or exempt supplies, the tax chargeable on the supply of the car was not deductible. The fact that he subsequently used the car for the purposes of his business cannot affect that position. Tax suffered on the purchase of a motor car for private purposes can never be transformed into tax capable of being deductible tax.

The United Kingdom submits that Article 17(5) of the directive lays down the principle to be applied when goods and services are to be used both for transactions in respect of which VAT is deductible and for transactions in respect of which VAT is not deductible. The structure and purpose of the directive precludes the word 'transactions' from referring to non-business and private activities. That interpretation is supported by Articles 2 and 4 of the directive.

The United Kingdom considers that the second issue that arises from the questions asked by the Finanzgericht is whether the existence of the mechanism for adjusting deductible tax under Articles 19 and 20 means that tax charged on the purchase of goods for non-business purposes can be converted into deductible tax in subsequent years. The United Kingdom submits that those provisions are solely concerned with the machinery for calculating the proportion of, and adjustments to, deductible tax and cannot transform tax which does not give rise to a right to deduct into deductible tax.

Finally, the expression 'capital goods' in Article 20(2) covers only goods which are used, or to be used, for the purposes of a business carried on, or to be carried on, by a taxable person.

The United Kingdom suggests the following reply to the whole of Question 1 asked by the Finanzgericht München:

'Where capital goods are supplied by one taxable person to another taxable person, Article 20(2) of the Sixth VAT Directive only applies to such goods that at the time of acquisition are used, or to be used, for the purposes of the recipient's business from the time of acquisition.'

Having regard to that answer, the United Kingdom considers that no answer is necessary to the Finanzgericht's other questions.

The *Commission* is of the opinion that the questions seek essentially to determine whether the conditions laid down in Article 17 of the directive for obtaining the initial right to deduct have been fulfilled.

In its judgment in *Kühne* v *Finanzamt München III* (judgment of 17 June 1989 in Case 50/88 [1989] ECR 1925), the Court rejected an interpretation of the Sixth Directive which would have led to such double taxation, contrary to the VAT system. In this case, there was no double taxation inasmuch as the input tax which was not deducted corresponded to the use of the vehicle for non-business purposes. The principle of the immediate deduction of the input tax determines any adjustment made thereto in the light of changes in the situation of law or fact on the basis of which the deduction was carried out.

The transfer of the vehicle from the domain of private use to that of business use is thus not a supply in respect of which deductible tax is chargeable. If the vehicle brought into the undertaking is used for transactions not subject to tax, VAT cannot in any event be deducted. If capital goods brought into the undertaking by a person who is not a taxable person are used for non-business purposes, they are not taxed under Article 6(2)(a), since the condition for such taxation, namely the deduction of input tax, has not been fulfilled.

The question whether, under the provisions of the directive in regard to deductions, it is possible to limit the initial right to deduct also arises. The discretion granted to the Member States under Article 20(4) of the directive in carrying out the adjustment does not go so far as to permit them to refuse to allow deduction of input tax at the time that the capital goods were supplied. The Member States clearly have a discretion in defining the concept of capital goods and the amount of tax to be paid.

Acceptance of the adjustment will provide no unfair advantage unless the right to deduct did not exist *ab initio* and the granting of a right to adjust gives rise to a right which does not exist or revives a right which has been extinguished. However, in the Commission's view, the use of the goods for non-business purposes during the first year following its acquisition was taxed normally in accordance with the apportionment rule.

The effect of administrative simplification cannot be to enlarge the basis of assessment or hinder the exercise of the right to deduct (see the judgment of 10 April 1984 in Case 324/82 *Commission* v *Belgium* [1984] ECR 1861). It is not clear why the derogation laid down in the second subparagraph of Article 18(4) should permit the Member States to limit the initial right to deduct at the time of adjustment or to apply that limitation to the adjustment itself.

The legislature has limited the cases in which the adjustment referred to in Article 20 may cover input tax where there is no right to deduct *ab initio*. That possibility is provided for in Article 20(6) of the directive (transfer from being taxed in the normal way to a special scheme or vice versa) and Article 4 of the Eighteenth VAT Directive (reclassification of the expenditure referred to in the first subparagraph of Article 17(6)).

It is essentially necessary to determine whether Article 17, read together with the other provisions of Title XI, must be interpreted as meaning that an initial minimum use of the capital goods gives a right to deduct input tax. An immediate deduction does not always mean a complete deduction. In accordance with the apportionment rule, only a part of the VAT invoiced is deducted immediately. In so far as it is not deducted, the VAT charged to the taxable person corresponds to non-taxable or non-business transactions.

According to the Commission, the right to deduct is a condition precedent to taxation. The deduction system laid down in the directive is meant to relieve the trader entirely of the burden of the VAT payable or paid in the course of all his economic activities (judgment in Case 268/83 *Rompleman* v *Minister van Financiën* [1985] ECR 655).

The determination of the degree of use of goods for non-business purposes and non-taxable transactions is carried out on the basis of the apportionment rules laid down in Article 17(5). All the possibilities of simplification and derogation provided for in Title XI are intended ultimately to facilitate deduction.

It must be concluded that actual use, albeit only minimal, of the capital goods supplied for taxable transactions gives a right to deduction of input tax.

The Commission proposes that the Court should answer the two questions referred to it as follows:

'Article 20 of the Sixth Directive applies to all capital goods supplied by one taxable person to another and used by the person to whom they are supplied for the purposes of taxable transactions.

Adjustment is carried out over five years.

If the capital goods are used for both taxable and non-taxable transactions (mixed use), the adjustment provided for in Article 20(2) of the directive is carried out in the light of the use of the capital goods in accordance with Article 17(5) and Article 19 of the directive.

Article 17(1) applies only where the capital goods are allocated to the undertaking at the time of their acquisition, regardless of whether they were used exclusively or only partly for the purposes of taxable transactions.

In the case of mixed use, the Sixth Directive lays down no minimum proportion in regard to use of the goods for taxable transactions.

The administration measures laid down in Article 20(4), cannot affect the right to deduct input tax provided for in Article 17(1), but it is for the national administration to determine whether the use for business purposes was real or merely fictitious.'

IV — Replies to questions put by the Court

The Government of the Federal Republic of Germany was asked to state why it was not considered necessary to obtain a decision from the Council, as a simplification measure under Article 27 of the Sixth Directive, authorizing it to refuse the right to deduct the VAT charged on expenditure for the acquisition of goods where the proportion of non-business use of those goods is greater than 90% of total use.

The German Government replied that the abovementioned practice of its tax authorities is not a special derogating measure but results from the economic point of view which must be adopted in interpreting Article 17 of the directive. The principle which requires that the economic aspect of the situation be taken into consideration (Grundsatz der wirtschaftlichen Betrachtungsweise) applies in regard to tax law. The VAT legislation applies only to supplies in the legal sense of the term if they are also supplies in the economic sense.

In regard to the taxation of turnover, the most important factor is the economic content of the transactions. The use of goods of which only a small proportion is for business purposes cannot give a right to a total deduction of tax under Article 17(2) of the directive. From the economic point of view, such goods must be regarded as having been acquired for non-business purposes. In the German Government's view, no deduction should be allowed where use for business purposes, as a proportion of total use, is so small that it is in any event insignificant in economic terms.

That is why the German tax authorities in general regard an acquisition as having been exclusively made for private purposes if private use represents more than 90% of total use. However, that is not a fixed limit but an indicator of whether the acquisition is 'for business purposes'. The fifth and sixth sentences of Section 192(17)(2) of the German guidelines on VAT permit a different decision to be taken in the light of the circumstances of the case.

Where a deduction is authorized, the private use of the vehicle must be taxed in accordance with Article 6(2)(a) of the directive. Under Article 11A(1)(c) of the directive, the taxable amount must include the full cost to the taxable person. All the costs which the taxable person had to pay in respect of the vehicle, including road tax and insurance, are subject to VAT. The taxable person is thus in a less favourable economic position than he would have been if he had not been allowed to deduct VAT at the time he purchased the vehicle.

The practice described above is not an application of Article 27 but results from Article 17 of the directive. The procedure in Article 27 is not suitable for resolving such questions of interpretation. According to the German Government, that procedure is intended only for cases in which a Member State is expressly seeking a derogation from the provisions of the directive in order to introduce measures intended to simplify the procedure for charging the tax or to prevent certain types of tax evasion or avoidance. For those reasons, the German Government did not consider it necessary to make an application to the Council under Article 27 in this matter.

T. F. O'Higgins
Judge-Rapporteur