

Value added tax (VAT): common system

2007/0238(CNS) - 07/11/2007 - Legislative proposal

PURPOSE: to amend the 2006/112/EC VAT Directive.

PROPOSED ACT: Council Directive.

BACKGROUND: both business and the Member States have drawn the Commission's attention to a number of elements of Directive 2006/112/EC, which require amending. None of the amendments call into question the guiding principles set out in the VAT Directive nor, however, are they of sufficient importance to justify a separate proposal.

CONTENT: the purpose of this proposal, therefore, is to amend the 2006 Directive. The amendments concern:

- the VAT scheme applicable to the supply of natural gas, electricity, heat and/or refrigeration;
- the tax treatment of joint undertakings set up pursuant to Article 171 of the EC Treaty;
- EU enlargement; and
- the conditions under which the right to deduct input VAT may be exercised.

In summary the amendments being proposed are:

VAT scheme applicable to the supply of natural gas, electricity, heat and/or refrigeration: The current VAT scheme for gas and electricity is derived primarily from Directive 2003/92/EC. However, it has become apparent that the technical terms used in that Directive have unduly limited the scope of the new tax scheme, which does not correspond to economic realities, particularly regarding the place where VAT is levied on the supply of natural gas and the VAT exemption for natural gas imports. It has also become clear that it would be expedient to apply the same rules to the supply of heat and refrigeration via head and/or refrigeration networks since this sector functions in a manner similar to the natural gas and electricity sector.

The Commission is therefore proposing to extend the scope to the supply and import of natural gas by all types of pipeline and by vessels transporting natural gas. It is also proposing to apply the same rules to the supply and import of heat or refrigeration via heat and/or refrigeration networks. With regard to the place where the VAT is to be levied, the proposal provides for taxation in the Member State of the customer of all services – and not only those services relating to access to the distribution systems. The procedure whereby Member States may apply a reduced VAT rate to supply natural gas, electricity and district heating has been simplified.

Article 171 Joint Undertakings: Article 171 on Joint Undertakings specifies that the Community may set up Joint Undertakings or any other structure necessary for the efficient execution of Community research, technological development and demonstration programme. These Joint Undertakings require a suitable tax framework.

The Commission is therefore proposing to clarify the tax status of JU in relation to VAT. Under proposed provisions these undertaking may be treated like international bodies in so far as they are set up by the European Communities, have legal personality and receive contributions that are charged to their general budget. The Commission proposal specifies that the exemption would not apply to the supply of goods and provision of services intended for the private use of the members of these Undertakings.

Enlargement: Both Bulgaria and Romania, upon accession to the EU, have been authorised to apply derogations regarding the tax exemption granted to SME's and the VAT scheme applicable to the international transport of passengers. The Commission is proposing to include these exemptions into the 2006 VAT Directive.

The right to deduct input VAT: One existing principle stipulates that a taxable person may deduct VAT on input transactions only in so far as the goods and services are used for his/her transactions that give rise to the right of deduction. The European Court of Justice has ruled that taxable persons have the right to choose whether to include mixed-use good, in part or in their entirety, in the assets relating to their economic activity. When taxable persons choose to include all of the goods in question in the economic activity they may immediately deduct all input VAT, irrespective of whether the good is used simultaneously for business and non-business purposes. The non-business use of the good will then be subject to VAT in the same way as a supply of services for consideration on the basis of the amount of expenditure incurred. The result of this could be that non-business use lowers the tax burden by an amount that could increase, in direct proportion, to the degree of use for non-business purposes. This is particularly true for immovable property. It therefore seems expedient to adapt the deduction of VAT relating to immovable property in such a way as to ensure that the initial exercise of the right to deduct input VAT will reflect the basic principle and to prevent certain constructions designed to create an unjustified cash-flow advantage.

Based on this, the Commission is proposing to apply a more effective principle, whereby deduction arises only in so far as the goods and services concerned are used for the transactions giving rise to the right of deduction. It proposes restricting the initial exercise of the deduction to the proportion of effective business use when mixed-use immovable property is included in the company's assets and liabilities. At the same time, an adjustment system is being proposed in order to reflect the variations between the business and private (or non-business) use of such immovable property.