

COMMISSION OF THE EUROPEAN COMMUNITIES

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COMMISSION REPORT TO THE COUNCIL
PRESENTED IN ACCORDANCE WITH ARTICLE 3 OF
THE COUNCIL DECISION 89/683/EEC
OF 21 DECEMBER 1989

(Application of a measure derogating from Article 2
of the sixth Directive (77/388/EEC) on the
harmonization of the laws of the Member States
relating to turnover taxes - Common system of value added tax)

Proposal for a

COUNCIL DECISION

authorizing the French Republic to extend the application
of a measure derogating from Article 2 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

(presented by the Commission)

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I. INTRODUCTION

By Council Decision 89/683/EEC of 21 December 1989,¹ France was authorized, on the basis of Article 27 of the sixth VAT Directive and following the entry into force of the eighteenth VAT Directive, to introduce special VAT arrangements derogating from the sixth Directive in respect of taxable transactions involving fresh industrial waste and recuperable material. Pursuant to Article 1 of that Decision, the authorization expires on 31 December 1992.

In addition, Article 3 of the Decision stipulates that the Commission is to present to the Council, prior to the date of expiry of the derogation, a report on its application, accompanied, where appropriate, by a proposal for a Council Decision providing for its extension.

The purpose of the present report is, therefore, to give an account of the application of that derogation and to examine the request for an extension of that derogation submitted by the French Republic by letter registered by the Secretariat-General of the Commission on 22 October 1992.

II. APPLICATION OF THE DEROGATION

1. Background

By virtue of Article 1(2)(a) of the eighteenth VAT Directive, France was obliged to abolish with effect from 1 January 1990 the derogation it applied on a transitional basis to supplies of recuperable material and fresh industrial waste pursuant to Article 28(3)(b) of the sixth Directive, read in conjunction with point 20 of Annex F.

However, point 4 ("Re Article 2, point F20") in the minutes adopting the eighteenth Directive² contains the following declaration:

"The Council and the Commission agree that they will consider with an open mind a request from France, on the basis of Article 27(1) to (4) of Directive 77/388/EEC, concerning a derogation based on the following principle:

1 OJ No L 398, 30.12.1989.

2 Council document 6016/89, Annex II, p. 8.

Sales, commission and brokerage operations relating to fresh industrial waste and recuperable material shall be subject to value added tax on the authorization of the competent tax authority.

This authorization may be subject, inter alia, to the following conditions: permanent installation, adequate annual turnover, the possible provision of a sufficient security."

At the time, the taxation of transactions involving fresh industrial waste and recuperable material were liable to give rise to substantial fraud, particularly in the "metal materials" sector. Such fraud consists in the issuing of false invoices designed to transfer a notional entitlement to tax deduction ("taxis") or in the invoicing of taxes never paid to the Treasury. In both cases, the revenue losses for the Treasury are considerable, with the waste-recovery sector in France having a total turnover of some FF 18 billion in 1989, a figure which this year will rise to FF 25 billion, and this for 15 million tonnes of recovered product and 5 000 waste-recovery firms.

2. Entry into force in France

The derogation was transposed into national law by Article 33 of Law No 90-1168 of 29 December 1990 (1991 Finance Law), with Articles 260, 261, 277, 273, 256, 290 and 1784 of the French General Tax Code being amended.

Administrative Instruction 3-A-1-91 of 27 December 1990, which was published in Official Tax Gazette No 9 of 14 January 1991 (Series 3 CA), contains a commentary on the provisions of national law arising from the derogation. Those provisions entered into force on 1 January 1991.

3. Disposition of the special arrangements introduced in France under cover of the derogation

The arrangements consist of the following three provisions:

3.1 Automatic taxation of supplies in respect of fresh industrial waste or recuperable material made by firms that satisfy the following two conditions simultaneously:

- existence of a permanent establishment

and

- turnover, exclusive of taxes, in respect of fresh industrial waste or recuperable material of not less than FF 6 million in the previous calendar year.

3.2 A "limited" exemption applicable in the case in point solely to supplies of fresh industrial waste and recuperable material made by firms:

- which either do not have a permanent establishment
- or which, although they have a permanent establishment, have achieved in the previous year a turnover figure, exclusive of tax, in respect of such supplies of less than FF 6 million.

This exemption carries an option for taxation, subject to authorization, that is available only to firms with a total annual turnover, inclusive of all taxes, of more than FF 500 000. In other words, the exemption is compulsory only for firms with an annual total turnover, inclusive of all taxes, of less than FF 500 000.

3.3 Compulsory suspension of payment of VAT in respect of supplies to taxable persons of fresh industrial waste and recuperable material in the form of non-ferrous metals and their alloys where these supplies attract tax automatically or subject to authorization, i.e. where they cannot be exempted.

Firms in the sector which make supplies under a suspension arrangement are not entitled to invoice VAT but, instead, they retain their entitlement to tax deduction, such entitlement being exercised by way of imputation where they carry out taxable transactions or by way of refund.

In addition, all imports of fresh industrial waste and recuperable material are exempt from VAT.

Commission operations in respect of fresh industrial waste or recuperable material rank as supplies of goods, unlike brokerage operations, which, as a result, are not covered by the derogation.

4. Position of the French administration on the application of the derogation

The French administration has made the following observations:

- "1. The waste-recovery sector in France has a turnover of some FF 25 billion, of which over a third is accounted for by exports, and this for a total of 15 million tonnes of recovered product. Some 5 000 firms are engaged in waste-recovery operations as their main activity.

Half of the firms in this sector are small firms with an annual turnover of less than FF 500 000. They account for some 10% of total turnover in the sector.

These firms differ very widely in nature (specialized small firms, charitable organizations, migrants, etc.), and the exemption in respect of supplies of fresh industrial waste or recuperable material made by them is quite consistent with the dual objective of simplification and repression of fraud, which led to the introduction of the arrangements provided for by the derogation.

The other firms, which are firms with an annual turnover exceeding FF 500 000 and should, therefore, attract VAT automatically or on authorization, account for 90% of total turnover in the sector.

Of the latter firms, some 60% are taxable automatically and account for over two thirds of turnover in this category.

The remaining firms in this category, which are liable to attract VAT subject to authorization, are those that do not have a permanent establishment or generate a turnover of between FF 500 000 and FF 6 million.

Of those firms without a permanent establishment, a relatively low percentage (some 8%) have a turnover of more than FF 6 million.

Over half of the firms liable to attract VAT subject to authorization have, at their request, been authorized to charge VAT on their supplies of fresh industrial waste and recuperable material. Very few requests for authorization are rejected.

Authorization may be conditional on the provision by the firm seeking authorization of good security. However, in 80% of cases, firms show themselves to be sufficiently solvent and are not required to provide any security.

Lastly, the VAT-suspension arrangement for fresh industrial waste and recuperable material in the form of non-ferrous metals is a useful complement to the system since the high value of such metals increases the risks of fraud.

2. Analysis of tax control statistics reveals that the firms in the sector that attract VAT present a lower-than-average risk of fraud as compared with other firms in France.

Moreover, if the average size of adjustments generally increases with firm size, it does so much less rapidly in the case of firms in this sector.

Lastly, the reasons for carrying out adjustments have more to do with errors in applying the tax rules (unjustified deductions) than with fraud proper (concealment of, or failure to report, taxable transactions).

This situation stems from the VAT arrangements applicable to firms in the sector and to the increased supervision by the administration authorized under the arrangements.

3. No particular difficulties have been encountered in administering the arrangements applicable to these firms (monitoring by the tax authorities of authorizations granted and securities provided).

Furthermore, the firms have welcomed the arrangements and are appreciative of them since, among other things, they safeguard against the risks to which they might be exposed as a result of fraudulent practices on the part of certain firms and for the consequences of which they might be liable vis-à-vis the administration."

III. REQUEST FOR EXTENSION OF THE DEROGATION

France is seeking an extension in full of the derogation for the entire transitional period defined in Article 281 of the sixth Directive, as amended by Directive 91/680/EEC of 16 December 1991 with a view to the abolition of fiscal frontiers.

It would also like to see the exemption currently applicable to all imports of fresh industrial waste and recuperable material being applied as from 1 January 1993 both to imports and to intra-Community acquisitions of such products.

IV. OPINION OF THE COMMISSION DEPARTMENTS

1. Application of the derogation by France

The transposition of Article 1 of the Council Decision calls for the following observations:

- It is not stipulated in the legal instrument amending Article 261-3-2 of the French General Tax Code that the exemption which is applicable in any event:

- * to firms whose annual turnover is less than FF 500 000

- * to firms not qualifying for the arrangements governing taxation subject to authorization

is limited over time and valid only until 31 December 1992.

Only Article 260F of the French General Tax Code, which deals with the authorization for taxation, expressly stipulates that such taxation subject to authorization is valid until 31 December 1992.

However, it should be pointed out that the administrative comments restore the limitation over time applicable to the limited exemption arrangements provided for in the Council Decision (see point 1, second subparagraph of Instruction 3-A-1-91);

- Only firms in the sector with a turnover, inclusive of all taxes, of between FF 500 000 and FF 6 million may be authorized to pay VAT, that is to say, to invoice it and, in so doing, to transfer an entitlement to tax deduction. These provisions are consistent with Article 1 of the Council Decision; they result from the combined provisions of the first indent of that Article. Accordingly, and this was the very purpose of the derogation, small firms necessarily remain exempt since, in the past, it was basically small waste-recovery operators that perpetrated fraud by using "taxi" systems. It should also be pointed out that the authorization to tax is generally granted only to firms which beforehand provide a security which, jointly and severally with the firm, must undertake to pay to the tax authorities the VAT invoiced in respect of transactions carried out during the period covered by the authorization.

Although there is no express provision to that effect in Article 1 of the Council Decision, the third recital to that Decision stipulates that the authorization procedure "may involve the provision of a guarantee";

- The examination made by the Commission departments has confirmed that supplies of fresh industrial waste and recuperable material which are exempt from VAT are not included in the numerator of the general deductible proportion in cases where the firm in the sector under consideration is a taxable person entitled to deduct tax in part. However, it would seem that such supplies, where made by the manufacturer himself and involving waste produced on his own premises, may be included in both the numerator and the denominator of the deductible portion, something which, at first sight, is contrary to the general principles of VAT. The Commission departments would, therefore, ask the French authorities to adapt, as appropriate the applicable provisions in this context.

2. Case for extending the temporary derogation granted to France

The Commission departments would note that the transitional period provided for in Article 281 of the sixth VAT Directive, as amended with a view to the abolition of fiscal frontiers, will not necessarily end on 31 December 1996. Since the derogation which the French Republic is now seeking to extend was initially granted for a period of two years, the Commission departments propose that it be extended for a further period of four years, so that it will expire on a definite date set in advance, namely 31 December 1996. This will make it possible, in particular, to ascertain whether extension of the exemption to the new category of intra-Community acquisitions is giving rise to any specific difficulties or fraudulent practices.

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EXPLANATORY MEMORANDUM

1. By letter registered by the Secretariat-General of the Commission on 22 October 1992, the Government of the French Republic requested an extension of the derogation previously granted to it for a limited period by Council Decision 89/683/EEC of 21 December 1989.¹ That Decision, which was based on Article 27 of the sixth VAT Directive,² authorizes France to introduce special VAT arrangements in respect of fresh industrial waste and recuperable material. The authorization expires on 31 December 1992.
2. Article 3 of the Decision stipulates that, in the light of a report from the Commission on the application by France of that Decision, the Council may, on the basis of a proposal from the Commission, decide before 31 December 1992 that the authorization is to be extended.
3. The report presented by the Commission on the application of that Decision over the period 1991-92 finds that the provisions of the Decision should be extended until 31 December 1996. The Commission will have to present to the Council before that date a new report on the application of the authorization in question, in particular with a view to ascertaining whether extension of the authorization to the new taxable category of intra-Community acquisitions is giving rise to any specific difficulties or fraudulent practices.
4. In accordance with Article 27(3) of the sixth VAT Directive, the other Member States were informed of the French request by letter dated 20 November 1992.

1 OJ No L 398, 30.12.1989.

2 OJ No L 145, 13.6.1977.

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THE COUNCIL OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Economic 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 assessment,¹ and in particular Article 27 thereof,

Having regard to Council Decision 89/683/EEC of 21 December 1989,²

Having regard to the Commission report on the application of the aforementioned Decision over the period 1991-92,

Having regard to the ensuing Commission proposal,

Whereas, under Article 27(1) of the sixth VAT Directive, the Council, acting unanimously on a proposal from the Commission, may authorize any Member State to introduce or extend 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 the Commission report on the application of the said derogation over the period 1991-92 has demonstrated the latter's usefulness and effectiveness in the waste-recovery sector, which is particularly vulnerable to fraud;

Whereas the said report finds that there is no reason to oppose extension of the derogation provided that the derogation is clearly limited over time and expires in the short term;

1 OJ No L 145, 13.6.1977.

2 OJ No.L 398, 30.12.1989

Whereas the other Member States were informed on 20 November 1992 of the request from the French Republic,

HAS ADOPTED THIS DECISION:

Article 1

By way of derogation from Article 2 of the sixth Directive (77/388/EEC), the French Republic is hereby authorized, until 31 December 1996 and in respect of fresh industrial waste and recuperable material, to exempt from value added tax (hereinafter referred to as "VAT"):

- on the one hand, supplies made by:
 - undertakings whose annual turnover is less than FF 500 000,
 - undertakings which do not have a permanent establishment or which, although they have a permanent establishment, have achieved in the previous year a turnover figure in respect of such products of less than FF 6 million, unless they are authorized to subject such transactions to VAT,
- on the other hand, imports and intra-Community acquisitions.

Article 2

By way of derogation from Article 10(2) of the sixth Directive (77/388/EEC), the French Republic is hereby authorized until 31 December 1996 to introduce in respect of supplies to taxable persons of fresh industrial waste and recuperable material in the form of non-ferrous metals and their alloys, where these supplies are not exempt from VAT on the basis of Article 1, arrangements suspending payment of the tax relating to these transactions.

The taxable persons receiving these supplies shall pay the tax on them where these products are intended neither for the export as such nor for the manufacture or resale as such of products liable to VAT.

Article 3

In the light of a report from the Commission on the application of the authorization referred to in Articles 1 and 2, accompanied, where appropriate, by a proposal for a Decision extending the said authorization, the Council, acting on the basis of that proposal, shall decide, before 1 January 1995, whether the said authorization is to be extended.

Article 4

This Decision is addressed to the French Republic.

Done at Brussels,

For the Council

The President

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