



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 21.03.1997  
COM(97)120 final

Proposal for a

COUNCIL DECISION

**AUTHORISING IRELAND TO APPLY A MEASURE DEROGATING FROM  
ARTICLE 21 OF THE SIXTH 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 5 February 1997, the Irish Government acting on the basis of Article 27 of the Sixth Council Directive (77/388/EEC) of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover tax - Common system of value-added tax: uniform basis of assessment<sup>1</sup>, requested authorisation to apply in respect of the surrender, including by way of abandonment, or assignment of a long-term lease of property, a measure derogating from Article 21 of that Directive.

Ireland exercises the option under Article 5(3) of the Directive to treat the supply of certain interests (i.e. a lease of ten years or more) in immovable property as a supply of goods. It also obtained a derogation under Article 27 (5) to treat the granting of such an interest by a lessor as a disposal of the lessor's entire interest in the property. Therefore, where a taxable person creates a lease of ten years or more in a developed property the supply is taxed, at that time, on the value of the interest disposed of in connection with the supply.

The lessee is, subject to the normal rules of Article 17 of the Directive, entitled to deduct the VAT charged.

Where a person having an exempt activity or a non-taxable person acquires the leasehold interest directly from the lessor no problem arises. However, avoidance schemes have arisen whereby a taxable person is inserted between the lessor and an ultimate user having no right of deduction of the tax (a taxable person carrying out exempted activities or a non-taxable legal person) Such an avoidance scheme works as follows :

The lessor grants a 35 years lease to a fully taxable person. The lessee deducts the VAT charged and carries out his taxable business from the premises. After one year the balance of the leasehold interest is assigned to the person having no right of deduction.

The taxable lessee, having disposed of his leasehold interest, has to charge VAT on the supply of the leasehold interest to assigned to the person having no right of deduction. However, the Irish administration established out that in these situations very often the lessee is liquidated and the VAT charge is not collectible.

The derogation from Article 21(1) would provide that in such circumstances the exempt person acquiring the leasehold interest would account for the VAT payable on the supply.

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<sup>1</sup> OJ No L 145, 13.6.1977, p. 1, as last amended by Directive 96/95/EC, OJ No L338, 28.12.1996, p. 89

While the avoidance schemes are all based on a person having no right of deduction of the tax acquiring an interest in property on which the VAT charged on the development has been deducted completely, it is also necessary to extend the derogation to the surrender or the assignment of a leasehold interest to a taxable person. Due to the nature of the VAT charge involved and the fact that the surrender or the assignment of a leasehold interest will often arise due to the financial difficulties of the lessee the derogation of Article 21(1) should also apply to the surrender or assignment of a taxable person to a taxable person.

The Commission is aware that the actual disposals of the Sixth VAT Directive, giving Member States a great deal of discretion in determining the tax treatment to be applied to the property sector under national legislation, are not functioning satisfactorily. This is illustrated by the fact that several Member States requested and obtained, on the bases of Article 27 of the Sixth VAT Directive, authorisation to introduce special measures, in order to prevent certain types of tax evasion or avoidance in this field.

Awaiting a complete revision of the VAT treatment of immovable property on Community level, the Commission takes the view that a Member State can be authorised to introduce a derogation in their VAT rules on immovable goods, in order to ensure its functioning for a limited period, on condition that this derogation respects the general conditions of Article 27 of the Sixth VAT Directive.

The Commission takes the view that the measure planned by Ireland is indeed a measure aimed at preventing tax avoidance and evasion within the meaning of Article 27 of the Directive and that, given the limited scope of the derogation, the special measure is proportionate to the aim pursued.

The Commission considers that Ireland can be authorised to apply the derogation for a period expiring on 31 December 1999. In fact, the Commission adopted on 10 July 1996 a work programme based on a step-by-step approach for progressing towards a new common system of VAT (COM (96) 328 final, 22 July 1996). The last package of proposals to be put forward by mid-1999, the Commission considers it appropriate to reconsider the necessity and the coherence of a specific measure in the framework of the global approach of the new common VAT system.

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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 assessment<sup>1</sup>, and in particular Article 27 thereof,

Having regard to the proposal from the Commission,

Whereas, under the terms of Article 27(1) of Directive 77/388/EEC, the Council, acting unanimously on a proposal from the Commission, may authorise any Member State to introduce special measure for derogation from the provisions of 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 5 February 1997, Ireland requested authorisation to introduce a measure derogating from Article 21(1) of the Sixth VAT Directive;

Whereas, in accordance with Article 27(3) of the Sixth VAT Directive, the other Member States were informed on 4 March 1997 of the request made by Ireland;

Whereas Ireland operates a specific system of applying VAT to property based on the one hand on the option under Article 5(3) of the Directive to treat the supply of certain interests (i.e. a lease of ten years or more) in immovable property as a supply of goods and on the other hand on a derogation authorised under Article 27 (5) to treat the granting of such an interest by a lessor as a disposal of the lessor's entire interest in the property;

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<sup>1</sup> OJ No L 145, 13.6.1977, p. 1, as last amended by Directive 96/95/EC, OJ No L338, 28.12.1996, p. 89

Whereas the Community provisions give Member States a great deal of discretion in determining the VAT treatment to be applied to immovable goods, its transposition have led to considerable variations in the national legislations applied in this field;

Whereas avoidance schemes have been set up, based on the use of surrender, including by way of abandonment of a leasehold interest or assignment of a leasehold interest, which result in the avoidance of the VAT where the ultimate acquirer of the property is not entitled to a full deduction of VAT;

Whereas it is also necessary to extend the derogation to the surrender or assignment of a leasehold interest to a taxable person having full right of deduction, as the surrender or the assignment of a leasehold interest will often arise due to financial difficulties of the lessee;

Whereas the measure envisaged is a derogation from Article 21(1)a of the Sixth VAT Directive, whereby the person liable for the tax is the taxable person who carries out the taxable transaction;

Whereas the derogation provides that, where a surrender or assignment of a leasehold interest is a taxable supply of goods, the person acquiring the interest is liable for the payment of the tax if that person is a taxable person or a non-taxable legal person;

Whereas this derogation shall ensure a better functioning of the actual VAT regime applied by Ireland on immovable goods;

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

Whereas the Commission adopted on 10 July 1996 a work programme based on a step-by-step approach for progressing towards a new common system of VAT (COM (96) 328 final, 22 July 1996);

Whereas the tax treatment of immovable goods is an important issue to be reviewed in this programme;

Whereas the last package of proposals is to be put forward by mid-1999, the authorisation is granted until 31 December 1999, in order to permit an evaluation of the coherence of the derogation with the global approach of the new common VAT system,

Whereas the derogation 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 21(1)a of the Directive 77/388/CEE, Ireland is hereby authorised to designate the person to whom the supply is made as the person liable to pay the tax where the two following conditions are met :

- a surrender or assignment of a leasehold interest is treated as a supply of goods made by a lessee;
- the person acquiring the leasehold interest is a taxable person or a non -taxable legal person.

### *Article 2*

This authorisation is granted until 31 December 1999.

This Decision is addressed to Ireland.

Done at Brussels,

For the Council,  
The President

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