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2015/0254 (NLE)

Proposal for a

COUNCIL IMPLEMENTING DECISION

authorising Latvia to introduce a special measure derogating from point (a) of Article 26(1) and Articles 168 and 168a of Directive 2006/112/EC on the common system of value added tax

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

• Reasons for and objectives of the proposal

Pursuant to Article 395(1) of Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (hereafter "the VAT Directive"), the Council, acting unanimously on a proposal from the Commission, may authorise any Member State to apply special measures for derogation from the provisions of that Directive in order to simplify the procedure for collecting VAT or to prevent certain forms of tax evasion or avoidance.

By letter registered with the Commission on 8 April 2015, Latvia requested authorisation to continue to apply a measure derogating from the overall principles governing the right of deduction of input VAT in relation to certain passenger cars. Together with the request for extension, Latvia submitted a report covering the application of Council Implementing Decision 2013/191/EU which includes a review of the percentage foreseen for the limitation of the right of deduction. The request and report were further completed on 30 July 2015.

In accordance with Article 395(2) of the VAT Directive, the Commission informed the other Member States by letters dated 21 and 24 August 2015 of the request made by Latvia. By letter dated 24 August 2015, the Commission notified Latvia that it had all the information it considered necessary for appraisal of the request.

General context

Article 168 of the VAT Directive provides that a taxable person is entitled to deduct VAT charged on purchases made for the purpose of taxed transactions. Article 26(1)(a) of the same Directive requires the use of goods forming part of the assets of a business for private purposes to be a supply of services for consideration if the VAT on the goods was eligible for deduction. This system allows for the recovery of initially deducted VAT in relation to the private use.

In the case of passenger cars, this system is difficult to apply, in particular because it is difficult to identify the split between private and business use. Where records are kept, they add an additional burden to both the business and the administration in maintaining and checking them, even in case Latvia would make use of the option provided for in Article 168a of the VAT Directive to limit the deduction on expenditure related to company cars to the proportion of the taxable person's effective business use.

In order to simplify VAT collection and combat tax evasion, in 2011 Latvia requested an individual derogation allowing it to restrict the right of deduction to 80% in relation to certain passenger cars. The derogation request was approved by the Council by Decision 2013/191/EU of 22 April 2013 and expires on 31 December 2015. Some categories of vehicles were specifically excluded from this restriction, such as cars purchased for resale, hire or lease; cars used for transportation of passengers (such as taxis) or goods; cars used for driving lessons; cars used for guard or emergency services; cars used as car sales demonstration vehicle. At the same time, businesses would be relieved from accounting from tax on the private use.

In accordance with Article 6(b) of the above mentioned Decision, Latvia has presented a report covering the application of the Decision which included a review of the percentage restriction.

It appears from the information provided by Latvia that the 80% rate of deduction no longer corresponds to the actual circumstances and that this rate should be decreased to 50%. Latvia is supporting the new percentage limitation with statistical figures derived from a special tax on light vehicles owned or held by commercial operators that are used for private and business activities. According to the information submitted by Latvia, the special tax was paid for 79% of all roadworthy light vehicles held or owned by legal persons. Latvian authorities also provide that the percentages of the legal persons that have at least one light vehicle registered and which paid the special tax on light vehicles was 87.6% in 2012, 92.5% in 2013 and 86.2% in 2014. In addition, 99.6% of the registered businesses in Latvia are small and medium enterprises. Latvia considers that, on the basis of this statistical information which covers most of the taxable persons, it can be concluded that their overall private use of passenger cars corresponds to 50%. The new limitation should therefore be set at 50%.

All the other conditions of the derogation will continue to apply. Thus, the new system will apply to all passenger cars with a maximum of eight seats in addition to the driver's seat and under a certain weight that are not used exclusively for business purposes. In the same way, passenger cars which are used for certain specific activities would also be excluded from the restriction on the right to deduct and would be treated under the normal rules: cars purchased for resale, hire or lease; cars used for transportation of passengers (such as taxis) or goods; cars used for driving lessons; cars used for guard or emergency services; cars used as car sales demonstration vehicle.

Given the change in percentage, a new derogation is more suitable than an extension of the existing one. The new derogation should be limited in time to 31 December 2018 in order to assess whether the conditions on which the derogation is based would still be valid. Any extension request should be accompanied by a report which includes a review of the percentage applied and should be sent to the Commission with that request by 31 March 2018.

- **Consistency with existing policy provisions in the policy area**

Similar derogations in relation to the right of deduction have been granted to other Member States, including Latvia through Decision 2013/191/EU of 22 April 2013.

Article 176 of the VAT Directive stipulates that the Council shall determine the expenditure on which the VAT is not deductible. Until such time, it authorises Member States to maintain exclusions which were in place on 1 January 1979. There are therefore a number of "stand still" provisions restricting the right to deduct in relation to passenger cars.

- **Consistency with other Union policies**

Not applicable

2. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY

- **Legal basis**

Article 395 of the VAT Directive.

- **Subsidiarity (for non-exclusive competence)**

Considering the provision of the VAT Directive on which the proposal is based, the proposal falls under the exclusive competence of the Union. The subsidiarity principle therefore does not apply.

- **Proportionality**

The proposal complies with the proportionality principle for the following reasons.

The Decision concerns an authorisation granted to a Member State upon its own request and does not constitute any obligation.

Given the limited scope of the derogation, the special measure is proportionate to the aim pursued, i.e. to combat tax evasion and to simplify VAT collection.

- **Choice of the instrument**

Under Article 395 of the VAT Directive, derogation from the common VAT rules is only possible with the authorisation of the Council acting unanimously on a proposal from the Commission. Moreover, a Council Decision is the most suitable instrument since it can be addressed to individual Member States.

3. RESULTS OF EX-POST EVALUATIONS, STAKEHOLDER CONSULTATIONS AND IMPACT ASSESSMENTS

- **Ex-post evaluations/fitness checks of existing legislation**

Not applicable.

- **Stakeholder consultations**

This proposal is based on a request made by Latvia and concerns only this Member State.

- **Collection and use of expertise**

There was no need for external expertise.

- **Impact assessment**

The Decision proposal aims in the first place at simplifying the collecting of VAT in relation to passenger cars partly used for non-business purposes and has therefore a potential positive impact. At the same time, tax evasion via incorrect record keeping is countered.

However, because of the narrow scope of the derogation and the limited application in time, the impact will in any case be limited.

4. BUDGETARY IMPLICATIONS

The proposal has no implication for the union budget.

5. OTHER ELEMENTS

- **Implementation plans and monitoring, evaluation and reporting arrangements**

The proposal includes a sunset clause; an automatic time limit which is set at 31 December 2018 for this derogation.

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax [1], and in particular Article 395(1) thereof,

Having regard to the proposal from the European Commission,

Whereas:

(1) By letter registered at the Commission on 8 April 2015, Latvia requested authorisation to continue under certain conditions to apply a measure derogating from Article 26(1)(a) and Articles 168 and 168a of Directive 2006/112/EC in order to restrict the right of deduction in relation to expenditure on certain passenger cars not wholly used for business purposes. The request was further completed on 30 July 2015.

(2) In accordance with the second subparagraph of Article 395(2) of Directive 2006/112/EC, by letters dated 21 and 24 August 2015, the Commission informed the other Member States of the request made by Latvia. By letter dated 24 August 2015, the Commission notified Latvia that it had all the information necessary to consider the request.

(3) Articles 168 and 168a of Directive 2006/112/EC establish a taxable person's right to deduct value added tax (VAT) charged on supplies of goods and services received by him for the use of his taxed transactions. Article 26(1)(a) of that Directive contains a requirement to account for VAT when a business asset is put to non-business use.

(4) Council Implementing Decision 2013/191/EU[2] authorised Latvia to introduce a derogating measure pursuant to Article 395(1) of Directive 2006/112/EC to limit the right of deduction of input VAT to 80% as regards purchase, leasing, intra-Community acquisition and importation of specified passenger cars and on related expenditure thereto, including the purchase of fuel, when the vehicles are not used exclusively for business purposes. Council Implementing Decision 2013/191/EU is due to expire on 31 December 2015.

(5) Together with the request, Latvia submitted a report covering the application of Council Implementing Decision 2013/191/EU which includes a review of the percentage foreseen for the limitation of the right of deduction. It appears from the information provided by Latvia that the 80% rate of deduction no longer corresponds to the actual circumstances and that this rate should be decreased to 50%. The

[1] OJ L 347, 11.12.2006, p. 1.
[2] OJ L 113, 25.04.2013, p.11

information is based on statistical figures derived from a special tax on light vehicles owned or held by commercial operators that are used for private and business activities.

(6) The limitation of the right of deduction under the measure should apply to VAT paid on the purchase, leasing, intra-Community acquisition and importation of specified passenger cars and on expenditure related thereto, including the purchase of fuel.

(7) The measure should only apply to passenger cars with a maximum authorised weight not exceeding 3500 kilograms and having not more than eight seats in addition to the driver's seat. Any non-business use of passenger cars exceeding 3500 kilograms or having more than eight seats in addition to the driver's seat is negligible due to their nature or the type of business they are used for. A detailed list of specific passenger cars excluded from that authorisation should also be provided, based on their particular use.

(8) Latvia should therefore be authorised to apply the measure for a limited period, until 31 December 2018.

(9) In the event Latvia were to request an extension of the derogating measure beyond 2018, a report should be submitted to the Commission together with the extension request no later than 31 March 2018.

(10) The derogation would only have negligible effect on the overall amount of tax revenue collected at the stage of final consumption and will have no adverse impact on the Union's own resources accruing from VAT,

HAS ADOPTED THIS DECISION:

Article 1

By way of derogation from Articles 168 and 168a of Directive 2006/112/EC, Latvia is authorised to limit to 50% the right to deduct the value added tax (VAT) on expenditure on passenger cars not wholly used for business purposes.

Article 2

By way of derogation from point (a) of Article 26(1) of Directive 2006/112/EC, Latvia shall not treat as supplies of services for consideration the use for private purposes of a passenger car included in the assets of a taxable person's business, where that car has been subject to a limitation authorised under Article 1 of this Decision.

Article 3

The expenditure referred to in Article 1 shall cover the purchase, leasing, intra-Community acquisition and importation of such cars as well as expenditure related to the maintenance, repair and fuel for such cars.

Article 4

This Decision shall only apply to passenger cars with a maximum authorised weight not exceeding 3500 kilograms and having not more than eight seats in addition to the driver's seat.

Article 5

Articles 1 and 2 shall not apply to the following categories of passenger cars:

(a) cars purchased for resale, hire or lease;

(b) cars used for transportation of passengers for a fee, including taxi services;

(c) cars used for the provision of transportation of goods;

(d) cars used for the provision of driving lessons;

(e) cars used for the provision of guard services;

(f) cars used as an emergency vehicle;

(g) cars used as a car sales demonstration vehicle.

Article 6

1. This Decision shall take effect on the day of its notification.

   This Decision shall apply from 1 January 2016. It shall expire on 31 December 2018.

2. Any request for the extension of the authorisation provided for in this Decision shall be submitted to the Commission by 31 March 2018 and accompanied by a report which includes a review of the percentage set out in Article 1.

Article 7

This Decision is addressed to the Republic of Latvia.

Done at Brussels,

For the Council
The President