Council of the European Union

Brussels, 13 October 2021
(OR. en)

12832/21

Interinstitutional File: 2021/0325(NLE)

FISC 165
ECOFIN 974

PROPOSAL

From:	Secretary-General of the European Commission, signed by Ms Martine DEPREZ, Director
date of receipt:	13 October 2021
To:	Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union
No. Cion doc.:	COM(2021) 631 final
Subject:	Proposal for a COUNCIL IMPLEMENTING DECISION amending Implementing Decision (EU) 2018/1994 authorising Croatia to introduce a special measure derogating from point (a) of Article 26(1) and Article 168 of Directive 2006/112/EC on the common system of value added tax

Delegations will find attached document COM(2021) 631 final.

Encl.: COM(2021) 631 final

EUROPEAN
COMMISSION

Brussels, 13.10.2021
COM(2021) 631 final

2021/0325 (NLE)

Proposal for a

COUNCIL IMPLEMENTING DECISION

amending Implementing Decision (EU) 2018/1994 authorising Croatia to introduce a special measure derogating from point (a) of Article 26(1) and Article 168 of Directive 2006/112/EC on the common system of value added tax

EXPLANATORY MEMORANDUM

Pursuant to Article 395(1) of Directive 2006/112/EC of 28 November 2006 on the common system of value added tax[1] ('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 31 March 2021, Croatia requested an extension of the derogation from Article 26(1), point (a), and Article 168 of the VAT Directive in order to continue to restrict the right to deduct the input VAT on the purchase and lease of passenger cars, including the purchase of all goods and services supplied in relation thereto. Together with the request for extension, Croatia submitted a report including a review of the percentage foreseen for the limitation of the right of deduction.

In accordance with Article 395(2) of the VAT Directive, the Commission informed the other Member States by letter dated 22 April 2021 of the request made by Croatia. By letter dated 23 April 2021, the Commission notified Croatia that it had all the information it considered necessary for appraisal of the request.

1. CONTEXT OF THE PROPOSAL

• Reasons for and objectives of the proposal

Article 168 of the VAT Directive provides that a taxable person is entitled to deduct the VAT charged on purchases made for the purpose of taxed transactions. Article 168a(1) of the VAT Directive provides that the VAT on expenditure related to immovable property forming part of the business assets of a taxable person and used both for business and non-business purposes shall be deductible only to the proportion of the property's use for purposes of the taxable person's business. Pursuant to Article 168a(2) of the VAT Directive Member States may also apply this rule in relation to expenditure related to other goods forming part of the business assets as they specify. 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.

Pursuant to Article 395 of the VAT Directive, Member States may apply measures derogating from the provisions of the VAT Directive to simplify the procedure for collecting VAT or to prevent certain forms of tax evasion or avoidance if they have been authorised by the Council.

[1] OJ L 347, 11.12.2006, p. 1.

Croatia is currently authorised on the basis of Council Implementing Decision 2018/1994/EU[2] to restrict to 50 % the right of deduction of VAT paid on the purchase and leasing of specified passenger cars, including the purchase of all goods and services supplied in relation thereto, when those cars are not wholly used for business purposes. The special measure also relieves taxable persons from having to treat the non-business use of such passenger cars as a supply of services. Passenger cars covered by this measure are motor vehicles intended for the transport of persons with a maximum of eight seats in addition to the driver's seat. If passenger cars are used for certain specific activities, they are excluded from the restriction to the right to deduct and are treated under the normal rules. This applies to vehicles used for the training of drivers, vehicle testing, repair services, an economic activity involving the transport of passengers and goods, the transport of deceased or rent, as well as to vehicles purchased for the purpose of resale. Council Implementing Decision 2018/1994/EU is valid until 31 December 2021.

The present request by Croatia to prolong further the special measure is based on the same grounds as those presented in the previous request. The request is accompanied by a report including a review of the percentage limitation applied on the right of deduction, as required by Article 6(3) of Council Implementing Decision 2018/1994/EU. Croatia considers that the conditions for the application of the special measure continue to apply and that the currently applied 50 % input VAT deduction limit continues to be the most appropriate.

Croatia explained that, based on data provided by both taxable persons and tax administrations, passenger cars forming part of business assets keep being used for private purposes at an average of 50 %. In this regard, Croatia submitted two surveys carried out in the beginning of 2021 on the use of passenger cars used for business and private use, indicating that setting the percentage of the right to deduction of input tax at 50 % still appears realistic.

Given the positive impact of the special measure on the administrative burden of taxpayers and tax authorities alike, it is proposed to authorise the extension of the current derogation measure. The authorisation should be valid for another limited period, i.e. until 31 December 2024, in order to allow for a review of the necessity and effectiveness of the derogating measure and the apportionment rate between business and non-business use it is based on. Any extension request should be accompanied by a report which includes a review of the percentage applied and should be sent to the Commission by 31 March 2024.

Since Croatia, under Article 168a(2) of the VAT Directive, opted to apply Article 168a(1) of the VAT Directive to other economic goods forming part of the business assets than immovable property, a reference to Article 168a of that Directive should, for reasons of completeness, be included in the title and Article 1 of Council Implementing Decision 2018/1994/EU.

- **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 (Estonia[3], Hungary[4], Latvia[5], Poland[6], Italy[7] and Romania[8]).

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2 Council Implementing Decision (EU) 2018/1994 of 11 December 2018 authorising Croatia to introduce a special measure derogating from point (a) of Article 26(1) and Article 168 of Directive 2006/112/EC on the common system of value added tax, OJ L 320, 17.12.2018, p. 35-36.

3 Council Implementing Decision (EU) 2017/1854 of 10 October 2017 amending Implementing Decision 2014/797/EU authorising the Republic of Estonia to apply a measure derogating from point (a) of

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 VAT in relation to passenger cars.

Notwithstanding previous initiatives to establish rules on which categories of expenditure may be subject to a restriction on the right to deduct[9], such derogation is appropriate in the awaiting of a harmonisation of these rules at EU level.

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 European Union. The subsidiarity principle does not apply.

• Proportionality

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 simplify the procedure for collecting the tax and to prevent certain forms of tax evasion or avoidance. In particular, given the potential for businesses to under declare their liability and the burdensome check of mileage data for tax authorities, the 50 % restriction would simplify the VAT collection in a specific sector.

Articles 26(1) and Article 168 and 168a of Directive 2006/112/EU on the common system of value added tax (OJ L 265, 14.10.2017, p. 17), valid until 31 December 2020.

[4] Council Implementing Decision (EU) 2018/1493 of 2 October 2018 authorising Hungary 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, OJ L 252, 8.10.2018, p. 44–46.

[5] Council Implementing Decision (EU) 2018/1921 of 4 December 2018 amending Implementing Decision 2015/2429/EU 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, OJ L 311, 7.12.2018, p. 36-37.

[6] Council Implementing Decision (EU) 2019/1594 of 24 September 2019 amending Implementing Decision 2013/805/EU authorising the Republic of Poland to introduce measures derogating from point (a) of Article 26(1) and Article 168 of Directive 2006/112/EC on the common system of value added tax, OJ L 248, 27.9.2019, p. 71–72.

[7] Council Implementing Decision (EU) 2019/2138 of 5 December 2019 amending Decision 2007/441/EC authorising the Italian Republic to apply measures derogating from Articles 26(1)(a) and 168 of Directive 2006/112/EC on the common system of value added tax, OJ L 324, 13.12.2019, p. 7–8.

[8] Council Implementing Decision (EU) 2020/1262 of 4 September 2020 amending Implementing Decision 2012/232/EU authorising Romania to apply measures derogating from Article 26(1)(a) and Article 168 of Directive 2006/112/EC on the common system of value added tax, OJ L 296, 10.09.2020, p. 6.

[9] COM (2004) 728 final - Proposal for a Council Directive amending Directive 77/388/EEC with a view to simplifying value added tax obligations (OJ C 24, 29.1.2005, p.10) withdrawn on 21 May 2014 (OJ C 153 21. 05. 2014, p. 3)

- **Choice of the instrument**

Proposed instrument: Council Implementing Decision.

Under Article 395 of the VAT Directive, a derogation from the common VAT provisions is only possible upon authorisation of the Council acting unanimously on a proposal from the Commission. A Council Implementing Decision is the most suitable instrument since it can be addressed to an individual Member State.

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

- **Stakeholder consultations**

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

There was no need for external expertise.

- **Impact assessment**

The proposal is designed to simplify the procedure for charging tax by removing the need for taxable persons to keep records on the private use of specified passenger cars, and, at the same time, prevent VAT evasion through incorrect record keeping. It has, therefore, a potential positive impact for both businesses and the tax administration. The solution has been identified by Croatia as a suitable measure and is comparable to other past and present derogations.

4. BUDGETARY IMPLICATIONS

The derogating measures will only have a negligible effect on the overall amount of tax revenue collected at the stage of final consumption and will have no adversely impact on the Union's own resources accruing from VAT.

5. OTHER ELEMENTS

The proposal is limited in time and includes a sunset clause set at 31 December 2024.

In case Croatia would consider another extension of the special measure beyond 2024, a report including a review of the percentage limit should be submitted to the Commission together with the extension request, no later than 31 March 2024.

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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), first subparagraph, thereof,

Having regard to the proposal from the European Commission,

Whereas:

(1) Articles 168 and 168a of Directive 2006/112/EC establish taxable persons' right to deduct value added tax (VAT) charged on supplies of goods and services received by them for the purposes of their taxed transactions. Article 26(1), point (a), of that Directive contains a requirement to account for VAT when a business asset is put to use for private purposes of taxable persons or their staff or, more generally, for purposes other than those of their business.

(2) Council Implementing Decision (EU) 2018/1994[2] authorised Croatia, until 31 December 2021, to limit to 50% the right to deduct VAT paid on the purchase and leasing of specified passenger cars with a maximum of eight seats in addition to the driver's seat, including the purchase of all goods and services supplied in relation thereto, when those cars are not wholly used for business purposes. The authorisation also relieved taxable persons from having to treat the non-business use of such passenger cars as a supply of services.

(3) By letter registered with the Commission on 31 March 2021, Croatia requested an authorisation to continue to apply the special measure derogating from Article 26(1), point (a), and Article 168 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').

(4) Croatia applies Article 168a(1) of Directive 2006/112/EC in relation to VAT on expenditure related to other economic goods forming part of the business assets under

[1] OJ L 347, 11.12.2006, p. 1.

[2] Council Implementing Decision (EU) 2018/1994 of 11 December 2018 authorising Croatia to introduce a special measure derogating from point (a) of Article 26(1) and Article 168 of Directive 2006/112/EC on the common system of value added tax, OJ L 320, 17.12.2018, p. 35-36.

Article 168a(2) of that Directive. Thus, Council Implementing Decision (EU) 2018/1994 should have included a reference to Article 168a of Directive 2006/112/EC.

(5) In accordance with Article 395(2), second subparagraph, of Directive 2006/112/EC, by letter dated 22 April 2021, the Commission informed the other Member States of the request made by Croatia. By letter dated 23 April 2021, the Commission notified Croatia that it had all the information it considered necessary for appraisal of the request.

(6) As required by Article 6(3) of Implementing Decision (EU) 2018/1994, Croatia submitted a report including the review of the percentage laid down for the limitation of the right of deduction. Based on currently available information, Croatia confirmed that the limit of 50 % is still justifiable and remains appropriate.

(7) Given the positive impact of the special measure on the administrative burden of taxpayers and tax authorities alike, Croatia should therefore be authorised to continue to apply the special measure. The extension of the special measure should be limited in time, until 31 December 2024, to allow for an evaluation of its effectiveness and of the appropriate percentage.

(8) In the event that Croatia considers that a further extension of the special measure is necessary, it should submit the request for an extension accompanied by a report that includes a review of the percentage applied to the Commission by 31 March 2024.

(9) The special measure will 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.

(10) Implementing Decision (EU) 2018/1994 should, therefore be amended accordingly,

HAS ADOPTED THIS DECISION:

Article 1

Implementing Decision (EU) 2018/1994 is amended as follows:

(1) the title is replaced by the following:

‘Council Implementing Decision (EU) 2018/1994 of 11 December 2018 authorising Croatia 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’;

(2) Article 1 is replaced by the following:

‘*Article 1*

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

(3) Article 6 is replaced by the following:

‘*Article 6*

The Decision shall apply from 1 January 2019 until 31 December 2024.

Any request for the extension of the authorisation provided for in this Decision shall be submitted to the Commission by 31 March 2024 and shall be accompanied by a report that includes a review of the percentage set out in Article 1.’.

Article 2

This Decision is addressed to the Republic of Croatia.

Done at Brussels,

For the Council
The President