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PROPOSAL

From:	Secretary-General of the European Commission, signed by Ms Martine DEPREZ, Director
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To:	Ms Thérèse BLANCHET, Secretary-General of the Council of the European Union
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Subject:	Proposal for a COUNCIL IMPLEMENTING DECISION amending Implementing Decision (EU) 2015/2429 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

Delegations will find attached document COM(2024) 488 final.

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2024/0270 (NLE)

Proposal for a

COUNCIL IMPLEMENTING DECISION

amending Implementing Decision (EU) 2015/2429 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

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 derogating from the provisions of this Directive, in order to simplify the procedure for charging VAT or to prevent certain forms of tax evasion or avoidance.

By letter registered with the Commission on 15 May 2024, Latvia requested an authorisation to continue to apply a measure derogating from point (a) of Article 26(1) and Articles 168 and 168a of the VAT Directive to restrict the right of deduction of input VAT in relation to expenditure on certain passenger cars not wholly used for business purposes and to relieve taxable persons from having to treat the private use of such vehicles as a supply of services for consideration. Together with the request for extension, Latvia 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 letters dated 10 September 2024 of the request made by Latvia. The Commission notified Latvia by letter dated 11 September 2024 that it had all the information necessary to consider 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 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. Point (a) of paragraph 1 of Article 26 of that Directive contains a requirement to account for VAT when goods forming part of the assets of a business are put to use for private purposes of the taxable person or for that of his staff or, more generally, for purposes other than those of his business, where the VAT on such goods was wholly or partly deductible. 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 347, 11.12.2006, p.1.

Latvia is currently authorised on the basis of Council Implementing Decision (EU) 2015/2429[2] to limit to 50% the right to deduct the VAT paid on the purchase, leasing, intra-Community acquisition and importation of certain passenger cars, and expenditure related to the maintenance, repair and fuel for such cars, when those passenger 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 for consideration. Passenger cars covered by the special measure are those with a maximum authorised weight not exceeding 3 500 kilograms and having not more than eight seats in addition to the driver's seat. Passenger cars which are used for certain specific activities are excluded from the restriction on the right to deduct VAT 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. The period of validity of this special measure was extended by Council Implementing Decision (EU) 2018/1921 of 4 December[3] until 31 December 2021 and by Council Implementing Decision (EU) 2021/1968 of 9 November[4] until 31 December 2024.

The present request by Latvia to prolong further the special measure is based on the same grounds as those presented in the previous requests. 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(2) of Council Implementing Decision (EU) 2015/2429. Latvia considers that the conditions for the application of the special measure continue to apply and that the applied 50% limit remains appropriate.

Latvia confirms that the special measure allows administrative burden to be eased for taxpayers and for the tax administration and limits the evasion of VAT through incorrect record-keeping of journeys made in connection with business activities and incorrectly completed VAT returns. According to the data submitted by Latvia, in 2023 micro-enterprises and SMEs accounted for 99.7% of economically active enterprises which complicates the task of the tax authorities when verifying the business and private use of passenger cars. As of 1 January 2024 the total number of registered traders in Latvia with one or two passenger cars was 23 627 or 80.6% of all registered traders who registered passenger cars. Since microenterprises and SMEs make up 99.7% of all operators, Latvia maintains that most of the passenger cars are used for private purposes. According to the data provided, as of 1 January 2024, 84.5% of all passenger cars belonging to registered traders were used not only for business but also for private purposes.

Given the positive impact of the special measure on the administrative burden of taxpayers and of tax authorities, it is proposed to authorise the extension of the current special measure. The authorisation should be valid for another limited period, i.e. until 31 December 2027, in order to allow for a review of the necessity and effectiveness of the special measure and

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2 Council Implementing Decision (EU) 2015/2429 of 10 December 2015 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 334, 22.12.2015, p. 15-17.

3 Council Implementing Decision (EU) 2018/1921 of 4 December 2018 amending Implementing Decision 2015/2429 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.

4 Council Implementing Decision (EU) 2021/1968 of 9 November 2021 amending Implementing Decision (EU) 2015/2429 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 401, 12.11.2021, p. 1–2.

whether the 50% restriction is still a correct reflection of the overall apportionment between business and private use. 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 2027.

- **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[5], Hungary[6], Croatia[7], Poland[8], Italy[9] and Romania[10]).

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[11], 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 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.

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5 Council Implementing Decision (EU) 2021/1998 of 15 November 2021 authorising Estonia to apply a measure derogating from Article 26(1), point (a), and Articles 168 and 168a of Directive 2006/112/EC on the common system of value added tax, OJ L 408, 17.11.2021, p. 3–5.

6 Council Implementing Decision (EU) 2021/1774 of 5 October 2021 amending Implementing Decision (EU) 2018/1493 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 360, 11.10.2021, p. 108–109.

7 Council Implementing Decision (EU) 2021/1997 of 15 November 2021 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, OJ L 408, 17.11.2021, p. 1–2.

8 Council Implementing Decision (EU) 2022/2385 of 6 December 2022 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 315, 7.12.2022, p. 87–88.

9 Council Implementing Decision (EU) 2022/2411 of 6 December 2022 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 317, 9.12.2022, p. 120–121.

10 Council Implementing Decision (EU) 2024/1641 of 24 May 2024 authorising Romania to apply special measures derogating from Article 26(1), point (a), and Article 168 of Directive 2006/112/EC on the common system of value added tax, OJ L, 2024/1641, 6.6.2024.

11 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)

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 and would prevent tax evasion inter alia through incorrect record keeping and incorrectly completed VAT returns.

- **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**

No stakeholder consultation has been conducted. 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 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, to prevent certain form of VAT evasion through incorrect record keeping. The proposed measure has, therefore, a potential positive impact for both businesses and tax administration. The solution has been identified by Latvia as a suitable measure and is comparable to other past and present derogations.

4. BUDGETARY IMPLICATIONS

The proposal will not adversely affect the Union's own resources from VAT.

5. OTHER ELEMENTS

The proposal is limited in time and includes a sunset clause set at 31 December 2027.

In case Latvia would consider another extension of the special measure beyond 2027, 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 2027.

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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) 2015/2429[2], as amended by Council Implementing Decision (EU) 2021/1968[3], authorises Latvia, until 31 December 2024, to limit to 50% the right to deduct VAT on expenditure on passenger cars not wholly used for business purposes and authorises Latvia to not treat as supplies of services for consideration the use for private purposes of a passenger car inlucded in the assets of a taxable person's business, where that car has been subject to a limitation authorised under Article 1 of that Decision ('the special measure').

(3) By letter registered by the Commission on 15 May 2024, Latvia submitted a request, in accordance with Article 395(2), first subparagraph, of Directive 2006/112/EC, to the Commission to continue to apply the special measure ('the extension request').

(4) In accordance with Article 395(2), second subparagraph, of Directive 2006/112/EC, the Commission transmitted the extension request to the other Member States by letters of 10 September 2024. By letter of 11 September 2024, the Commission

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1 OJ L 347, 11.12.2006, p. 1, ELI: http://data.europa.eu/eli/dir/2006/112/oj.

2 Council Implementing Decision (EU) 2015/2429 of 10 December 2015 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 334, 22.12.2015, p. 15, ELI: http://data.europa.eu/eli/dec_impl/2015/2429/2022-01-01).

3 Council Implementing Decision (EU) 2021/1968 of 9 November 2021 amending Implementing Decision (EU) 2015/2429 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 401, 12.11.2021, p. 1, ELI: http://data.europa.eu/eli/dec_impl/2021/1968/oj).

notified Latvia that it had all the information necessary to consider the extension request.

(5) In accordance with Article 6(2) of Implementing Decision (EU) 2015/2429, Latvia submitted, together with the extension request, a report including the review of the percentage set for the limitation of the right to deduct VAT referred to in Article 1 of that Implementing Decision. Based on currently available information, namely tax audit experience and statistical data relating to private use of passengers cars, Latvia claims that the limit of 50% is still justifiable and remains appropriate.

(6) Given the positive impact of the special measure on the administrative burden of the taxpayers and of tax authorities by simplifying VAT collection and preventing tax evasion through incorrect record keeping, the Commission therefore considers it appropriate to authorise Latvia to continue to apply the special measure.

(7) It is appropriate to limit the extension of the special measure in time to allow for an evaluation of its effectiveness and of the appropriate percentage. Latvia should therefore be authorised to continue to apply the special measure until 31 December 2027.

(8) The special measure is proportionate to the objectives pursued, namely, to simplify the procedure for collecting VAT and to prevent certain forms of tax evasion or avoidance, since it is limited in time and scope. In addition, the special measure does not give rise to the risk that fraud would shift to other sectors or to other Member States.

(9) In the event that Latvia considers that a further extension of the special measure is necessary beyond 2027, it should submit to the Commission a report that includes a review of the percentage applied, together with the extension request, by 31 March 2027.

(10) 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.

(11) Implementing Decision (EU) 2015/2429 should therefore be amended accordingly,

HAS ADOPTED THIS DECISION:

Article 1

Article 6 of Implementing Decision (EU) 2015/2429 is replaced by the following:

'*Article 6*

1. This Decision shall expire on 31 December 2027.

2. Any request for the extension of the authorisation provided for in this Decision shall be submitted to the Commission by 31 March 2027 and shall be accompanied by a report which includes a review of the percentage set out in Article 1.'.

Article 2

This Decision is addressed to the Republic of Latvia.

Done at Brussels,

For the Council
The President