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PROPOSAL

From:	Secretary-General of the European Commission, signed by Mr Jordi AYET PUIGARNAU, Director
date of receipt:	9 August 2017
To:	Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union
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Subject:	Proposal for a COUNCIL IMPLEMENTING DECISION amending Implementing Decision 2014/797/EU authorising the Republic of Estonia to apply a measure derogating from point (a) of Articles 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(2017) 421 final.

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Proposal for a

COUNCIL IMPLEMENTING DECISION

amending Implementing Decision 2014/797/EU authorising the Republic of Estonia to apply a measure derogating from point (a) of Articles 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 ('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 18 April 2017, Estonia requested an extension of the derogation from Article 168 of the VAT Directive in order to continue to restrict the right to deduct the input VAT on expenditure connected with passenger cars. In accordance with Article 395(2) of the VAT Directive, the Commission informed the other Member States by letter dated 14 June 2017 of the request made by Estonia. By letter dated 15 June 2017, the Commission notified Estonia 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

Articles 168 and 168a of the VAT Directive provide 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.

Estonia is currently authorised on the basis of Council Implementing Decision 2014/797/EU¹ to restrict to 50 % the right to deduct VAT on the purchase, leasing, intra-Community acquisition, and importation of certain passenger cars as well as expenditure related thereto. This Decision shall expire on 31 December 2017.

Estonia has requested to prolong the authorisation to limit the initial deduction to a set percentage and in turn to relieve the business from accounting for tax on the private use. Estonia informed the Commission that the grounds for the prolongation of the measure are largely the same as described in the previous request. The application for a derogation is a continuation of the arrangements provided for in the aforementioned Council Decision. In accordance with Article 6 of Council Decision 2014/797/EU, Estonia has also presented a report informing that from the moment of the implementation of the derogation, companies have declared that around 66% of the cars owned by them are used partly for business-related purposes confirming that the derogation is justified.

¹ Council Implementing Decision 2014/797/EU of 7 November 2014 authorising the Republic of Estonia to apply a 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 330, 15.11.2014, p. 48).

The measure will apply to all passenger cars with a maximum of eight seats in addition to the driver's seat, not exceeding 3500 kilograms and which are not used exclusively for business purposes. However, passenger cars which are used for certain specific activities would 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), and cars used for driving lessons.

The restriction to the right of deduction limit should apply to VAT paid on the purchase, leasing, intra-Community acquisition, and importation of specified passenger cars as well as expenditure related thereto.

According to Estonia, the deduction limit should be set at 50%. The estimated extent of company cars use for private purposes in Estonia is around 60%. However as this is based on indirect evidence and assumptions and thus could be overestimated, the 50% input VAT deduction limit is the most appropriate.

The derogation should be limited in time to 31 December 2020, so that it can be assessed 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 with that request by 31 March 2020.

- **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.

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.

Notwithstanding previous initiatives to establish rules on which categories of expenditure may be subject to a restriction on the right to deduct², 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 therefore does not apply.

² 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)

- **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 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.

- **Choice of the instrument**

Proposed instrument: Council Implementing Decision.

Under Article 395 of Council Directive 2006/112/EC, derogation from the common VAT rules 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 Estonia 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 counter VAT evasion and to simplify the procedure for charging tax and has, therefore, a potential positive impact for both businesses and administrations. The solution has been identified by Estonia as a suitable measure and is comparable to other past and present derogations.

4. BUDGETARY IMPLICATIONS

The proposal will have no negative implication for the EU budget.

5. OTHER ELEMENTS

The proposal includes a sunset clause; an automatic time limit which is set at 31 December 2020.

In case Estonia would consider another extension of the derogating measure beyond 2020, 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 2020.

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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 tax³, and in particular Article 395(1) thereof,

Having regard to the proposal from the European Commission,

Whereas:

- (1) 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 purposes of his taxed transactions. Point (a) of Article 26(1) of that Directive contains a requirement to account for VAT when a business asset is put to use for private purposes of the taxable person or his staff or, more generally, for purposes other than those of his business.
- (2) Council Implementing Decision 2014/797/EU⁴ authorised Estonia to restrict the right to deduct VAT on the purchase, leasing, intra-Community acquisition and importation of certain passenger cars and to relieve the taxable person from accounting for VAT on the non-business use of vehicles covered by the restriction.
- (3) By letter registered with the Commission on 18 April 2017, Estonia requested an authorisation to continue to apply special measures concerning the purchase, leasing, intra-Community acquisition, and importation of certain passenger cars, derogating from the provisions laid down in Directive 2006/112/EC which govern a taxable person's right to deduct VAT paid on the purchase of goods and services and those which require tax to be accounted for on business assets used for non-business purposes.
- (4) In accordance with Article 395(2) of Directive 2006/112/EC, the Commission informed the other Member States by letter dated 14 June 2017 of the request made by

³ OJ L 347, 11.12.2006, p. 1.

⁴ Council Implementing Decision 2014/797/EU of 7 November 2014 authorising the Republic of Estonia to apply a 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 330, 15.11.2014, p. 48).

Estonia. By letter dated 15 June 2017, the Commission notified Estonia that it had all the information it considered necessary for appraisal of the request.

- (5) In accordance with Article 6(2) of Implementing Decision 2014/797/EU Estonia submitted, together with the extension request, a report to the Commission on the application of that Implementing Decision, including a review of the percentage restriction applied on the right of deduction. Based on currently available information, Estonia submits that a rate of 50% is still justifiable and remains appropriate.
- (6) The extension of these derogating measures should be limited in time to allow for an evaluation of their effectiveness and of the appropriate percentage. Estonia should therefore be authorised to continue to apply the measure for a limited period, until 31 December 2020.
- (7) Where Estonia considers that an extension of the authorisation beyond 2020 is necessary, it should submit to the Commission a report which includes a review of the percentage limit applied together with the request for an extension no later than 31 March 2020.
- (8) The derogation will only have a 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.
- (9) Implementing Decision 2014/797/EU should therefore be amended accordingly,

HAS ADOPTED THIS DECISION:

Article 1

Article 6 of Implementing Decision 2014/797/EU is replaced by the following:

'Article 6

1. This Decision shall expire on 31 December 2020.
2. Any request for the extension of the authorisation provided for in this Decision shall be submitted to the Commission by 31 March 2020 and accompanied by a report which includes a review of the percentage set out in Article 1.'

Article 2

This Decision shall apply from 1 January 2018.

Article 3

This Decision is addressed to the Republic of Estonia.

Done at Brussels,

*For the Council
The President*