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2019/0229 (NLE)

Proposal for a

COUNCIL IMPLEMENTING DECISION

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

EXPLANATORY MEMORANDUM

Pursuant to Article 395(1) of Council 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 12 April 2019, Italy requested an extension of the derogation from Articles 168 and 26(1)(a) of the VAT Directive that it currently applies. In particular, Italy asks for an authorisation to continue to derogate from Article 168 by limiting to 40% the right to deduct input VAT charged on expenditure related to motorised road vehicles not wholly used for business purposes. In addition, Italy requests an authorisation to continue to derogate from Article 26(1)(a) by exempting from VAT the use for private purposes of vehicles included in the assets of a taxable person's business, where such vehicles are subject to a restriction of the right to deduct.

In accordance with Article 395(2) of the VAT Directive, the Commission informed the other Member States by letter dated 13 May 2019 on the request made by Italy. By letter dated 14 May 2019, the Commission notified Italy that it had all the information it considered necessary for the 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 VAT charged on purchases of goods or services used for the purposes of taxed transactions in the Member State where such transactions take place. Article 26(1)(a) of the same directive stipulates that the use for private purposes of goods forming part of the assets of a business shall be considered as a supply of services for consideration if the VAT on such goods was eligible for deduction.

In the case of motorised road vehicles forming part of the assets of a business, the application of the above provisions encounters a number of practical difficulties, in particular because it is not easy to distinguish between private and business use of those vehicles. In cases where records about the use of such vehicles are kept, they add an additional burden to both businesses and administrations in terms of maintaining and controlling them. Moreover, the application of those provisions may increase the risk of VAT abuse or fraud attempts, notably through a possible underreporting of the private use of such vehicles.

Italy is currently authorised to derogate from Article 168 of the VAT Directive by limiting to 40% the right to deduct VAT on the purchase of a vehicle, including contracts of assembly and the like, manufacture, intra-Community acquisition, importation, leasing or hire, modification, repair or maintenance, and expenditure on supplies or services performed in relation to vehicles and their use, including lubricants and fuel, provided that the vehicle in question is not used exclusively for business purposes. The derogation covers all motor vehicles but agricultural or forestry tractors, normally used for carrying persons or goods by road and having a total maximum weight lower than 3.5 tonnes and fewer than nine seats, including the driver's seat. In contrast, it does not cover expenditure relating entirely to the taxable person's business. This would be the case with vehicles that belong to the taxable

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

person's stock-in-trade in the exercise of their activity, and vehicles used as taxis, as well as vehicles used for instruction by driving schools, and those used for hire or leasing or by sales representatives.

Likewise, Italy is authorised to derogate from Article 26(1)(a) of the VAT Directive by exempting from VAT the use for private purposes of vehicles forming part of the assets of a taxable person's business where those vehicles are covered by the above derogation.

The authorisation for the derogating measures mentioned above was first granted by the Council by means of Decision 2007/441/EC of 18 June 2007[2] until 31 December 2010. Subsequently, the derogating measures were prolonged three times following Italy's request: Council Implementing Decision 2010/748/EU of 29 November 2010[3] extended them for the period 1 January 2011 until 31 December 2013; Council Implementing Decision 2013/679/EU of 15 November 2013[4] for the period 1 January 2014 until 31 December 2016; last, Council Implementing Decision 2016/1982/EU of 8 November 2016[5] for the period 1 January 2017 until 31 December 2019.

The present request from Italy to prolong further the derogation until 31 December 2022 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 of Decision 2007/441/EC.

The information provided by Italy demonstrates that the current rate of 40% is still appropriate because it corresponds to the current circumstances of the Italian economy with regard to the ratio of business and private use of the motorised road vehicles concerned. According to Italy's report, the Italian economy is dominated by microenterprises, which represent 99% of Italian firms and amount to some 5.2 million taxable persons. This is revealing about the difficulty for the authorities to verify the private and business use of motorised vehicles owned by such microenterprises. The predominance of microenterprises also justifies the adoption of simplification measures to ensure compliance with tax obligations.

Italy reports that those microenterprises have minimal turnover and in most cases only one employee, thus it can be assumed that the vehicles concerned are used for private purposes to a significant extent. It is estimated that the average rate of private use by Italian taxable persons of corporate vehicles subject to the derogation is around 60%. This is explained by the preponderance of microenterprises, which own most of the corporate vehicles circulating in Italy. Moreover, larger firms (with a turnover of above EUR 5 million) represent only 1% of the total, and allocate most of their corporate vehicles to employees or directors as a fringe benefit. In this regard, it is recalled that the payment of the tax on these fringe benefits falls to the employee (or director) who enjoys that benefit and who therefore lawfully uses the company car for personal and family purposes throughout the year. According to Italy, non-business use of vehicles of larger companies also amounts to more than 50%.

To justify the appropriateness of the percentage of 40%, Italy further refers to the judgment of the Court of Justice of the European Union in Case C-228/05 *Stradasfalti*[6], which held that a

[2] OJ L 165, 27.6.2007, p. 33.
[3] OJ L 318, 4.12.2010, p. 45.
[4] OJ L 316, 27.11.2013, p. 37.
[5] OJ L 305, 12.11.2016, p. 30.
[6] Judgment of the Court of 14 September 2006 in Case C-228/05, *Stradasfalti Srl v Agenzia delle Entrate - Ufficio di Trento*, ECLI:EU:C:2006:578.

restriction to the right to deduct for expenditure related to motorised vehicles previously in force in Italy did not comply with EU legislation. As a result of this judgment, Italy was obliged to establish a procedure for filing claims for the reimbursement of non-deducted VAT. The Italian legislator decided that taxpayers could claim reimbursement in two different ways: either through an "analytical filing" procedure, supplying evidence that the percentage rate of the deduction for which reimbursement was claimed was appropriate, or through an "online filing" procedure, using a 40% flat-rate reimbursement. Italy states that 95% of the claims for reimbursement followed the "online filing" procedure. In its view, this is a confirmation that the interested parties themselves acknowledge the suitability of this percentage rate for the economic landscape of Italy.

It is true that establishing a distinction between private and business use of corporate vehicles would entail onerous and disproportionate costs on keeping appropriate records as compared to the potential benefits, notably as regards sole traders and microenterprises. It could also give rise to legal disputes between the tax authorities and taxable persons resulting in additional costs.

The percentage rate of 40% appears to reflect adequately the actual business use of such vehicles. Indeed, applying a higher or a lower rate would lead to excessively high discrepancies between the set rate and the actual use of vehicles for business activities and private purposes. This rate is similar to the percentage used in other Member States.

The measures adopted by Decision 2007/441/EC are considered as a satisfactory compromise between the adopted rules and expensive, time-consuming and largely ineffective record keeping with the view to confirming that a particular vehicle has indeed been used for business activities.

The derogating measures are not expected to affect significantly the overall amount of the tax revenue of Italy collected at the stage of the final consumption. Likewise, they are not expected to adversely affect the Union's own resources accruing from VAT.

In the light of the above, and given that the EU legal framework and the factual situation remain unchanged, the requested extension of the derogating measures until 31 December 2022 appears to be justified. Therefore, it is proposed that the request be granted. Should Italy wish to ask for a further extension beyond 2022, it shall submit an extension request by 1 April 2022, accompanied by a report including a review of the percentage restriction applied.

- **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 then, it authorises Member States to maintain exclusions that were in place under national laws on 1 January 1979. On this basis, there is a number of 'stand still' provisions restricting the right to deduct VAT in relation to corporate motor vehicles.

Previous initiatives to establish rules on which categories of expenditure may be subject to a restriction on the right to deduct have failed[7]. Until those rules are harmonised at EU level, derogations such the present one are considered as appropriate.

The proposed measures are therefore consistent with the provisions of the VAT Directive.

2. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY

• Legal basis

Article 395 of the VAT Directive is the only possible legal basis.

• Subsidiarity (for non-exclusive competence)

Considering the provision of the VAT Directive on which it is based, the proposal falls under the exclusive competence of the European Union. Hence, 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 tax collection 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 40% restriction would simplify the VAT collection procedure and would prevent tax evasion *inter alia* through incorrect record keeping.

• Choice of the instrument

The instrument proposed is a Council Implementing Decision.

Under Article 395 of the VAT Directive, a derogation from the common VAT rules is only possible upon authorisation by the Council, which is 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. The present proposal is based on a request made by Italy and concerns only this particular Member State.

• Collection and use of expertise

There was no need for external expertise.

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7 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).

- **Impact assessment**

The proposal aims to simplify the procedure for collecting VAT and to prevent VAT evasion. It has, therefore, a potential positive impact for both businesses and administrations. The derogating measures have been identified by Italy as the most appropriate solution. The measures are comparable to other past and present derogations granted to other Member States.

- **Fundamental rights**

The proposal does not have any consequences for the protection of fundamental rights.

4. BUDGETARY IMPLICATIONS

The proposal will not have a negative impact on the EU budget.

5. OTHER ELEMENTS

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

The proposal includes a sunset clause which is set at 31 December 2022.

In case Italy considers a further extension of the derogating measures beyond 2022, it should submit to the Commission an extension request accompanied by a report including a review of the percentage limit no later than 1 April 2022.

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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[8], and in particular the first subparagraph of Article 395(1) thereof,

Having regard to the proposal from the European Commission,

Whereas:

(1) Article 168 of the Directive 2006/112/EC establishes a right for taxable persons to deduct value added tax (VAT) charged on supplies of goods and services that they use for the purposes of their taxed transactions. Article 26(1)(a) of that Directive treats the use of business assets by taxable persons or their staff for private purposes or, more generally, for purposes other than those of their business as a supply of services for consideration.

(2) Council Decision 2007/441/EC[9] authorises Italy to limit the right under Article 168 of Directive 2006/112/EC to deduct VAT to 40% in the case of VAT charged on certain expenditure on certain motorised road vehicles not wholly used for business purposes. For vehicles subject to that 40% limit, Italy is required to relieve taxable persons from having to treat their use for private purposes as a supply of services for consideration in accordance with Article 26(1)(a) of Directive 2006/112/EC. Decision 2007/441/EC, which has been extended several times, is due to expire on 31 December 2019.

(3) By letter registered with the Commission on 12 April 2019, Italy requested authorisation to continue to apply the derogating measures authorised by Decision 2007/441/EC ('the derogating measures') for a further period until 31 December 2022.

(4) By letter dated 13 May 2019, the Commission informed the other Member States, pursuant to the second subparagraph of Article 395(2) of Directive 2006/112/EC, of the request that had been made by Italy. By letter dated 14 May 2019, the Commission notified Italy that it had all the information necessary to consider the request.

(5) Alongside the request, Italy submitted a report to the Commission, in accordance with Article 6 of Decision 2007/441/EC, including a review of the percentage limitation applied on the right to deduct VAT. Based on the information currently available, Italy maintains that a rate of 40% is still justified. Italy also maintains that suspending the

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

[9] Council Decision 2007/441/EC of 18 June 2007 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 165, 27.6.2007, p. 33).

requirement to account for VAT on the private use of a motor vehicle subject to that 40% limit is still necessary to ensure that the measure is complete and consistent. This would prevent double taxation. Those derogating measures are justified by the need to simplify the procedure for collecting VAT and to prevent tax evasion resulting from incorrect record-keeping and false tax declarations.

(6) Extension of the derogating measures should be limited to the time needed to evaluate the effectiveness of the derogating measures and the appropriateness of the percentage. Italy should therefore be authorised to continue to apply the derogating measures until 31 December 2022.

(7) A deadline should be set for requesting authorisation for any further extension of the derogating measures beyond 2022 which Italy may consider necessary. Italy should be required to submit a report alongside any such extension request, including a review of the percentage restriction applied on the right to deduct VAT.

(8) The derogating measures will only have a negligible effect on the overall amount of tax collected at the stage of final consumption and will not adversely affect the Union's own resources accruing from VAT.

(9) Decision 2007/441/EC should be therefore amended accordingly,

HAS ADOPTED THIS DECISION:

Article 1

Decision 2007/441/EC is amended as follows:

(1) Article 6 is replaced by the following:

'*Article 6*

Any request for authorisation to extend the derogating measures authorised by this Decision shall be submitted to the Commission by 1 April 2022. The request shall be accompanied by a report including a review of the percentage restriction applied on the right to deduct VAT on the basis of this Decision.';

(2) Article 7 is replaced by the following:

'*Article 7*

This Decision shall expire on 31 December 2022.'.

Article 2

This Decision is addressed to the Italian Republic.

Done at Brussels,

For the Council
The President