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2020/0138 (NLE)

Proposal for a

COUNCIL IMPLEMENTING DECISION

amending Implementing Decision (EU) 2017/2408 authorising the Republic of Latvia to apply a special measure derogating from Article 287 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 valued 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 17 April 2020, Latvia requested an authorisation to continue to apply, until 31 December 2024, a measure derogating from Article 287 of the VAT Directive, allowing Latvia to exempt from VAT taxable persons whose annual turnover is no higher than EUR 40 000.

In accordance with Article 395(2) of the VAT Directive, the Commission informed the other Member States by letter dated 19 May 2020 of the request made by Latvia. The Commission notified Latvia by letter dated 20 May 2020 that it had all the information necessary to consider the request.

1. CONTEXT OF THE PROPOSAL

• Reasons for and objectives of the proposal

Chapter 1 of Title XII of the VAT Directive allows for the possibility for Member States to apply special schemes for small enterprises, including the possibility of exempting taxable persons below a certain annual turnover. This exemption implies that a taxable person does not have to charge VAT on his supplies and, consequently, he or she cannot deduct the VAT on his inputs.

Under Article 287(10) of the VAT Directive, Latvia may exempt from VAT taxable persons whose annual turnover is no higher than the equivalent in national currency of EUR 17 200 at the conversion rate on the day of its accession. By virtue of Council Implementing Decision 2010/584/EU[2] Latvia was authorised to apply a higher threshold and thus to exempt from VAT taxable persons with an annual turnover not exceeding EUR 50 000. This measure was extended by Council Implementing Decision 2014/796/EU[3] until 31 December 2017. By Council Implementing Decision (EU) 2017/2408[4], Latvia was authorised to extend the measure until 31 December 2020 and, at the same time, to decrease the exemption threshold from EUR 50 000 to EUR 40 000.

According to the Latvian authorities, the measure facilitates VAT collection, enabling Latvia to simplify administrative procedures for small enterprises and thus reduce the administrative burden on them. Moreover, the measure also reduces the workload for the tax authorities.

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

[2] Council Implementing Decision 2010/584/EU of 27 September 2010 authorising the Republic of Latvia to apply a measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 256, 30.9.2010, p. 29).

[3] Council Implementing Decision 2014/796/EU of 7 November 2014 authorising the Republic of Latvia to apply a measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 330, 15.11.2014, p. 46-47).

[4] Council Implementing Decision (EU) 2017/2408 of 18 December 2017 authorising the Republic of Latvia to apply a special measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 342, 21.12.2017, p. 8-9).

Further, the Latvian authorities explain that in the last years they observed a reduction in the number of registered VAT payers, partly due to the faster removal of VAT payers from the VAT register as a result of measures adopted to combat VAT fraud, while the VAT revenue continued to increase and the cost incurred by the Latvian tax administration to collect one euro decreased. Those results, coupled with the fact that Latvia´s neighbouring countries have similar thresholds for the application of the special scheme for small enterprises (the threshold in Estonia is fixed at EUR 40 000 while the threshold in Lithuania is of EUR 45 000), advise to maintain the threshold at the current level. According to the estimates of the Latvian authorities, lowering the threshold further will not have a major positive fiscal impact or increase the number of persons registered for VAT purposes, because, as actual data for 2018 show, the impact in fiscal terms and in terms of the number of enterprises was lower than forecast. By contrast, increasing it, for example to EUR 50 000, would have a negative fiscal impact.

The measure has an optional character. Therefore, small businesses whose turnover does not exceed the threshold will still have the possibility to exercise their right to apply the normal VAT arrangements.

Derogations are normally granted for a limited period to allow an assessment of whether the derogating measure remains appropriate and effective. Moreover, the provisions of Articles 281 to 294 of the VAT Directive on the special scheme for small enterprises have recently been reviewed. The new directive laying down simpler VAT rules for small enterprises[5] requires that Member States adopt and publish the laws, regulations and administrative provisions, which are necessary to comply with the new rules, by 31 December 2024 at the latest. Member States will have to apply those national provisions from 1 January 2025.

It is therefore appropriate to authorise Latvia to apply the derogating measure until 31 December 2024.

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

The derogating measure is in line with the philosophy of the new directive amending Articles 281 to 294 of the VAT Directive on a special scheme for small enterprises, which resulted from the VAT action plan[6], and aims to create a modern, simplified scheme for those businesses. In particular, it seeks to reduce VAT compliance costs and distortions of competition both domestically and at EU level, reduce the negative impact of the threshold effect, and facilitate business compliance as well as monitoring by tax administrations.

Moreover, the threshold of EUR 40 000 is consistent with the new directive, insofar as it allows Member States to set the annual turnover threshold required for an exemption from VAT at a level no higher than EUR 85 000 (or the equivalent in national currency).

Similar derogations, exempting from VAT taxable persons whose annual turnover is below a certain threshold, as provided for in Articles 285 and 287 of the VAT Directive, have been

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[5] Council Directive (EU) 2020/285 of 18 February 2020 amending Directive 2006/112/EC on the common system of value added tax as regards the special scheme for small enterprises and Regulation (EU) No 904/2010 as regards the administrative cooperation and exchange of information for the purpose of monitoring the correct application of the special scheme for small enterprises (OJ L 62, 2.3.2020, p.13).

[6] Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee on an action plan on VAT – Towards a single EU VAT area – Time to decide COM(2016)148 final.

granted to other Member States. Malta[7] has been granted a threshold of EUR 20 000; the Netherlands[8] a threshold of EUR 25 000; Italy[9] a threshold of EUR 30 000; Luxembourg[10] a threshold of EUR 35 000; Poland[11] and Estonia[12] have been granted a threshold of EUR 40 000; Croatia[13] and Lithuania[14] a threshold of EUR 45 000; Hungary[15] a threshold of EUR 48 000; Slovenia[16] a threshold of EUR 50 000; and Romania[17] a threshold of EUR 88 500.

As already mentioned, derogations from the VAT Directive should always be limited in time so that their effects can be assessed. The inclusion of an expiry date of the special measure until 31 December 2024, as requested by Latvia, is aligned with the requirements of the new directive on simpler VAT rules for small and medium-sized enterprises. That directive provides for 1 January 2025 as the date on which Member States will have to apply the national provisions, which they are required to adopt to comply with it.

The proposed measure is therefore consistent with the provisions of the VAT Directive.

- **Consistency with other Union policies**

The Commission has been consistently stressing the need for simpler rules for small enterprises in its annual work programmes. In this regard, the 2020 Commission Work

7 Council Implementing Decision (EU) 2018/279 of 20 February 2018 authorising Malta to apply a special measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 54, 24.2.2018, p. 14).

8 Council Implementing Decision (EU) 2018/1904 of 4 December 2018 authorising the Netherlands to introduce a special measure derogating from Article 285 of Directive 2006/112/EC on the common system of value added tax (OJ L 310, 6.12.2018, p. 25).

9 Council Implementing Decision (EU) 2016/1988 of 8 November 2016 amending Implementing Decision 2013/678/EU authorising the Italian Republic to continue to apply a special measure derogating from Article 285 of Directive 2006/112/EC on the common system of value added tax (OJ L 306, 15.11.2016, p.11-12).

10 Council Implementing Decision (EU) 2019/2210 of 19 December 2019 amending Implementing Decision 2013/677/EU authorising Luxembourg to introduce a special measure derogating from Article 285 of Directive 2006/112/EC on the common system of value added tax (OJ L 332, 23.12.2019, p. 155).

11 Council Implementing Decision (EU) 2018/1919 of 4 December 2018 amending Decision 2009/790/EC authorising the Republic of Poland to apply a measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 311, 7.12.2018, p. 32).

12 Council Implementing Decision (EU) 2017/563 of 21 March 2017 authorising the Republic of Estonia to apply a special measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 80, 25.3.2017, p.33)

13 Council Implementing Decision (EU) 2017/1768 of 25 September 2017 authorising the Republic of Croatia to introduce a special measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 250, 28.9.2017, p. 71).

14 Council Implementing Decision (EU) 2017/1853 of 10 October 2017 amending Implementing Decision 2011/335/EU authorising the Republic of Lithuania to apply a measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 265, 14.10.2017, p. 15).

15 Council Implementing Decision (EU) 2018/1490 of 2 October 2018 authorising Hungary to introduce a special measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 252, 8.10.2018, p.38).

16 Council Implementing Decision (EU) 2018/1700 of 6 November 2018 amending Implementing Decision 2013/54/EU authorising the Republic of Slovenia to introduce a special measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 285, 13.11.2018, p. 78).

17 Council Implementing Decision (EU) 2017/1855 of 10 October 2017 authorising Romania to apply a special measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 265, 14.10.2017, p. 19)

Programme[18] refers to "a dedicated SME Strategy that will make it easier for small and medium-sized businesses to operate, scale up and expand". The derogating measure is in line with such objectives, as far as fiscal rules are concerned. It is notably consistent with the 2017 Commission Work Programme[19], which referred specifically to VAT, pointing out that the administrative burden of VAT compliance for small businesses is high and that technical innovations pose new challenges for effective tax collection, and stressed the need to simplify VAT for smaller companies.

Likewise, the measure is consistent with the 2015 single market strategy[20], where the Commission set out to help small and medium-sized businesses grow, inter alia by reducing the administrative burdens that prevent them from taking full advantage of the single market. It also follows the philosophy of the 2013 Commission Communication 'Entrepreneurship 2020 Action Plan: Reigniting the entrepreneurial spirit in Europe'[21], which underlined the need to simplify tax legislation for small businesses.

Finally, the measure is in line with EU policies on small and medium-sized enterprises, as set out in the 2016 Start-Up Communication[22], and the 2008 Communication '"Thinks small first" – a "Small Business Act" for Europe'[23] which called on the Member States to take account of the special features of SMEs when designing legislation and simplify the existing regulatory environment.

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 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.

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18 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions – Commission Work Programme 2020 – A Union that strives for more (COM(2020) 37 final).

19 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions – Commission Work Programme 2017 (COM(2016) 710 final).

20 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions upgrading the Single Market: more opportunities for people and businesses (COM(2015) 550 final).

21 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions – Entrepreneurship 2020 Action Plan: Reigniting the entrepreneurial spirit in Europe (COM(2012) 795 final).

22 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions – Europe's Next Leaders: The Start-Up and Scale-Up Initiative (COM(2016) 733 final).

23 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions 'Think Small First' A 'Small Business Act' for Europe (COM(2008) 394 final).

Given the limited scope of the derogation, the special measure is proportionate to the aim pursued, i.e. to simplify the tax collection for small taxable persons and for the tax administration.

- **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 Latvia and concerns only this particular Member State.

- **Collection and use of expertise**

There was no need for external expertise.

- **Impact assessment**

The proposal for a Council Implementing Decision authorises Latvia to continue to exempt from VAT taxable persons whose annual turnover does not exceed EUR 40 000. Persons whose taxable turnover does not exceed the threshold do not have to register for VAT purposes, and thus the administrative burden on them will reduce as a result of the measure, since they will not need to keep VAT records or submit a VAT return. Subsequently, the measure will have a potential positive impact on the tax administration as it will reduce its administrative burden.

According to the Latvian authorities, the lowering of the VAT registration threshold from EUR 50 000 to EUR 40 000 was forecast to generate an extra EUR 5.9 million of VAT revenue for the State budget and create an additional 3 426 new persons registering for VAT purposes per year. In order to determine the actual fiscal impact, account was taken of persons registered for VAT purposes whose total value of transactions for the 2018 VAT return was between EUR 40 000 and EUR 50 000 and who were not registered for VAT purposes in 2017. The fiscal impact is assumed to be the total amount of VAT declared by persons registered for VAT purposes, which in 2018 was EUR 2.8 million. The number of this type of registered VAT payer is 2 636, which can be taken to be the increase in the number of VAT payers created by this measure. Data from VAT returns for 2019 show that persons registered for VAT purposes with a total value of transactions declared in VAT returns of between EUR 40 000 and EUR 50 000, generated EUR 10.7 million of revenue for the State budget, compared with the EUR 5.8 million generated in 2018. The Latvian authorities therefore conclude that the fiscal impact on the State budget from this measure is positive, although slightly lower than previously forecasted.

In the view of the Latvian authorities, lowering the threshold further will not have a major positive fiscal impact or increase the number of persons registered for VAT purposes, because, as actual data for 2018 show, the impact in fiscal terms and in terms of the number of enterprises was lower than forecast. By contrast, increasing it, for example to EUR 50 000, would have a negative fiscal impact.

The derogating measure will be optional for taxable persons. Taxable persons will be able to opt for the regular VAT arrangements in accordance with Article 290 of Directive 2006/112/EC.

- **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 because Latvia will carry out a compensation calculation in accordance with Article 6 of Council Regulation (EEC, EURATOM) 1553/89.

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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) Pursuant to point (10) of Article 287 of Directive 2006/112/EC, Latvia may exempt taxable persons whose annual turnover is no higher than the equivalent in national currency of EUR 17 200 from value added tax ('VAT') at the conversion rate on the day of its accession.

(2) By Council Implementing Decision 2010/584/EU[2] Latvia was authorised to introduce a special measure derogating from Article 287 of Directive 2006/112/EC ('the derogating measure') to exempt taxable persons whose annual turnover was no higher than EUR 50 000 from VAT until 31 December 2013. The derogating measure was extended by Council Implementing Decision 2014/796/EU[3] until 31 December 2017.

(3) By Council Implementing Decision (EU) 2017/2408[4], Latvia was both authorised to further extend the derogating measure until 31 December 2020, and to decrease the exemption threshold from EUR 50 000 to EUR 40 000.

(4) By letter registered with the Commission on 17 April 2020, Latvia requested authorisation to continue to apply the derogating measure until 31 December 2024, being the date by which Member States are to transpose Council Directive (EU) 2020/285[5], which lays down simpler VAT rules for small enterprises. That Directive

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

[2] Council Implementing Decision 2010/584/EU of 27 September 2010 authorising the Republic of Latvia to apply a measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 256, 30.9.2010, p. 29).

[3] Council Implementing Decision 2014/796/EU of 7 November 2014 authorising the Republic of Latvia to apply a measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 330, 15.11.2014, p. 46).

[4] Council Implementing Decision (EU) 2017/2408 of 18 December 2017 authorising the Republic of Latvia to apply a special measure derogating from Article 287 of Directive 2006/112/EC on the common system of value added tax (OJ L 342, 21.12.2017, p. 8).

[5] Council Directive (EU) 2020/285 of 18 February 2020 amending Directive 2006/112/EC on the common system of value added tax as regards the special scheme for small enterprises and Regulation (EU) No 904/2010 as regards the administrative cooperation and exchange of information for the

also lays down the maximum threshold allowing Member States to exempt taxable persons whose Member State annual turnover does not exceed EUR 85 000 or the equivalent in national currency.

(5) By letter dated 19 May 2020, the Commission informed the other Member States, pursuant to Article 395(2) of Directive 2006/112/EC, second subparagraph, of the request made by Latvia. By letter dated 20 May 2020, the Commission notified Latvia that it had all the information necessary to consider the request.

(6) The derogating measure is in line with Directive (EU) 2020/285, which seeks to reduce VAT compliance costs of small enterprises and distortions of competition both at national and Union level, and to reduce the negative impact of transition from exemption to taxation (the so-called threshold effect). It also seeks to facilitate business compliance by small enterprises as well as monitoring by tax administrations. The threshold of EUR 40 000 is consistent with Article 284 of Directive 2006/112/EC, as amended by Directive (EU) 2020/285.

(7) The derogating measure will remain optional for taxable persons. Taxable persons may still opt for the normal VAT arrangements in accordance with Article 290 of Directive 2006/112/EC.

(8) According to the information provided by Latvia, the derogating measure will only have a negligible effect on the overall amount of the tax revenue of Latvia collected at the stage of final consumption.

(9) The derogating measure will not adversely affect the Union's own resources accruing from VAT because Latvia will carry out a compensation calculation in accordance with Article 6 of Council Regulation (EEC, Euratom) No 1553/89[6].

(10) Given the potential positive impact of the derogating measure in reducing the administrative burden and compliance costs for small enterprises and for the tax authorities, and the lack of any major impact on the total VAT revenue generated, Latvia should be authorised to continue applying the derogating measure.

(11) The authorisation to apply the derogating measure should be limited in time. The time limit should be sufficient to allow the effectiveness and appropriateness of the threshold to be evaluated. Moreover, according to Directive (EU) 2020/285, Member States are to adopt and publish, by 31 December 2024, the laws, regulations and administrative provisions necessary to comply with Article 1 of that Directive, and apply those provisions from 1 January 2025. It is therefore appropriate to authorise Latvia to apply the derogating measure until 31 December 2024.

(12) Implementing Decision (EU) 2017/2408 should therefore be amended accordingly,

HAS ADOPTED THIS DECISION:

Article 1

In Article 2 of Implementing Decision (EU) 2017/2408, the second paragraph is replaced by the following:

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purpose of monitoring the correct application of the special scheme for small enterprises (OJ L 62, 2.3.2020, p. 13).

6 Council Regulation (EEC, Euratom) No 1553/89 of 29 May 1989 on the definitive uniform arrangements for the collection of own resources accruing from value added tax (OJ L 155, 7.6.1989, p. 9).

‘This Decision shall apply until 31 December 2024.’.

Article 2

This Decision is addressed to the Republic of Latvia.

Done at Brussels,

For the Council
The President