

Opinion of the European Economic and Social Committee on the ‘Proposal for a Council Directive amending Directive 2006/112/EC on the common system of value added tax as regards the temporary application of a generalised reverse charge mechanism in relation to supplies of goods and services above a certain threshold’

(COM(2016) 811 final — 2016/0406 (CNS))

(2017/C 288/06)

Rapporteur: **Giuseppe GUERINI**

Consultation	European Council, 25.1.2017
Legal basis	Article 113 of the Treaty on the Functioning of the European Union
Plenary Assembly decision	13.12.2016
Section responsible	Economic and Monetary Union and Economic and Social Cohesion
Adopted in section	6.4.2017
Adopted at plenary	31.5.2017
Plenary session No	526
Outcome of vote (for/against/abstentions)	142/1/1

1. Conclusions and recommendations

1.1 The EESC supports the measures that the European Union has put in place to tackle all forms of tax fraud and takes the view that the reverse charge mechanism for collecting value added tax (VAT) may be a useful tool in countering carousel fraud and VAT evasion.

1.2 However, the use of the reverse charge mechanism, which is a derogation from the established principles on VAT, must not be allowed to harm the internal market and it must be temporary and properly assessed by the Commission in relation to the possible negative effects on the internal market. The EESC is worried about the risk of a possible fragmentation of the VAT system deriving from the proposed measures, also considering the steps envisaged in the first stage of the Commission’s VAT Action Plan, which is currently supposed to apply only to certain supplies of goods and not to services ⁽¹⁾.

1.3 In particular, it will be necessary to assess whether the benefits brought about when tackling fraud are offset by the possible adverse effects on the cohesion of the single market. For this reason, the Commission should constantly monitor the functioning of the Generalised Reverse Charge Mechanism (GRCM), retaining the power to intervene in the event of adverse effects.

1.4 The EESC recommends focusing particular attention on the proportionality principle, as the cost of compliance for small and medium-sized enterprises (SMEs) related to introducing a reverse charge mechanism could be considerable and may have an impact on cash flow with the risk that SMEs in particular may experience liquidity problems induced by the GRCM.

1.5 The EESC draws attention to studies ⁽²⁾ that have shown that reverse charge and split payment mechanisms have, where implemented so far, often caused cash flow problems for tax compliant enterprises. In other words, attempts to combat tax fraud by a small number of dishonest businesses have caused major operational problems for tax-abiding economic operators, which create jobs and wealth in the internal market.

⁽¹⁾ OJ C 389, 21.10.2016, p. 43, point 1.3.

⁽²⁾ See the study of Italian association of craftsmanship: CNA, Reverse Charge e Split Payment: in Fumo la Liquidità delle Imprese, 2015.

1.6 The EESC emphasises that solutions adopted to combat VAT fraud should not impose excessive and disproportionate burdens on tax compliant businesses, particularly SMEs. Indeed, as stated earlier by the EESC with regard to the Commission VAT Action plan, *bona fide* enterprises should be protected and no new excessive measures should be imposed on them⁽³⁾.

1.7 The EESC notes that the national dimension of the fight against tax fraud requires that all Member States take full responsibility for the functioning of their own tax systems and that they provide instruments to tackle VAT fraud that do not damage or influence the functioning of tax systems in other Member States.

1.8 Overall, for the EESC, the proposed measures should not affect negatively the objectives set out in the VAT Action plan, nor hinder or delay its complete and timely realisation. The Committee believes that now is time to take a qualitative step forward (a 'quantum leap') in this field to support the single market and contribute to employment, growth, investments and competitiveness. Furthermore, in the Committee's view, it is important to implement all parts of the Action Plan as an indivisible whole⁽⁴⁾.

1.9 To ensure that this legislative proposal functions correctly and to reduce any future need to use additional derogations relating to the established principles and rules on the VAT system in the EU, Member States requesting the application of the GRCM should impose specific and tangible electronic invoicing requirements to ensure that payments are fully traceable.

2. Commission proposal

2.1 In its communication of 7 April 2016, the European Commission presented its Action Plan on VAT. A legislative proposal to reform and modernise the current European rules on VAT will follow in 2017.

2.2 Both the Commission's Action Plan and the future legislative proposal scheduled for 2017 seek, inter alia, to close the 'VAT gap' — the difference between expected and actual VAT revenue — by minimising fraud associated with VAT.

2.3 Pending completion of the reform of the European VAT system and at the behest of some national governments, the Commission has recognised the urgent need to allow some Member States to introduce Generalised Reverse Charge Mechanisms (GRCM) on a temporary basis.

2.4 The Commission has developed the GRCM in the proposal for a Directive (2016/0406 — CNS) amending Directive 2006/112/EC, which forms the subject of this opinion.

2.5 Given that the GRCM derogates from one of the fundamental principles of EU VAT legislation, fractioned payments, the Commission has decided to allow Member States to apply it only under specific conditions.

2.6 Specifically: a) the Member State must have a VAT gap exceeding the EU median VAT gap by 5 percentage points; b) carousel fraud must account for more than 25 % of the Member State's VAT gap; c) it must be established that other control measures are not sufficient to combat fraud on the Member State's territory.

2.7 To prevent the generalised application of the reverse charge mechanism resulting in the fragmentation of the internal market, a possibility which has been highlighted by some Member States, the Commission has provided for the option of reviewing the application of the mechanisms where they are shown to have an adverse impact on the internal market, in conflict with the overarching objectives of the EU.

3. General comments

3.1 VAT evasion is a European epidemic which must be combated. The most troubling form of VAT fraud is 'carousel fraud', which the VAT reverse charge mechanism seeks to prevent.

⁽³⁾ OJ C 389, 21.10.2016, p. 43, point 1.9.

⁽⁴⁾ OJ C 389, 21.10.2016, p. 43, points 1.1 and 1.2.

3.2 For this reason the EESC welcomes the introduction of appropriate mechanisms to tackle tax fraud, while noting that any derogation from the unitary nature of the European VAT system should be temporary, proportionate and adequately assessed in order to determine the possible negative effects on the internal market. This is especially the case in view of the fact that Article 113 of the Treaty, which underpins the Commission's legislative proposal, provides the possibility of taking action in the area of taxation through harmonisation measures which aim to guarantee the proper functioning of the internal market and to ensure that competition is not distorted.

3.3 Overall, the proposed measures should not negatively affect the objectives set out in the VAT Action plan, nor hinder or delay its complete and timely realisation. Now is the time to take a qualitative step forward (a 'quantum leap'), in order to support the single market and contribute to employment, growth, investment and competitiveness.

3.4 Furthermore, it is important to strive to implement all parts of the Action Plan as an indivisible whole, as this would also allow the lion's share of VAT frauds to be addressed in a comprehensive manner.

3.5 Compliance with the principle of proportionality referred to in the Commission's legislative proposal must therefore be ensured, and proper consideration given to the various public interests to be reconciled, including the general interest in not jeopardising the harmonisation of national VAT systems, with a view to fully consolidating the single market.

3.6 In view of the above, it should be acknowledged that tax evasion policy, including harmonised taxes, largely falls to the Member States and that tax authorities are highly domestic in character. Similarly, both statistical understanding of this issue and the practices and forms of evasion and of combating evasion have strong national ties.

3.7 From this point of view, an anti-tax evasion mechanism activated by the Member State and derogating from EU rules is consistent with the role and responsibilities entrusted to the national governments in the fight against tax fraud. In this regard, the Commission proposal complies with the principle of subsidiarity, enabling the Member States to take action at national level to combat illegal activity in the tax domain.

3.8 However, the EESC notes that the national dimension of the fight against tax fraud requires that all Member States take full responsibility for the functioning of their own tax systems and that they provide instruments to tackle VAT fraud that do not damage or influence the functioning of tax systems in other Member States.

3.9 The derogation provided for in the Commission proposal through the reverse charge mechanism is not a generalised measure, but instead is subject to specific conditions. Member States may request that this derogation be applied under specific conditions, but it remains entirely optional.

3.10 Member States requesting the derogation via the reverse charge mechanism must have a VAT gap exceeding the EU median by 5 percentage points. If we consider that the EU median is 14 %, a further 5 percentage points would appear to constitute sufficient and substantial grounds for the adoption of extraordinary measures to reduce the VAT gap ⁽⁵⁾.

3.11 Similarly, the Commission's proposal for a provision requiring that carousel fraud account for more than 25 % of the Member State's VAT gap would appear to be supported by preliminary evidence, if we compare that figure to the EU average (24 %) ⁽⁶⁾.

3.12 The EESC also supports the general provision whereby the Member State must be experiencing administrative difficulties in combating VAT fraud, as this condition shows that a GRM is the most effective and proportional method for meeting the objective of reducing the VAT gap, in line with the public interest of both the EU and the Member States.

3.13 The Commission proposal stipulates that the reverse charge mechanism is applicable to transactions worth more than EUR 10 000. We consider this *de minimis* rule to be acceptable, given the varied and often diametrically opposed interests which need to be considered simultaneously in combating tax evasion, harmonising tax systems and simplifying the administrative burden related to fiscal duties.

⁽⁵⁾ SWD(2016) 457 final, p. 18.

⁽⁶⁾ SWD(2016) 457 final, p. 15.

4. Specific comments

4.1 The regulatory impact assessment carried out by the Commission shows that the adoption of a GRM does not necessarily resolve all possible cases of fraud: on the contrary, new forms of fraud, or fraud in Member States other than those most affected at the present time may arise. The Commission should therefore monitor the functioning of the GRM properly, retaining the power to intervene in the event of adverse effects on the functioning of the European single market.

4.2 If the legislative proposal under examination in the present opinion is to function correctly and reduce any future need to use additional derogations relating to the established principles and rules on the VAT system in the EU, Member States requesting the application of the GRM should impose specific electronic invoicing requirements upon taxable persons to ensure that payments are fully traceable.

4.3 In this regard, the EESC would like to emphasise in particular the possibility of limiting or eliminating reverse charge and split payment mechanisms where electronic invoicing for the certification of sale proceeds is used widely and correctly. This invoicing method would make it possible to verify the correct payment of VAT in real time, thereby preventing harmful financial repercussions for many tax compliant businesses.

4.4 Tackling VAT fraud is without doubt an objective to be pursued vigorously and through the development of appropriate legislative measures by the Member States. Nevertheless, it should be noted that the application of reverse charge mechanisms in B2B relationships between private entities and split payment mechanisms in relationships between businesses and public administrations may heavily penalise tax compliant businesses.

4.5 Firstly, as has been shown by the regulatory impact assessment proposed by the Commission, the compliance costs linked with the use of the reverse charge mechanism on SMEs will be very high for domestic transactions and even higher for cross-border transactions. According to the Commission impact assessment, the reverse charge mechanism implies a 43 % increase in compliance costs for businesses ⁽⁷⁾. Although a generalised reverse charge is expected to generate less compliance costs than a reverse charge limited to a certain sector, this still shows that compliance costs will increase dramatically.

4.6 Secondly studies ⁽⁸⁾ have shown that reverse charge and split payment mechanisms have, where implemented so far, often caused cash flow problems for many tax compliant businesses.

4.7 In other words, attempts to combat tax fraud by a small number of dishonest businesses have caused major operational problems for tax-abiding economic operators, which create jobs and wealth in the internal market.

4.8 For this reason, the EESC reminds the Commission and the Member States that the principle of proportionality must be upheld within the Commission proposal and in the individual national legal systems, ensuring that the measures adopted are proportional to the need to combat VAT fraud without damaging the internal market. At the same time, in line with the very same principle, the solutions adopted should tackle illegal activities without imposing excessive and disproportionate burdens on honest businesses, particularly SMEs.

4.9 The above considerations are further arguments in favour of the transitional basis of the generalised mechanism. Otherwise, we will witness an unacceptable worsening of the administrative burden, particularly for SMEs, and at the same time a distortion in the dynamics of the European single market, as there is a serious risk of differentiated cash flow operations for companies located in different Member States.

Brussels, 31 May 2017.

The President
of the European Economic and Social Committee
Georges DASSIS

⁽⁷⁾ COM(2016) 811 final, p. 43.

⁽⁸⁾ OJ C 389, 21.10.2016, p. 43, point 1.9.