

THE HARMONISATION OF LEGISLATION ON COMBATING TAX EVASION IN THE EUROPEAN UNION

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Abstract

Combating tax evasion is part of the Lisbon Strategy. Tax fraud created a significant distortion in the functioning of the internal market and prevented fair competition.

In its resolution of 2th of September 2008 on a coordinated strategy to improve the fight against fiscal fraud (2008/2033 (INI)) the European Parliament stressed that the Member States cannot combat cross-border fraud in isolation and called on the Commission to propose mechanisms to promote cooperation between Member States.

This paper aims to analyse the main mechanisms to combat the tax evasion at the European level and, also, the changes that our country had to make in the field of legislation in order to achieve the EU standard on the fight against tax evasion.

Keywords: *tax evasion, fraude, harmonisation, VAT, Eurofisc*

Introduction

The harmonisation of fiscal legislation in the field of preventing and combating tax evasion constitutes an imperative for Member States of the European Union, especially in the current economic context. At present, there are many efforts to diminish the effects of fiscal evasion at a community level, especially in the case of VAT tax evasion. This is the reason why a document that contains proposals for the modification of legislation on the value added tax has been put forward for discussion, with the goal of unifying this legislation in the member states of the European Union.

The Member States cannot fight fiscal fraud each on its own, therefore cooperation mechanisms have been instituted among them.

The battle against tax fraud is a challenge for the European Union that goes beyond its borders and consequently it must be reflected in the international agreements concluded by the European Union with third party states or in multilateral covenants of which it is a signatory.

In order to efficiently combat fraud, the European Union negotiates agreements or multilateral covenants, on behalf of itself and the Member States.

The paper analyse the main mechanisms created in order to fight against the fiscal fraud at the European level and, also the measures that must be taken to achieve this goal. Those measures are underlined, especially, in the European Parliament Resolution from 2 September 2008. Part of them were already applied, but some of them are still object of a proposal submitted to the Member State's analyse, as the proposal of modifying the Directive concerning VAT.

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1. Measures on combating fiscal fraud in the European Union

The protection of their financial interests has been a main concern for the Member States of the European Union, so on 26 July 1955 it drew up the Convention on the Protection of the European Communities' Financial Interests. Any type of fraud that injures community interests is defined as¹: in respect of expenditure, any intentional act or omission relating to: “the use or presentation of false, incorrect or incomplete statements or documents, which has as its effect the misappropriation or wrongful retention of funds from the general budget of the European Communities or budgets managed by, or on behalf of, the European Communities, non-disclosure of information in violation of a specific obligation, with the same effect, the misapplication of such funds for purposes other than those for which they were originally granted” and in respect of revenue “the use or presentation of false, incorrect or incomplete statements or documents, which has as its effect the illegal diminution of the resources of the general budget of the European Communities or budgets managed by, or on behalf of, the European Communities, non-disclosure of information in violation of a specific obligation, with the same effect, misapplication of a legally obtained benefit, with the same effect.”

Pursuant to the provisions of the Convention, serious fraud is any type of fraud whose minimum value must be fixed by every Member State, though no more than 50 000 euros.

Article 3 from the Convention sanctions the principle, according to which leaders that exert a legal power or that head businesses cannot be automatically exonerated from any form of liability, when there is fraud affecting the financial interests of the European Union.

The text of the definition in the Convention has been assimilated into the national legislature, in Law 78/2000 on the prevention, discovery and punishment of acts of corruption, thus fulfilling the obligation stipulated by article 1, paragraph 2 from the Convention².

Tax fraud causes important distortions in the workings of the domestic market and constitutes an obstacle for loyal competition.

In its resolution from 2 September 2008 on a strategy coordinated for the intensifying of the fight against tax fraud (2008/2033 (INI)), the European Parliament highlights the fact that Member States cannot fight against cross-boarder tax fraud each on their own and therefore they appeal to the Commission to propose measures of promoting the cooperation between member states.

An efficient fight against VAT fraud in the domestic market requires a common approach both in the legislative field but also on certain aspects of the operational management of the VAT system, operational differences between Member States can provide fraudsters the opportunity to undermine the efficiency of subjacent community legislative measures.

The measures that the Commission was to propose or implement aimed to³: prevent the illegal use of the VAT system by potential fraudsters, consolidate the means used to detect TVA fraud and improve possibilities of collecting taxes lost due to fraud and the punishment of the tax evaders.

Measures for enhancing the tax system and fiscal cooperation with the goal of preventing VAT fraud impose: common minimum standards for the registration and deregistration of taxable persons⁴, confirmation of information, invoicing rules, chargeability on intra-Community transactions.

Among the measures for enhancing the efficiency of the tax administration in order to detect VAT fraud, we must mention the reduction of the timeframes for both the reporting of intra-

¹ Article 1 from the Convention on the Protection of the European Communities' Financial Interests.

² Ioana Maria Costea, *Combaterea evaziunii fiscale și fraudă comunitară*, (București: Ed. C.H.Beck, 2010), 289.

³ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2008:0807:FIN:EN:PDF>.

⁴ A correct and valid VAT identification number represents an essential element within the framework of current VAT systems, because it establishes the rules and obligations applicable especially in intra-Community commerce. Both financial administrations, as well as companies must be able to rely on the correct information concerning the VAT status of the economic agent.

Community transactions by traders and the exchange of information between tax administrations, exemption of VAT at importation, enhancing cooperation between Member States, automated access to data, the creation of a European network, called Eurofisc, for closer operational cooperation between Member States in the fight against VAT fraud.

The measures of enhancing the capacity of the tax administration to collect and recover taxes include several liability⁵, recovery of taxes - uniform instruments including enforcement or precautionary measures, which should reduce the administrative burden of the authorities concerned and allow quicker reactions -, shared responsibility for the protection of all revenues of Member States.

Concerning the rules of invoicing, Directive 2006/112/CE on the joint VAT system was amended through Directive 2010/45/UE⁶ by the Council, on 14 July 2010.

The directive contains measures in view of the simplification of different existing requirements concerning invoicing, including electronic invoicing. The directive stipulates the equal treatment applied to both invoices on paper and in electronic form, the principle applicable to both types being that the authenticity of the origin, the integrity of content and the legibility of the invoice should be ensured from the moment of issue until the invoice is placed in storage. The directive contains the method of electronic data exchange and the advanced electronic signatures, as well as the stipulations concerning self-invoicing, invoice simplification, translation of invoice, currency, centralised invoices, modifications concerning the origin and VAT changeability, the right to deduct VAT, etc.

Member States must adopt and implement the provisions of the directive by 31 December 2012.

On 6 October 2009, pursuant to article 93 of the Treaty establishing the European Community, the Council decided to consult the European Economic and Social Committee on the Proposal for a Council Directive amending Directive 2006/112/CE as regards an optional and temporary application of the reverse charge mechanism in relation to supplies of certain goods and services susceptible to fraud COM (2009) 511 final – 2009/0139 (CNS)⁷.

The EESC was in favour of the proposal for a Council Directive, which introduces a reverse charge mechanism for certain products and services.

The EESC has expressed its approval of the proposals contained in the European Parliament Resolution from 2 September 2008 concerning a coordinated strategy for enhancing the fight against tax fraud, especially taxation in the country of origin with a single 15% rate for intra-Community transactions. This option would conform to the provisions of article 402 from Directive 2006/112/EC.

Combating fiscal fraud, especially intra-Community fraud, has not made great progress these last years. Total fiscal losses caused by fraud amount to a sum between 200 and 250 billion EUR, the equivalent of 2% of the EU gross domestic product.

VAT fraud accounts for 40 billion EUR, i.e. 10% of revenues from this tax.

The progressive increase of exchanges has led to a proliferation of the so-called „carousel” fraud. Legislation on this matter stipulates that merchandise transiting through the EU should pass freely, the VAT on commercial transactions between Member States are to be collected in the country of destination.

By introducing a fictitious taxable person in the transaction, one obtains an illegal triad, which thus simulates the double transfer of the same goods. The buyer has the right to reclaim VAT, which has not been paid by the third conspirator however, who in turn has bought the VAT-exempt goods from a supplier from another Member State. The third conspirator thus vanishes.

⁵ The provision concerning several liability already exists in the VAT Directive, however until now Member States have used it only in national transactions.

⁶ http://discutii.mfinante.ro/static/10/Mfp/infotva/Directiva_2010_45_facturarea.pdf.

⁷ Official Journal C 339(14/12/2010): 0041 – 0044.

Due to the reverse charge mechanism, the supplier from the same Member State does not invoice the VAT to the taxable persons who, in turn, must pay this tax. Theoretically, the possibility of using the carousel fraud is eliminated by this procedure.

The contraindications of the system based on applying the country of destination principle, which – in order to function correctly – is conditioned by a consolidated and efficient system of exchanges of information between Member States, give rise to fiscal frauds, which are difficult to counteract. The Community has definitely opted for the country of origin principle, which provides a form of compensation between Member States, by redistributing VAT. Article 402 from Directive 2006/112/EC from 28 November 2006 states that taxation on intra-Community exchanges should be done in the country of origin.

Redistribution is necessary for the compensation effect on the revenue resulted from taxation, exportation and import tax deductions, which are already charged in the country of origin.

Adopting a permanent scheme, which should drastically reduce intra-Community fiscal fraud, needs a system integrated by administrative cooperation.

In order to counteract the growing cases of intra-Community fraud perpetrated through the so-called *missing traders* (Missing Trader Intra-Community fraud) better known as *carousel fraud* (given that it refers to the repeated transfer of the same goods between operators in different Member States), some Member States have appealed to the Commission to grant the derogation stipulated in article 395 of the EU VAT Directive, which allows the introduction of a temporary system of reverse taxation on certain goods and services.

The Commission considered that an amendment of the VAT Directive would be more suitable, by introducing article 199 a, which grants the derogation until 2014.

On the list of goods that might benefit from the optional introduction of this reverse charge system, there are among other things common appliances, such as mobile telephones and devices with integrated circuits. This scheme is already being used in the United Kingdom, which has been granted derogation from the Council.

Perfumes and objects made from precious metal, which are not collection pieces or antiquities, complete the list of the four types of goods given by the directive. The services include transactions with issued certificates.

Since 2008, the European Parliament has emphasized the risks connected with the possibility of new acts of fraud occasioned by the introduction of the generalised reverse charge system, especially in retailing and by the abusive utilisation of the VAT identification number, via an appeal addressed to the Council to act more decisively in the fight against fiscal fraud⁸. Parliament suggested in its resolution that the transit and charge policy of intra-Community delivery of goods should be surpassed by a rate of 15%, as an optimal solution.

The European Court of Justice has already decided on the matter of reverse taxation⁹. The decision refers to the request of payment from a tax administration, owing to a misinterpretation of the reverse charge mechanism. In order to avoid useless and costly proceedings, it will be necessary to verify the national legislations, which although applying general principles, present inadvertencies for example between the terms of the reimbursement requests and those for the payment of taxes.

The administrations of Member States which will adopt this system shall have to examine a great number of requests for the reimbursement of VAT surplus, filed by taxable persons who can no longer deduct the VAT previously charged.

The burden of paying this tax is transferred onto smaller and smaller economic operators, who may prove to be less reliable than the VAT taxpayers (medium-sized and large companies that pay

⁸ The European Parliament Resolution from 2 September 2008 on a coordinated strategy for the enhancement of the fight against fiscal fraud [2008/2033(INI)], JO C 295 E/13 from 04.12.2009.

⁹ Reunited cases C 95/07 and C 96/07 from 08.05.2008.

the most considerable part of the revenues obtained from these taxes). By eliminating the fragmented payments, the system increases the risk of losing fiscal revenues.

After a complete analysis, it seems that a rigorous control system is necessary, in order to protect Member States against the negative effects, which the reverse charge mechanism could occasion. It is necessary that the process of enhancing the monitoring measures take place at the same time as the consolidation of administrative cooperation and the utilisation of standard systems of information exchange between administrations.

A part of the European strategy to combat tax evasion and fraud in general, the European Council adopted on 7 October 2010, Regulation 904/2010 on administrative cooperation and combating fraud in the field of value added tax¹⁰ with the purpose of extending and strengthening the legal framework for the cooperation and exchange of information between the competent authorities of Member States. The regulation does not prevent Member States from applying the rules on mutual assistance in criminal matters.

Starting from the premise that, in order to collect due taxes, the Member States should not only monitor the correct application of the tax owed on its own territory, but it must also equally offer assistance to other Member States, so that it guarantees the correct application of the tax owed in another Member State as a result of activities on its own territory, the regulation establishes the conditions, in which the competent authorities from the Member States responsible for the application of VAT legislation should cooperate amongst themselves and with the Commission, in order to ensure the respective legislation.

Every Member State designates a single central liaison office, which has been delegated with the responsibility for contacts with the other member states in the field of administrative cooperation. The competent authority of every Member State may designate liaison departments, in which case the central liaison office must update a list of these departments and supply it to other central liaison offices from other Member States.

At the request of a requesting authority, the requested authority communicates information, including any information concerning one or more specific cases, which could help to effect a correct assessment of VAT, to monitor the application of VAT, particularly on intra-Community transactions, and to combat VAT fraud.

This information will be transmitted, without any prior request, by the competent authority of each Member State to the competent authority of every other Member State concerned, in the following cases: when it is considered that the taxes will be collected in the Member State of destination, and the information given by the Member State of origin is necessary to the efficiency of the control system of the Member State of destination; when a Member State has reasons to believe that a breach of the VAT law has been committed or is possible in the other Member State; when there is a risk of fiscal losses in the other Member State.

Every Member State may abstain from taking part in the automatic exchange of information, with respect to one or more categories of information, in case the collection of the respective information would impose new obligations on the persons liable for VAT or would force a disproportionate administrative burden upon the Member State.

From 1 January 2015, the competent authority in every Member State will proceed to automatically exchange information, which will allow the Member States to ascertain whether taxable persons not residing in their territory declare and correctly pay VAT owed for telecommunication, television and radio services as well as electronically supplied services, regardless of whether these persons use the special scheme stipulated by Directive 2006/112/EC in Title XII, chapter 6, section 3, or not. The Member State of residence informs the Member State of consumption of any discrepancies discovered.

¹⁰ Official Journal of the European Union L268/1 from 12.10.2010.

The regulation also regulates the storage and automatic exchange of specific information, simultaneous controls¹¹ and providing of information to taxable persons.

In order to promote and facilitate cooperation in the fight against VAT fraud, the regulation establishes a network of quick exchanges of specific information between Member States, called Eurofisc. Within the framework of this network, the competent authorities of every Member State designates at least one Eurofisc liaison official to establish a multilateral early warning mechanism for counteracting VAT fraud, to coordinate the rapid and multilateral exchange of information within the Eurofisc working fields¹².

The battle against tax fraud is a challenge for the European Union that goes beyond its borders and consequently it must be reflected in the international agreements concluded by the European Union with third party states or in multilateral covenants of which it is a signatory.

In order to efficiently combat fraud, the European Union negotiates agreements or multilateral covenants, on behalf of itself and the Member States.

In the context of the reinforced arrangement of the EU and the G-20 to establish a high level of cooperation internationally with the financial centres and tax havens in third party countries, which meet the OECD standards on fiscal cooperation, and following the Ecofin Council meeting of February 2009, the Commission amended its proposal, adopted on 10 December 2008, for a Council Decision on the signing and concluding of a cooperation agreement between the European Community and the Member States, on one side, and the Principality of Liechtenstein, on the other side, to combat fraud and any other illegal activity to the detriment of their financial interests¹³. The amended proposals were adopted in November 2009 and include the recent standards providing for the exchange of information in the field of taxation and the changes imposed by the coming into effect of the Lisbon Treaty.

This agreement would bring considerable value to the extent to which its scope covers not only tax evasion, tax fraud and any other unlawful activities affecting the financial interests of the parties involved, but also the exchange of information on fiscal matters, in accordance with the OECD standard, in this way preventing banking secrecy from being invoked as an exception that would hinder the exchange of information.

The agreement is particularly important because it should be used as a model for anti-fraud agreements made with third party countries, in accordance with the recommendations adopted by the European Commission in June 2009.

„The existence of tax havens and the effects of economic activities of people residing in such places impose the adoption of a strong joint stance of all states. The stated purpose is to attract the financial resources to the state budget of the country, which receives the taxable revenue, in order to efficiently use it for the benefit of the respective country's nationals.”¹⁴

2. The harmonization of the Romanian legislation with the European legislation

The accession of Romania to the European Union has led to a series of important measures in the fight against tax evasion and fiscal fraud, with efforts aimed firstly at diminishing underground commerce and promoting legislative measures to accelerate the development of the market economy.

The following measures have been taken in view of the Romanian accession to the European Union: the acceleration of reforms in public administration; the reform of the social security system

¹¹ Member States may agree to perform simultaneous controls every time they consider such controls to be more efficient than controls performed by a single Member State.

¹² Article 33 from Regulation 904/2010 on the administrative cooperation and combatting VAT fraud.

¹³ http://ec.europa.eu/anti_fraud/reports/commission/2009/RO.pdf Commission Report to the Council and the European Parliament - The Protection of the Financial Interests of the European Union – Combatting Fraud – Annual Report 2009.

¹⁴ Dan Drosu Şaguna, Mihaela Tofan, *Drept financiar și fiscal european*, (Bucureşti: Ed. C.H.Beck, 2010), 289.

with an emphasis on social insurance – especially financial reliability and the relation between paid contributions and received benefits; the general reform of indirect taxation, especially VAT, in agreement with the conditions for integration into the European Union; the increase of regulation simplicity, transparency and stability concerning taxes and tariffs; the elimination of wasteful policies that generate problems in the activities of the official sector of the economy; the acceleration of institutional reforms, in accordance with the conditions of integration into the European Union.

Romanian legislation on fiscal fraud and tax evasion has been adapted to the requirements of Community directives, and the main provisions are contained in the Position Document of Romania, Chapter 10 – Taxation, Chapter 12 – Statistics, Chapter 24 – Justice and Domestic Affairs, Chapter 28 – Financial Monitoring, Chapter 29 – Financial and Budgetary Provisions. However, national legislation is not effective enough to eliminate tax evasion¹⁵.

Conclusions

Combating fiscal fraud, especially intra-Community fraud, has not made great progress these last years. Total fiscal losses caused by fraud amount to a sum between 200 and 250 billion EUR, the equivalent of 2% of the EU gross domestic product.

An efficient fight against VAT fraud in the domestic market requires a common approach both in the legislative field but also on certain aspects of the operational management of the VAT system, operational differences between Member States can provide fraudsters the opportunity to undermine the efficiency of subjacent community legislative measures. So, it must be realised: common minimum standards for the registration and deregistration of taxable persons, confirmation of information, invoicing rules, chargeability on intra-Community transactions.

According to the EC, the tax evasion concerning VAT is about 100 billion EUR every year, at the communitarian level¹⁶. That's why the European Union wishes to reduce the tax evasion effects at the communitarian level. In this respect, it was submitted to a public debate a consultative document concerning the amendments to the VAT legislation with the purpose of using a single rate, reducing the number of exceptions to the payment and extending the tax base.

Reducing tax evasion and increase revenue collection will be the result of simplifying the system and reducing administrative burdens.

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¹⁵ *Ibidem*.

¹⁶ http://www.efin.ro/articole_financiare/international/ce_vrea_sa_simplifice_legislatia_referitoare_la_tva.html.