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**REPORT FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN
PARLIAMENT**

**On the application of Council Regulation (EC) no 1798/2003 concerning administrative
cooperation in the field of value added tax**

{SEC(2009) 1121}

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1. INTRODUCTION

According to Article 45 of Council Regulation No. 1798/2003 on administrative cooperation in the field of VAT, the Commission shall present every three years a report to the European Parliament and the Council on the application of this Regulation. In the past, there have been five reports which describe the functioning of the administrative cooperation in the field of value added tax, but this is the first report since the adoption of the Council Regulation No 1798/2003 on 1 January 2004.

This Regulation was designed to be a considerable improvement of the legal framework for administrative cooperation and an important tool in the fight against VAT fraud. In particular, the Regulation introduced improvements relating to;

- Clearer and binding rules governing cooperation between Member States.
- More direct contacts between services with a view to making cooperation more efficient and faster.
- More automatic or spontaneous exchanges of information between Member States in order to combat fraud more effectively.

This report assesses the functioning of administrative cooperation within the current legal framework and focuses in particular on the use that is made of these newly introduced arrangements in order to evaluate whether these changes have been effective.

However, the present report cannot be dissociated from the broader context of the coordinated strategy to improve the fight against VAT fraud set out in the recent Commission's Communication¹.

This Communication announces a range of measures which will substantially affect the way administrative cooperation in the field of VAT between tax authorities will function in the future.

2. SOURCES OF INFORMATION USED FOR THE EVALUATION OF THE APPLICATION OF REGULATION 1798/2003.

The Commission gathered much information from the **discussions** relating to administrative cooperation and the fight against fiscal fraud held during the numerous Anti Tax Fraud Strategy expert group meetings(ATFS) and the Standing Committee on Administrative Cooperation meetings (SCAC), but since the practical use of the different instruments of administrative cooperation is a matter for the

¹ Communication from the Commission, A coordinated strategy to improve the fight against VAT fraud in the EU, COM(2008)807 final, 1.12.2008

national tax authorities, consequently this evaluation could only be done on the basis of substantial input from the Member State.

Therefore, the Commission was of the opinion that the information required for a comprehensive assessment of administrative cooperation under the new Regulation was best collected by way of a **questionnaire** sent to the Member States. The Commission Staff working document SEC(2009)1121 du 18/08/2009 provides a detailed analysis of the replies given by the Member States².

Member states were given the opportunity to elaborate on certain replies given in the questionnaire and, more generally, to share their views on the functioning of VAT administrative cooperation and in particular on the possibilities they saw for its further improvement. Only 2 Member States showed an interest in having an open discussion with the Commission on this issue.

Interesting sources of information are the **annual statistics** sent by the Member States in respect of Article 35(3) of Regulation (EC) n° 1798/2003. Information relating to the statistics for 2006 and 2007 was taken into account to underpin a number of conclusions.

Furthermore, the European Court of Auditors analyzed the functioning of administrative cooperation in 2006, based notably on visits to 7 Member States. Their **Special Report** pointed out that "*despite new arrangements introduced in 2004, administrative cooperation between Member States in the field of VAT is still not intensive enough to cope with intra-Community VAT evasion and fraud*"³. This report has been a valuable source of input for the Commission.

The German authorities dispute the competence of the Court of Auditors to carry out audits in this field and notably to verify whether Germany has set up the necessary administrative and organizational structures for administrative cooperation. This issue is subject of an infringement case for which the application to the Court of Justice is under examination.

3. MAIN FINDINGS

3.1. Practical functioning

3.1.1. Exchange of information upon request

One of the key factors to a smooth system for the exchange of information is a robust and efficient internal management and procedural system in the Member States. Where this is lacking this report has identified that problems will arise such as late replies to the request for information, wrong use of standard forms, poor quality of the request and the reply, difficulties to identify the competent liaison department, and difficulties in collecting relevant data and technical problems with CCN mail⁴.

In particular in a decentralised system, requesting Member States have difficulties in identifying the liaison department (and the contact persons) to whom the request should be addressed. On the other hand, those Member States that implement a decentralised system point out that this leads to better use of resources.

² 25 Member States replied to the questionnaire, sent with letter D29096 of 31.3.2008

³ ECA's Special Report 08/2007, OJ C20, 25.1.2008,p1

⁴ mail sent via Common Communication Network (secured mailbox in all Member States)

A major concern is the timeliness of the reply and statistics have shown that the number of late replies has reached an unacceptable level. Moreover, although the Regulation foresees that Member States should inform each other in case of non respect of the deadlines, the statistics show that this is hardly ever done in practice. The delays in responding to requests for information and for informing the requesting Member State about the failure to meet the deadlines, is due to a number of internal factors: the exchange of information not being considered a priority, lack of human resources and linguistic problems. The standard forms contribute to more structure and clarity and to a more harmonised and coherent approach in administrative cooperation. In general, it seems that although most Member States would advocate mandatory use of the standard forms, there are concerns that this would reduce the efficiency of cooperation in certain cases. Member States complain also that the XML-format has still not been applied by all in 2008 although they had agreed unanimously in 2007 to use it.

The Commission is convinced that automated access to databases of other Member States would substantially reduce the number of requests for "standard" information. Automated access would therefore facilitate and speed up administrative cooperation, and it would also release time and resources for the in-depth enquiries required for more complex requests.

Furthermore, the quality of the reply does not always meet the appropriate standard. Therefore, replies can be in time but without value for the requesting party. Member States themselves have pointed out that the quality of the information exchanged needs to improve and the Commission has therefore looked into the matter in a specific project group set up under the Fiscalis 2013 programme⁵.

A lot of problems need to be addressed at management level in the Member States such as the priority to be given within the tax administration to provide assistance to other Member States. Among ways to improve the current situation, management should raise the awareness of local officials to prioritise these requests in their planning, the local offices should be encouraged to take direct contact with the contact points in the other Member States when there is a need to clarify requests, enough staff should be allocated to the administrative cooperation, and the XML-format should be implemented.

3.1.2. *Exchange of information without prior request*

Article 3 of Regulation 1925/2004 defines the categories for which the Member States can indicate whether they will automatically exchange information without prior request. Only few Member States participate in all categories for the exchange of information. Furthermore, some Member States indicate that they participate in the exchange for certain categories but in practice statistics show otherwise (for example for distance selling only 5 exchanges of information were carried out in 2007). Member States consider some categories more relevant than others. However, some Member States do not participate because they do not have a systematic collection and centralized storage of the necessary data. The reasons for not having

⁵ The Fiscalis 2013 programme (Decision n°1482/2007/EC of 11 December 2007) is a Community programme set up to improve the proper functioning of taxation systems in the internal market by increasing co-operation between the tax administrations of the participating countries. A project group is a group of national experts having meetings in order to propose solutions for a specific problem in well-defined areas, set up and financed under the Fiscalis 2013 programme.

this are numerous (lack of staff resources, disproportionate effort, internal administrative organisation and difficulty to get the information). It is regrettable that some Member States are still not in a position to exchange certain categories of information, despite this being the intention when the Regulation was adopted⁶.

Therefore, a review of article 3 of the Regulation 1925/2004 could be envisaged with a view to updating the current list and/or introducing a new list including types of transactions with a cross-border element where participation in the exchange of information would be obligatory for all Member States.

During discussions in the ATFS meetings a large number of Member States were not opposed to establishing such a specific list. Other categories considered irrelevant to the Member States should be deleted. However, as indicated above, it appears that there is a contradiction between the policy views expressed in the ATFS and the application of the automatic exchange of information in practice.

As concerns the spontaneous exchange of information, Member States should increase the awareness of their auditors to the importance of spontaneously exchanged information for other Member States' tax collecting purposes. Some Member States consider that Eurocanet⁷ is a good approach for the spontaneous exchange of information, because it creates direct contacts between officials specialized in a certain topic and it allows for information to be exchanged rapidly. In this way it can draw the attention of local staff to the importance of certain information that can be exchanged spontaneously and motivate them to actively use this tool. In this respect, the Commission considers that the establishment of EUROFISC, based on the guidelines approved by the Council in October 2008, would provide a solid framework for enhancing this rapid information exchange.

The Commission is of the opinion that Member States should implement efficient procedures to collect the data to be exchanged automatically, because the majority of the Member States consider the received information useful and of benefit in practice. Furthermore, management should improve the training of its tax auditors so that they become aware of the importance spontaneous information exchange potentially can have for tax purposes in other Member States.

3.1.3. *Feedback mechanism*

Most Member States have no feedback system and therefore cannot comment on whether the information transmitted has been used effectively. Such a mechanism and the improvement of the quality of information exchanged would be helpful for management to tackle shortcomings in the procedures and to motivate tax auditors to increase the use of this instrument.

Member States indicated the lack of feedback as a weakness and the Commission has examined the possible design of an appropriate feedback system in a Project Group under the Fiscalis 2013 programme.

⁶ See the Commission's reply to chapter 51, ECA's Special Report 08/2007, OJ C20, 25.1.2008,

⁷ Eurocanet is an informal network for rapid exchange of information relating potential missing trader fraud

3.1.4. *Improvements of the functionality in VAT Information Exchange System (VIES)*

The non-validity of VAT numbers and delays in correcting the data are often quoted as problems identified in relation to the quality of the information contained in the database, thus jeopardising the reliability of the database itself.

Technical work is progressing to modernise the VIES, such as crosschecking the name and address of the tax payer with his VAT ID-number to confirm these data. Furthermore, the Commission will present a proposal concerning minimum standards for registration/deregistration of VAT ID-numbers, in order to enhance the accuracy and completeness of the data in VIES.

3.1.5. *Presence of officials in administrative offices and participation in administrative enquiries in another Member State*

The statistics submitted annually show that use of the instrument mentioned in article 11 is limited, although it is considered a useful tool in border regions. The most important and recurrent reasons for this limited use are: language problems, lack of a national legal basis to allow participation in national enquiries, and specific national conditions to apply this instrument. However, national conditions should not hamper the use of this instrument.

There is a need for raising the awareness of the officials and encouraging them to use this instrument. Furthermore, developing the language skills should be dealt with at national level.

3.1.6. *Simultaneous controls – multilateral controls (MLC)*

The Member States recognize the added value of the instrument mentioned in article 12 of Regulation 1798/2003. Moreover, efforts have been made for promoting and facilitating the use of this instrument, notably by the setting up of the MLC-platform and the update of the MLC-guide. These efforts seem to achieve their objective since the number of MLCs initiated is increasing. However, there is still room for improvement. A number of bottlenecks slow down the procedure: lack of time and resources, language knowledge, lack of experience, no direct contacts at lower level, and no delegation by the competent authority to the responsible tax auditor. However, the functionality for communication between local tax authorities already exists within CCNmail phase II bis, but appears not to be implemented in all Member States. The exchange of information should, to the largest extent possible, always be directly between the tax auditors involved.

The Member States consider that their internal procedures are flexible enough to allow for swift reaction in cases of (carousel-) fraud. Nevertheless, at EU level it appears that the communication between the Anti Fraud Unit platform and the MLC coordination could still be improved.

3.1.7. *Special scheme for non established taxable persons supplying electronic services to non taxable persons (chapter VI of Regulation 1798/2003)*

No major problems have been encountered in the management of the special scheme, since the number of non established taxable persons (NETP's) and the amounts of tax paid are not significantly high. Nevertheless, this is tax that otherwise would not be collected in the absence of the special scheme. Furthermore, as a consequence of the introduction of the special scheme, a number of suppliers established themselves in the EU for their B2C transactions and pay VAT in the Member State of identification.

As concerns audits in the field of e-commerce, Member States consider it difficult to carry out audits on NETP's. Nevertheless, it is essential to carry out such audits as this is the only tool that allows Member States to verify that businesses correctly apply the provisions of the special scheme. Member States that carried out successful audits are encouraged to share audit experiences and practices in the framework of NETP's (for example addressing perceived risks, identifying compliance and revenue errors, providing confidence that remote and outside EU established businesses can be audited). Sharing these experiences and practices could be done through the MLC platform or anti-fraud platform.

3.1.8. *National evaluation arrangements*

Article 35 of the Regulation states that the Member States shall examine and evaluate how the arrangements for administrative cooperation are working. In practice, it appears that the vast majority of the Member States do not systematically perform an internal evaluation but rather seem to base their self-assessment solely on the annual statistics they have to provide to the Commission in this respect.

3.1.9. *Central Liaison Office (CLO)*

The CLO is in the vast majority of Member States the contact point for information requests. All Member States declare to have a monitoring system in order to follow up the treatment of requests. The CLO sets internal deadlines for responding, but it seems that they are not met, because there are no incentives to urge the responsible field office to reply in time or to explain why it cannot do so. In particular in a decentralised system with liaison departments, it is necessary that an efficient monitoring system is set up, not only to meet the deadlines, but also to ensure the standards of quality of information exchanged. Furthermore, it appears that some Member States send a single request to all liaison departments, which are then counted as more than one. This is one of the reasons for the differences between the received and sent requests in the statistics.

Differences in languages used slows down the procedure. It could be best practice if Member States agree the working language in which they want to communicate for CLO-purposes. However, in the view of the Commission, the absence of an agreement should not continue to hinder smooth cooperation but instead it could be envisaged that English be used as a fall back position in case no agreement can be reached. The lack of language knowledge is a problem occurring mainly at the local level of the administration. Direct contacts (telephone or CCN-mail) asking for clarification could avoid burdensome translation. For the MLCs, the support of interpreters could be helpful. A linguistic support tool was indeed set up under the Fiscalis 2007 and Fiscalis 2013 programmes.

3.2. **Legal framework**

The Member States consider that the Regulation has improved administrative cooperation. In general, the legal framework provides tax authorities with a solid basis for exchanging information and for working together using the different instruments available to obtain valuable information to combat fraud.

However, Member States came across a number of rules lacking clarity and inaccuracies in applying the rules. Therefore, the legal framework would need to be updated in the areas listed below.

3.2.1. *Presence in administrative offices, participation to administrative enquiries and simultaneous controls (Articles 11-12-13)*

Member States pointed out that an interpretation at European level about the application of article 11 would be useful and that no further international agreements or domestic legislation would then be required (which limit the use of the tool).

Some difficulties were indeed pointed out resulting from differences in interpretation of the relevant article.

However, after careful consideration the Commission services are of the opinion the abovementioned articles require very little amendment as the key is rather to apply the provisions at hand with an open mind.

3.2.2. *Exchange of information without prior request (Articles 17 to 21)*

Article 17 of the Regulation provides for Member States to exchange information without prior request. It specifies that each Member State should forward information to any other Member State concerned in three situations, which represent a very broad obligation.

Articles 3 and 4 of Commission Regulation 1925/2004 define the (sub) categories for which the Member States will exchange information in an automatic or structured automatic way.

Article 18, however, limits the obligation provided for in Article 17, stating that the Member States may determine whether they will exchange certain categories of information without prior request.

The replies to the questionnaire made clear that the Member States understand and apply the interaction between articles 17 and 18 in divergent ways. This leads to inconsistency in the exchange of information between the Member States. The definition of the categories has not achieved its full objective. Furthermore, the definition of "automatic" and "structured automatic" exchange causes confusion.

The Commission will therefore propose amending the interaction between article 17 and 18 of the Regulation. Furthermore, as indicated above, in Commission Regulation 1925/2004 the current list could be updated or a new list with types of transactions could be introduced for which exchange of information would be compulsory for all Member States (at least for some categories).

3.2.3. *Relations with third countries (article 36)*

There is little experience regarding the exchange of information coming from third countries. Member States considered that information coming from third countries could be very useful to facilitate tax assessment or fraud detection, but strict rules need to be applied (principle of secrecy). Not all Member States have concluded tax treaties including VAT matters and thus it is not possible for all of them to pass on the information from third countries.

The majority of the Member States are not opposed to make the passing of information coming from third countries to other interested Member States obligatory. A possibility could be to broaden the scope of the provision in the Regulation, so that the passing on of information is not explicitly excluded.

The Commission is still convinced that in the longer term an approach coordinated at EU level to cooperation with third countries in the area of VAT is the appropriate way forward.

4. CONCLUSION

The Commission's Communication of 31 May 2006 concerning the need to develop a co-ordinated strategy to improve the fight against fiscal fraud (COM (2006)254final of 31.5.2006) already expressed the view that the legal framework for administrative cooperation in the field of VAT has been reinforced, but that Member States do not make sufficient use of it and the level of administrative cooperation is not commensurate with the size of intra-Community trade. The European Court of Auditors came largely to the same conclusion in the Special Report presented in 2007.

This report does not come to a different conclusion; the new arrangements introduced in 2004 with Regulation 1798/2003 offered improved possibilities, but the intensity of the administrative cooperation between Member States to cope with intra-Community VAT evasion and fraud is still unsatisfactory.

As concerns the practical functioning, the willingness to improve the application of the administrative cooperation arrangements should be reflected in the management support and organisation of the tax administration through the following actions:

- An appropriate number of resources should be allocated to administrative cooperation and tax controls;
- Training should be provided for tax officials to raise their awareness as regards the instruments available (requests, presence in administrative offices, participation in administrative enquiries, simultaneous controls) and the spontaneous exchange of information;
- A proactive and open-minded approach should be adopted towards the application of the instruments available and obstacles should be avoided at national level which could hamper the functioning of the administrative cooperation and undermine the efficient use of the instruments;
- Local officials should be given instructions on how to prioritise the requests for information;
- The software should be adjusted in order to use the XML-format for sending requests;
- Efficient procedures should be implemented to collect data to be exchanged;
- Direct contacts between local tax auditors should be encouraged (via CCN mail II bis).

These recommendations are in fact not new; they can already be found in previous reports presented several years ago. The fact that they need to be repeated is a worrying signal as concerns the level of follow up that has been given to them in the past.

The political importance given within a Member State to ensuring that a service of good quality is provided to the partner authorities in the other Member States is a key factor for substantial improvements.

The ECOFIN Council has had in the past 2 years several discussions about combating VAT fraud. The conclusions which have been drawn on these occasions point out the need for a common approach at EU level. The emphasis has been put on the so-called "conventional measures" which aim at strengthening the capacity of tax authorities to tackle VAT fraud within the context of the current VAT system.

Reinforcing administrative cooperation is essential in this context and the proposal for a recast of the Regulation 1798/2003 that is presented today contains substantial changes like automated access to databases and will provide the legal base to set up EUROFISC. The present report demonstrates the need for further amendments to the legal framework which are taken on board in this proposal.

However, improving the practical functioning is equally important and the Commission counts on the political willingness of the Member States to put the necessary efforts in this objective.

The willingness has to come from the Member States but the Commission is prepared to provide its assistance to these efforts. A number of actions to be taken could be coordinated at EU level and the Fiscalis 2013 programme provides appropriate tools for supporting the development and implementation of these actions.