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Proposal for a

COUNCIL IMPLEMENTING DECISION

**authorising Poland to introduce a special measure derogating from Article 226 of
Directive 2006/112/EC on the common system of value added tax**

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EXPLANATORY MEMORANDUM

Pursuant to Article 395(1) of Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (hereafter '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 15 May 2018 Poland requested an authorisation to derogate from Article 226 of the VAT Directive with regard to value added tax (VAT) invoicing requirements and to introduce the mandatory split payment mechanism for supplies of goods and services susceptible to fraud covered generally by the reverse charge mechanism and joint and several liability in Poland. In accordance with Article 395(2) of the VAT Directive, the Commission informed the other Member States by letter dated 3 September 2018 of the request made by Poland. By letter dated 4 September 2018, the Commission notified Poland that it had all the information necessary to consider the request.

1. CONTEXT OF THE PROPOSAL

• Reasons for and objectives of the proposal

In order to tackle VAT fraud, Poland intends to introduce the mandatory split payment mechanism for the payment of VAT for certain supplies of goods and services susceptible to fraud.

The split payment mechanism is an alternative VAT collection system. Under a standard procedure, for a given transaction, a VAT taxable person collects the payment of the taxable amount and the VAT (if applicable) from its client (or a third party). The VAT taxable person then reports this transaction in its periodical VAT return. Depending on the outcome of the VAT return, VAT is due by the taxable person to the tax authorities or it could be refunded by the tax authorities. If VAT is due, the VAT taxable person pays the VAT to the Member State on a defined periodical basis (monthly, quarterly, etc.). The use of the split payment introduces a change to this (regular) transaction chain since a split has to be made between the payment of the VAT amount due and the taxable amount due. When a supplier is covered by these split payment provisions, he will be obliged to have, in addition to his regular bank account, a separate blocked VAT account. The latter can only be used to receive VAT from its customers and to pay VAT to its suppliers. In that case the purchaser will pay the taxable amount to the supplier, normally to an ordinary bank account, whereas the VAT due on the supply will have to be paid to his blocked VAT bank account.

Poland submits that notwithstanding numerous measures taken to fight fraud (e.g. the introduction of the reverse charge mechanism and of the joint and several liability for the customer, the introduction of the Standard Audit File, tighter rules for VAT registration and de-registration of taxable persons, increased number of audits, etc.), these solutions still remain insufficient to exclude VAT fraud and increase VAT revenues. The recent study on the VAT Gap in the EU-28 Member States¹ indicates the VAT gap of 25% for Poland. Poland is of the view that the application of the mandatory split payment mechanism will eliminate VAT fraud at the very beginning. Since the effect of the split payment model is that the amount of VAT deposited on a separate VAT account of a taxable person can only be used by that taxable person for restricted purposes, namely for the payment of the VAT liability to the tax authority or the payment of VAT on invoices received from suppliers, it is better

¹ Study and Reports on the VAT Gap in the EU-28 Member States: 2018 Final Report.

guaranteed that the tax authorities will receive the whole VAT amount which should be transferred by the taxable person to the State Treasury.

Poland, therefore, introduced the voluntary split payment mechanism on 1 July 2018. However, Poland considers that in areas particularly exposed to VAT fraud and in which fraud has been detected for years, it is worth going a step further and introducing the mandatory split payment mechanism. These areas cover economic sectors such as steel, scrap, electronical equipment, gold, non-ferrous metals, fuels and plastics which are generally subject to the reverse charge mechanism and to joint and several liability in Poland (the list of sectors to be covered by the split payment mechanism is included in Annex to the Decision).

The mandatory split payment model will apply to the given supplies between taxable persons (B2B supplies) and will cover only electronic bank transfers. The bank will act as a splitting agent and perform the activities with the aim of transferring the amount paid by the customer to the relevant accounts of the supplier, i.e. the tax amount to the regular account of the trader while the VAT amount to the trader's blocked VAT account. Funds on the blocked VAT account will be owned by the taxable person, however, his possibility to dispose of the funds will be limited in principle to the payment of VAT due to the tax authority or VAT resulting from invoices received from suppliers.

Under the general rules applicable in Poland, in case of the surplus of input tax over the output tax recognised by the taxable person in the VAT return as a VAT refundable amount, such refund will be carried out within 60 days to taxable person's regular account. To diminish the effects of the split payment model on traders' cash flow, a faster procedure is foreseen by Poland for the refund of the input tax surplus. At the request of the taxable person the refund will take place within 25 days. Furthermore, Poland underlined in the request that ensuring effective and timely performed tax refund procedures will be the priority issue.

According to Poland, the costs of operating the split payment system should not be significant and will mostly be connected to the implementation of the system, its servicing and to managing the bank account. Taxable persons will not incur costs of opening and operating the VAT account, as the VAT account will be provided by the bank without any commission or fee charged.

The obligatory split payment mechanism will be also applicable to traders not established in Poland which will have to hold a bank account operated pursuant to Polish Banking Law. In this respect Poland confirmed to the Commission, that the non-established traders will not incur any additional costs relating to the obligation of opening the bank account in Poland, since these taxable persons will be able to open and hold the bank account in Poland free of charge.

For the smooth functioning of the split payment mechanism, information concerning the use of the mandatory split payment mechanism will have to be displayed on the invoice issued by the supplier. Article 226 includes a list of details which are to be included on the invoices. Member States do not have discretion to include additional invoicing details. In view of the fact that the application of the split payment mechanism requires an additional mention on the invoice, Poland requested a derogation from Article 226 of the VAT Directive.

The mandatory split payment mechanism as envisaged by Poland will impose significant changes for taxable persons. However, as the system is already operational, on a voluntary basis since 1 July 2018, taxable persons had the opportunity to get acquainted with it.

Taking into account the above, the Commission is of the view that the mandatory split payment mechanism for supplies of goods and services susceptible to fraud and listed in the Annex can bring effective results in the fight against tax fraud. It is, therefore, proposed to grant the derogation as from 1 March 2019 until 28 February 2022.

Nonetheless, given the novelty and the broad scope of the derogation, it is important to ensure the necessary follow-up within the framework of this derogation and in particular the impact of the measure on the level of VAT fraud and its impact for the taxable persons (regarding the refunds of VAT, the administrative burden, costs for taxable persons etc.). Consequently, Poland is requested to provide a report on the impact of the measure eighteen months after its entry into force.

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

The derogation can be authorised based on Article 395 of the VAT Directive in order to simplify the procedure for collecting VAT or to prevent certain forms of tax evasion or avoidance. Poland requested the derogating measure to fight tax evasion in the sectors in which VAT fraud has been detected for years. The derogation is consistent with the existing policy provisions.

By Council Implementing Decision (EU) 2017/784² Italy was granted a similar derogation to apply the split payment mechanism. Under the Italian split payment system, the VAT due is paid to the blocked VAT account at the tax authorities. The scope of the Italian derogation is limited to supplies to public authorities, entities controlled by public authorities and a number of companies listed on the stock exchange.

Also Romania applied for derogation to apply the split payment mechanism to supplies by certain taxable persons. The Romanian split payment mechanism raises serious concerns regarding its proportionality and its compatibility with the Treaty. Consequently, the Commission objected to the Romanian request by derogation³.

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 the proposal is based, the subsidiarity principle does not apply.

- **Proportionality**

The proposal complies with the proportionality principle for the following reasons.

The Decision concerns an authorisation granted to a Member State upon its own request and does not constitute any obligation.

² Council Implementing Decision (EU) 2017/784 of 25 April 2017 authorising the Italian Republic to apply a special measure derogating from Articles 206 and 226 of Directive 2006/112/EC on the common system of value added tax and repealing Implementing Decision (EU) 2015/1401, OJ L 118, 6.5.2017, p. 17.

³ Communication from the Commission to the Council in accordance with Article 395 of Council Directive 2006/112/EC, COM/2018/666 final

As the derogation is limited in time and restricted to specific supplies, the scope is targeted to sectors which pose considerable problems of tax fraud. Therefore, the special measure is proportionate to the aim pursued, i.e. to combat tax fraud.

Given the novelty and the broad scope of the derogation, Poland is requested to provide a report on the impact of the measure on the level of VAT fraud and on the taxable persons (regarding the refunds of VAT, the administrative burden, costs for taxable persons etc.) eighteen months after its entry into force in Poland.

- **Choice of the instrument**

Proposed instrument: Council Implementing Decision.

Under Article 395 of the VAT Directive, derogation from the common VAT rules is only possible upon authorisation of the Council 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**

This proposal is based on a request made by Poland and concerns only this Member State.

- **Collection and use of expertise**

There was no need for external expertise.

- **Impact assessment**

The proposal for a Council Implementing Decision authorises Poland to derogate from Article 226 of the VAT Directive and to introduce the mandatory split payment mechanism for the payment of VAT on specific supplies of goods and services.

By imposing that the VAT due is paid to a blocked VAT bank account of the supplier, the proposal for a Council Implementing Decision aims at combating tax fraud in the form of non-payment of VAT liability by suppliers of goods and services which are susceptible to fraud. Since the amount of VAT deposited on a separate VAT account of a taxable person can only be used for restricted purposes, namely for the payment of the VAT liability to the tax authority or the payment of VAT on invoices received from suppliers, it is better guaranteed that the tax authorities will receive the whole VAT amount which should be transferred by the taxable person in favour of the State Treasury.

The funds on the blocked VAT account cannot be disposed of by the taxable person unless it is for the payment of VAT due to the tax authority or VAT resulting from invoices received from suppliers impacting thus traders' cash flow. To diminish the negative impact, in case of the surplus of input tax over the output tax recognised by the tax authorities, a faster procedure is foreseen by Poland for the refund of the input tax surplus. At the request of the taxable person the refund will take place within 25 days, instead of 60 days under the normal procedure. Furthermore, Poland underlined in the request that ensuring effective and timely performed tax refunds will be the priority issue.

Traders that are not established in Poland will also be covered by the mandatory split payment mechanism when carrying out the supplies of goods or services subject to the mandatory split payment in Poland. These traders will have to hold a bank account operated pursuant to Polish

Banking Law. In this respect Poland confirmed to the Commission, that the non-established traders will not incur any additional costs relating to the obligation of opening the bank account in Poland, since these taxable persons will be able to open and hold the bank account in Poland free of charge.

4. BUDGETARY IMPLICATIONS

The measure will have no negative impact on the Union's own resources accruing from VAT.

5. OTHER ELEMENTS

The proposal includes a sunset clause; an automatic time limit.

Proposal for a

COUNCIL IMPLEMENTING DECISION

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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 tax⁴, and in particular Article 395(1) thereof,

Having regard to the proposal from the European Commission,

Whereas:

- (1) By letter registered with the Commission on 15 May 2018 Poland requested an authorisation to derogate from Article 226 of Directive 2006/112/EC and to require the inclusion of a special statement that value added tax (VAT) has to be paid to the blocked VAT account of the supplier on invoices issued in relation to the supplies of goods and services susceptible to fraud and generally covered by the reverse charge mechanism and the joint and several liability in Poland. Poland requested the derogation for period of three years, from 1 January 2019 to 31 December 2021.
- (2) In accordance with the second subparagraph of Article 395(2) of Directive 2006/112/EC, the Commission transmitted the request of Poland to other Member States by letters dated 3 September 2018. By letter dated 4 September 2018, the Commission notified Poland that it had all the information necessary to consider the request.
- (3) Although Poland has taken numerous measures to fight fraud (e.g. the introduction of the reverse charge mechanism and of the joint and several liability by the customer, the introduction of the Standard Audit File, tighter rules for VAT registration and de-registration of taxable persons, increased number of audits, etc.), it considers that those measures are still insufficient to exclude VAT fraud.
- (4) Poland is of the view that the application of the split payment mechanism will eliminate VAT fraud. Since under the split payment model the amount of VAT deposited on a separate VAT account of a taxable person can be used for restricted purposes only, namely for the payment of the VAT liability to the tax authority or for the payment of VAT on invoices received from suppliers, it is better guaranteed that the tax authorities will receive the whole VAT amount which should be transferred by the taxable person to the Polish State Treasury.
- (5) Poland introduced the voluntary split payment mechanism on 1 July 2018. Poland considers that in areas particularly exposed to VAT fraud the mandatory split payment mechanism should be introduced. These areas are sectors of economy such as steel,

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OJ 347, 11.12.2006, p. 1.

scrap, electronics, golds, non-ferrous metals, fuels, plastics, generally covered by the reverse charge mechanism and joint and several liability in Poland.

- (6) The mandatory split payment model will apply to the supplies between taxable persons, business-to-business (B2B) supplies, of goods and services listed in the Annex and will cover only electronic bank transfers.
- (7) In case of the surplus of input tax over the output tax recognised by the taxable person in the VAT return as a refundable amount, such refund is normally carried out within 60 days to taxable person's regular account. However, Poland has informed that for the transactions covered by the mandatory split payment model, upon request of a taxable person disposing of a blocked VAT account the refund will take place within 25 days.
- (8) Taxable persons will not incur costs on opening and operating the VAT bank account, as the VAT account will be free from any commissions and fees by the bank.
- (9) The obligatory split payment mechanism will be applicable to all traders, including those traders who are not established in Poland and they will have to hold a bank account operated pursuant to Polish Banking Law. In this respect Poland confirmed, that the traders will not incur any additional costs relating to the obligation of opening a bank account in Poland, since those taxable persons will be able to open and hold the bank account for VAT payments in Poland free of charge.
- (10) The mandatory split payment mechanism as envisaged by Poland will impose significant changes on taxable persons. However, as the system already operates since 1 July 2018 on a voluntary basis, taxable persons have had the opportunity to get acquainted with it.
- (11) The Commission is of the view that the mandatory split payment mechanism for supplies of goods and services susceptible to fraud can bring effective results in the fight against tax fraud. The derogations are usually granted for a limited period of time. The derogation requested by Poland should therefore be authorised from 1 March 2019 until 28 February 2022.
- (12) Given the novelty and the broad scope of the derogation, it is important to ensure the necessary follow-up within the framework of this derogation and in particular the impact of the measure on the level of VAT fraud and on the taxable persons (regarding the refunds of VAT, the administrative burden, costs for taxable persons etc.). Poland should therefore provide a report on the impact of the measure eighteen months after the entry into force of the national measure in Poland.
- (13) The derogation will not negatively affect the overall amount of tax revenue collected at the stage of final consumption and will have no adverse impact on the Union's own resources accruing from VAT,

HAS ADOPTED THIS DECISION:

Article 1

By way of derogation from Article 226 of Directive 2006/112/EC, Poland is authorised to require the inclusion of a special requirement that VAT has to be paid to the separate and blocked VAT bank account of the supplier opened in Poland on invoices issued in relation to supplies between taxable persons of goods and services listed in the Annex of this Decision where payments for supplies are made by electronic bank transfers.

Article 2

Poland shall notify the national measure referred to in Article 1 to the Commission.

Within 18 months after the entry into force in Poland of the measure referred to in Article 1, Poland shall submit a report to the Commission on its overall impact on the level of VAT fraud and on the taxable persons concerned.

Article 3

This Decision shall apply from 1 March 2019 to 28 February 2022.

Article 4

This Decision is addressed to the Republic of Poland.

Done at Brussels,

*For the Council
The President*