BUSINESSEUROPE

POSITION PAPER

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AN AGENDA FOR THE EU IN 2010-2014

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BUSINESSEUROPE POSITION PAPER REGARDING THE VAT REVERSE CHARGE MECHANISM

Introduction

In general, it is the business supplier of a good and or a service who is liable for collecting and paying VAT to the tax authorities. In recent years, a type of fraud has consisted in business suppliers people "disappearing" without paying taxes to the authorities – the so-called missing trader-. This kind of fraud was traditionally organised with small goods of high value but, in 2009, several Member States detected this type of fraud also in other areas (e.g. emission trading permits).

As a response, the European Commission published a proposal[1] to introduce an optional and temporary application of a reverse charge mechanism, by which the supplier does not charge VAT, but instead it is paid by the final customer, who deducts this VAT at the same time (if eligible). Therefore, the need for an effective payment to the tax authority is removed, as well as the theoretical possibility to commit this type of fraud. The proposal was to introduce a temporary application of an optional reverse charge mechanism on the supply of five categories of goods: mobile phones, electronic circuit devices, precious metals, fragrances, and greenhouse gas emission allowances.

In December 2009, the ECOFIN Council agreed to implement, on an optional and temporary basis, a reverse charge mechanism, and also decided that Member States can make use of a derogation procedure[2] for other products.

BUSINESSEUROPE view

BUSINESSEUROPE fully endorses the fight against VAT fraud. VAT fraud has a negative impact on government revenues, is a threat to the internal market, and harms legitimate business.

However, we are of the opinion that the use of optional reverse charge mechanism or an extension of derogations is not the way forward to fight fraud within the European Union. Reverse charge fundamentally changes the way VAT is collected by passing the full liability for the VAT payment from the supplier(s) to the end customer. In seeking a solution to missing trader fraud, all the VAT from the supply chain is put at risk through the retailer. That could result in the growth of retail fraud, which the reverse charge cannot solve.

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[1] Proposal COM(2009) 511 final for a Council Directive amending Directive 2006/112 on the Common System of VAT, which was adopted on the European Parliament on February 10, 2010

[2] Article 395 of VAT

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Besides, an optional reverse charge mechanism leads also to a less harmonised system of national VAT legislation which is another burden for business. Furthermore, it is doubtful whether an optional reverse charge mechanism only for certain products will be successful. This creates weaknesses, since fraud and fraudster would move from one Member State where the reverse charge mechanism is applied, to another where it is not, and from one product which is subject to the reverse charge, to another which is not. This 'creeping' effect means that the scope of the mechanism is dictated by the fraudster and not the Member State. It is not the goods and or the service but the missing trader that causes the fraud.

Moreover, most of the existing accounting systems and procedures are not designed to apply the optional reverse charge to domestic supplies or to services – as it is a departure from the general rule-, and this would therefore involve significant implementation costs. Furthermore, if reverse charge is introduced with reporting on a transaction basis, legitimate business will be confronted with an additional increase in administrative burdens.

Experience from the UK on extending the reverse charge to selected products clearly reveals the insufficiency of this mechanism to contain fraud. Fraud operates outside the normal business systems, and so the solution should be targeted at the fraud and not affect legitimate business in the way the reverse charge mechanism does.

The reverse charge for mobile phones in the UK showed that the list of products subject to reverse charge was arbitrary (for example mobile phone handsets were included, but not accessories). In addition, the use of *de minimis limits* adds complications to billing systems, software logic, and increases the potential for error and consequently penalties.

BUSINESSEUROPE does recognise that in some Member States, for certain domestic situations, a mandatory reverse charge did solve specific fraud issues in a practical way; however, whether the VAT fraud is combated in the most efficient way through this mechanism depends on the sector, on the type of products/services, and on the consequences for reporting.

Conclusion

BUSINESSEUROPE opposes the application of an optional reverse charge mechanism, as it does not solve VAT fraud, creates barriers to the internal market, makes a less harmonised set of rules, and increases regulatory burden. The optional reverse charge is not a solution, since fraud moves from one Member State to another, and from one product to another.

While we endorse the fight against VAT fraud, we are of the opinion that it should be combated by proper risk analysis and timely exchange of information, so that the root cause of the fraud - the missing traders - can be found and stopped.