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

**Seventh report under Article 12 of Regulation (EEC, Euratom) n° 1553/89 on VAT  
collection and control procedures**

{SWD(2014) 38 final}

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## 1. INTRODUCTION

Article 12 of Council Regulation 1553/89<sup>1</sup> on the definitive uniform arrangements for the collection of own resources accruing from VAT requires the Commission to submit a report to Parliament and Council every three years on the procedures applied in the Member States for registering taxable persons and determining and collecting VAT, as well as on the modalities and results of their VAT control systems.

Six reports have been made since 1989<sup>2</sup>. Past reports have covered all the subject areas indicated by the above mentioned Regulation and have made recommendations on improvements concerning most of them. The last report<sup>3</sup> moreover evaluated whether the reporting process, and the recommendations derived therefrom, had been effective.

This report is the seventh in the series and is aimed at measuring the improvements in VAT administration in Member States within the framework of Article 12 of the above mentioned Regulation. At the same time, this report is also intended to identify good practices in the various stages of effective VAT collection and to enable Member States to assess risks and identify opportunities to improve VAT control and collection systems. In this respect, the Commission stresses that the report should be seen as an opportunity *"to consider whether improvements to these procedures can be contemplated with a view to improving their effectiveness"* (Article 12, Paragraph 2 of the abovementioned Regulation).

The findings in this report are measured against common benchmarks that were drawn up by the Commission on the basis of recommendations contained in previous reports<sup>4</sup> as well as developments at EU and national level in the field of tax administration. These developments concern, most importantly, preventive measures, measures promoting voluntary compliance, client-service approaches, risk management and optimisation of the use of IT tools.

In order to gather the information necessary for the preparation of this report, a questionnaire on selected issues was submitted to all Member States<sup>5</sup>. The questions concerned the following main subject areas: the organisation of tax administrations; VAT identification, registration and deregistration; Customs Procedure 42; VAT returns and payments; VAT collection and recovery; VAT audit and investigation; tax dispute resolution system; and VAT compliance. All Member States replied to the questionnaire and provided the requested information. The information submitted was discussed on several occasions with Member States. In this report the findings resulting from the answers to the questionnaire are summarised by subject area and in the sequential order described above.

## 2. THE IMPACT OF EFFICIENCY AND EFFECTIVENESS OF TAX ADMINISTRATION

The efficiency and effectiveness of tax administration in the Member States have an impact on the size of VAT-gap as well as on the amount of VAT own resources due by Member

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<sup>1</sup> Council Regulation (EEC, EURATOM) 1553/89 of 29 May 1989 on the definitive uniform arrangements for the collection of own resources accruing from value added tax.

<sup>2</sup> 6<sup>th</sup> Report: COM/2008/719 final + Annex SEC (2008) 2759  
5<sup>th</sup> Report: COM/2004/0855 final + Annex SEC (2004) 1721  
4<sup>th</sup> Report: COM/00/0028 final  
3<sup>rd</sup> Report: COM/98/0490 final  
2<sup>nd</sup> Report: COM/95/354 final  
1<sup>st</sup> Report: SEC(92) 280 final

<sup>3</sup> See 6<sup>th</sup> Report under footnote 2.

<sup>4</sup> See Annex to the 6<sup>th</sup> Report under footnote 2.

<sup>5</sup> Croatia is not included in this report as it was not yet an EU member when the data was being collected.

States to the EU. Consequently, these factors also have an impact on the relative share in total own resources paid by other Member States. At the same time, the efficiency and effectiveness of tax administration also influence compliance costs of businesses and the costs of tax administration to governments. Since VAT constitutes a large part of the administrative burden of businesses, it is important to improve the quality of VAT administration for this reason too.

## **2.1. The VAT gap and the VAT own resource**

The VAT gap is the difference between the amount of VAT theoretically collectable<sup>6</sup> and the amount of VAT actually collected, and it arises as a consequence of revenue loss through cases of fraud and evasion, legal tax avoidance, bankruptcies, financial insolvencies as well as miscalculations and the performance of tax administrations. In a recent study<sup>7</sup> the total VAT-gap<sup>8</sup> for 26 Member States in 2011<sup>9</sup> was estimated to be around Euro 193 billion, which is around 18 per cent of the VAT theoretically collectable in the EU-26, or about 1.5 per cent of the total GDP of EU-26. This latter percentage shows an increase from the 1.1 per cent of the total GDP of EU-26 recorded in 2006, and is also above the 2000-2011 average of 1.2 per cent. The average VAT gap as a percentage of GDP showed a moderate declining trend prior to 2008<sup>10</sup>, while since 2008 the difficult economic times have placed a strain on VAT systems and have led to an increase in the average VAT gap. In particular, countries that have been hardest hit by the economic and financial crisis have recorded significant increases in their VAT gaps and have been unable to improve their situation substantially over the time. In general, the estimated VAT gaps for individual Member States have a very wide dispersion across Member States and show great disparities in their performance.

The overall conclusion of the study is that VAT compliance appears to fall during recessions and also when tax rates are increased, in particular in countries with weaker tax enforcement. These results are consistent with predictions from the theory of tax avoidance and with some previous estimates, and indicate the importance of tax administration and enforcement in determining reforms to VAT policy and in responding to fiscal pressures.

The VAT own resource represented 11 per cent of EU revenue, being around Euro 14 billion in 2011. For the calculation of the VAT own resource, as a rule, a uniform call rate of 0.3% is levied on the harmonised VAT base of each Member State<sup>11</sup>. However, this VAT base is capped at 50% of GNI for each Member State.

## **2.2. Compliance costs for businesses**

In the current fragile economic and financial climate, compliance costs for businesses have become an important issue for governments to bear in mind when considering how best to

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<sup>6</sup> The VAT theoretical liability is estimated by identifying the categories of expenditure that give rise to irrecoverable VAT and combining these with the appropriate VAT rates. Since the VAT gap is estimated primarily on the basis of national accounts data, it depends on the accuracy and the completeness of such data. Moreover, it does not take account of taxable activities that are outside the scope of national accounts.

<sup>7</sup> Source: Study to quantify and analyse the VAT Gap in the EU-27 Member States commissioned by the EC and conducted by CASE and CPB. The study is published by the Commission on 19 September 2013 and is available at: [http://ec.europa.eu/taxation\\_customs/common/publications/studies/index\\_en.htm](http://ec.europa.eu/taxation_customs/common/publications/studies/index_en.htm).

<sup>8</sup> The total VAT gap is calculated for the EU-26 as being one unit.

<sup>9</sup> The study could not cover Cyprus due to an ongoing major revision of national account statistics.

<sup>10</sup> This trend was more evident in the data of New Member States (EU-10 and EU-2).

<sup>11</sup> The harmonised VAT base is calculated by the relevant Member State using what is known as the revenue method. It consists of dividing the total net VAT revenue collected by the Member State in question by the weighted average rate of VAT to obtain the intermediate VAT base. The intermediate base is subsequently adjusted with negative and positive compensations in order to obtain a harmonised VAT base pursuant the VAT Directive.

stimulate and sustain economic growth. In the 2013 study on Paying Taxes<sup>12</sup>, it was concluded that there is a link between economic growth and administrative burdens on businesses. The study shows that in economies where action was taken to reduce complexity in tax administration – both in terms of the number of payments and the time taken to deal with tax matters – there has been a positive change in economic growth. Furthermore, it appeared that reducing the administrative burden on businesses is more strongly linked with economic growth than cutting tax rates.

With regard to the EU&EFTA region<sup>13</sup>, the study shows that both the average hours taken to comply and the number of payments fell over the period of the study. This development has been largely due to the increased use of improved electronic filing and payment capabilities, and to greater efficiencies in tax administration. The VAT systems account on average for 32% of the time to comply with tax legislation in the region. There is, however, considerable variation between Member States because of the administrative procedures used to implement the tax vary considerably.

### **2.3. Costs of tax administration for Member States**

The aggregate level of expenditure of a tax administration to carry out its taxation and other mandated responsibilities is an important and topical issue for all Member States. Member States have limited resources available for the administration of national tax laws and are continuously seeking to reduce the costs of tax administration. According to a recent OECD survey<sup>14</sup>, the costs of collection ratio<sup>15</sup> shows a decreasing trend for the majority of tax administrations, which may be, at least partially, attributable to increased efficiency resulting from technology investments and other initiatives. The survey showed also that the aggregate salary costs - as a share of total administrative costs for OECD countries - declined sharply by 6% (absolute) in each of 2010 and 2011. This development most likely reflects the impacts of government-mandated reductions in staffing and/or efficiency gains from automation and internal reorganisations initiatives. Differences between Member States, however, remain.

## **3. CHALLENGES TO RAISE THE EFFICIENCY OF TAX ADMINISTRATION**

In a modern tax administration, regular evaluations of performance have an important role to play as they can be used to improve the efficiency and effectiveness of administration. The Article 12 arrangements provide an opportunity to evaluate the functioning of VAT administrations and to understand the patterns of both VAT compliance and non-compliance, which in turn can contribute to a reduction in the VAT-gap and to economic benefits. In this

<sup>12</sup> Paying Taxes indicators (the Total Tax Rate, the time to comply and the number of payments) are part of the World Bank Group Doing Business Project and are prepared by PWC, the World Bank and IFC.

<sup>13</sup> European Union & European Free Trade Association (EU & EFTA). The following economies are included in the analysis of EU & EFTA: Austria; Belgium; Bulgaria; Cyprus; Czech Republic; Denmark; Estonia; Finland; France; Germany; Greece; Hungary; Iceland; Ireland; Italy; Latvia; Lithuania; Luxembourg; Malta; Netherlands; Norway; Poland; Portugal; Romania; Slovak Republic; Slovenia; Spain; Sweden; Switzerland; United Kingdom.

<sup>14</sup> OECD (2013), Tax Administration 2013: Comparative Information on OECD and Other Advanced and Emerging Economies, OECD Publishing. (<http://dx.doi.org/10.1787/9789264200814-en>)

<sup>15</sup> The costs of collection ratio is computed by comparing the annual costs of administration incurred by a revenue body, with the total revenue collected over the course of the fiscal year, and is often expressed as a percentage or as the cost of collecting 100 units of revenue. This ratio is impacted by measures that reduce administrative costs or that improve compliance and revenue. However, there are also a number of other factors that influence the ratio (e.g. changes in tax rates, macro-economic changes, changes in the scope of taxes collected), but which have nothing to do with relative efficiency or effectiveness. For these sorts of reasons, international comparisons of these ratios need to be made with considerable care.

chapter the benchmarks and the findings of the evaluation underlying this report are summarised per subject area.

### **3.1. The organisation of tax administrations**

There are two major trends recognisable in the organisation of tax administrations of Member States. Firstly, there is a trend towards increasing the autonomy of tax administrations. As a basic principle, autonomy can lead to better performance by removing impediments to effective and efficient management while maintaining appropriate accountability and transparency. Generally, the different institutional arrangements of Member States offer more budgetary autonomy as well as autonomy in the management of human resources and the design of the organisational structure. However, in many Member States significant restrictions remain on management.

Secondly, there is a trend from a tax-type towards a taxpayer-type approach in the organisational structure of tax administrations. The taxpayer-type approach embraces, *inter alia*, the creation of specific units for large taxpayers, for high wealth individuals and self-employed, and for risk management. Most Member States have a large taxpayers unit; however, this unit is very often merely an audit centre and does not embrace filing, payment, enforced collection or taxpayer services. Only a few Member States have a distinct unit responsible for the compliance management of high wealth individuals and self-employed, and have set up a distinct risk management unit, supporting a holistic compliance approach.

### **3.2. VAT identification, registration and deregistration**

#### *3.2.1. Benchmarks*

*Registration is transparent and taxpayers are well-informed about how, when and where they can register. There is access to services for taxpayers through helpdesks, online systems or call centres. Non-established taxpayers can easily get access to information. Requests for registration are dealt with timely. The registration process collects information enabling the tax administration to detect and stop fraud at an early stage. From the start, the tax administration monitors filing and payment compliance for risky registrations, embracing early and on-going post-registration on-site visits. Deregistration procedures are effective to deregister quickly missing traders from the VAT system. The register is kept up to date and measures are taken to ensure the quality and reliability of the data in VIES. Tax Authorities and economic operators can rely on the validity of the VAT identification numbers in the VIES system. In cases of suspicious fraudulent intentions and when registration cannot be refused, the tax administrations take precautionary and additional security measures as a pre-requisite for registration.*

#### *3.2.2. Current situation*

The registration process is transparent in most Member States and taxpayers – including non-established taxpayers – are well-informed of how, when and where they can register for VAT (AT, BG, CY, CZ, DK, DE, EE, ES, FI, HU, IE, IT, LT, LV, MT, NL, PL, PT, RO, SE, SI, SK and UK). Non-established taxpayers can easily get access to information in foreign languages, most commonly in English (AT, BG, CZ, DK, EE, ES, FR, HU, IT, LT, LV, LU, MT, NL, PL, SE, SK and UK). However, when more specific and business-related issues emerge, the information given becomes scarcer in foreign languages. Despite noticeable efforts made by many Member States on their website, it remains difficult to know whether certain businesses need to be registered or not, and what the relevant obligations are.

In the registration process the intended activity and the identity of the taxpayer needs to be verified in order to prevent frauds associated with fictitious businesses (also called "missing traders"). A modern registration process is an end-to-end process that embraces pre-registration checks, post-registration monitoring programs for VAT filing and payment compliance of risky traders, and deregistration as soon as the conditions for registration fail to be complied with<sup>16</sup>. With the implementation of Council Regulation 904/2010<sup>17</sup>, pre-registration and deregistration have received more significant attention, but not all Member States have developed an end-to-end process for registration.

At the pre-registration stage, the majority of Member States (except for EL, FR, IT and PT) systematically cross-check the registration application against other sources of data (e.g. company register and internal databases), but they only occasionally carry out on-site visits. Most Member States rely on risk indicators. Insofar as data is available on the rejection of registration in the individual Member States (BE, BG, DK, DE, EE, ES, FR, HU, IE, LT, MT, PL, SE, SI and UK), it appears that registration procedures rarely result in a rejection of registration. Post-registration monitoring programs are implemented by around half of the Member States. On deregistration there is little information available, however, the number of deregistrations ex officio seems to be low and the procedures are generally too slow to stop VAT fraud by missing traders.

Concerning the VIES system (VAT Information Exchange System), the up-to-dateness, completeness, and accuracy of the data available in the system needs to be improved. In particular, the long timeframes for updating the system (BE, EL, ES and PT) and the retroactive deregistration (CY, DK, EL, FR, IE, PL, PT, RO and UK) in a number of Member States are problematic. In the latter case, according to the principle of transparency and legal certainty, the real date of deletion of the VAT number should be made visible in the VIES web version.

### **3.3. Customs Procedure 42**

#### *3.3.1. Benchmarks*

*Member States have put in place a system to enable checking of VAT identification numbers at the time of importation. This embraces an online access to the VIES database containing all valid VAT identification numbers in the EU database. Customs authorities systematically transmit data concerning importations using the Customs Procedure 42 to the tax administration for an efficient exchange of data. Importations using the Customs Procedures 42 are identified as an additional risk in the tax administration's risk analysis system. Results of this risk analysis are exchanged through Eurofisc<sup>18</sup> working field number 3 "Customs Procedure 4200".*

#### *3.3.2. Current situation*

The Customs Procedure 42 is the regime an importer uses in order to obtain a VAT exemption when imported goods will be transported to another Member State. VAT is due in the Member State of destination. When goods are reimported, customs procedure 63 is used. For

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<sup>16</sup> See Article 23 a) and b) of the above mentioned Council Regulation No 904/2010.

<sup>17</sup> Article 22 of COUNCIL REGULATION (EU) No 904/2010 of 7 October 2010 on administrative cooperation and combating fraud in the field of value added tax.

<sup>18</sup> See article 33 of the above mentioned Council Regulation No 904/2010.



the purposes of this report, references to Customs Procedure 42 include customs procedure 63.

Under the Customs Procedure 42, a significant number of Member States fail to check systematically the validity of VAT identification numbers (for both the importers and the customers) (BE, BG, FR<sup>19</sup>, HU, IE, LU, NL, PT and UK) and to exchange the information on the transaction between the Customs and tax administration (EL, IT, NL<sup>20</sup>, PL and SK). Once the information is available to Customs administration, it should be transmitted to the tax administration of the Member State of importation. At that stage, the tax administration can check whether the recapitulative statement has been filed by the importer (or his fiscal representative) and the transaction can thereafter be further monitored.

Despite the high loss of VAT revenue incurred due to the abuse of the Customs Procedure 42, not all Member States identify these transactions as additional risks in domestic risk analysis systems and transmit information through Eurofisc (EE, FI, LU and MT). Since 2011, a specific working field within Eurofisc has been set up to exchange information rapidly on possible fraudulent transactions and traders abusing the Customs Procedure 42.

Several Member States use specific tools, such as licenses (LU, MT, NL and SK) and guarantees (AT, DK, EE, ES, HU, IT, LU, MT, NL, RO and SK) to prevent the abuse of Customs Procedure 42. Licenses and guarantees are a useful tool in the case of risky traders. However, imposing an overall guarantee or license on all traders or fiscal representatives that intend to use the Customs Procedure 42, is a disproportionate burden on honest business and jeopardises the smooth functioning of the internal market by taking away the flexibility and attraction of the simplification provided for by this procedure. Therefore, Member States imposing such a license or guarantee system should only target risky traders.

### **3.4. Filing of VAT returns and payment**

#### *3.4.1. Benchmarks*

*Filing VAT returns is the first step (after registration) in the end-to-end process of establishing VAT liabilities. A systematic approach is in place to monitor and enforce filing obligations and ensure on-time filing of returns. Highly automated business processes, embracing electronic filing of VAT returns and recapitulative VIES statements, are supported by taxpayer profiling tools to determine the most appropriate follow-up action for stop-filers (e.g., phone call, e-mail, text messages, demand notice, personal visit, default assessment or prosecution). Electronic filing is widely used. VAT due and VAT refunds are paid timely. Interest is charged or paid automatically for late payments and refunds. Reasonable penalties support compliance with filing and payment obligations.*

#### *3.4.2. Current situation*

The medium filing ratio (i.e. the number of returns received compared to the number of returns expected) in the EU is high, around 96 per cent. However, there are significant differences across Member States. The individual filing ratio depends inter alia on the

<sup>19</sup>

In France, a systematic and automatic control system is introduced with effect from 1 June 2013.

<sup>20</sup>

The NL has a general domestic reverse charge mechanism for VAT due upon importation. As there is no exemption of VAT upon importation, the recommendations listed for this procedure in the report are not applicable to these types of importations. This does not, however, exclude that there could be importations where the Customs 42 procedure is used, and for which the comments made are valid.

efficiency of an automated filing and payment system, the interest and penalties schemes and the accuracy of the taxpayers' register.

The use of electronic filing is increasing but is not yet in line with reasonable expectations. Only a small majority of Member States have appropriate legislation in place providing for a compulsory electronic filing of VAT returns (AT, BE, BG, DE, DK, EL, ES<sup>21</sup>, FR, IE, IT, LU, LV, NL, PT, RO, SI and UK). In the remaining Member States an option-based system is applicable (CY, CZ<sup>22</sup>, EE, ES, FI, FR<sup>23</sup>, HU, LT, MT, PL, RO, SE and SK). The filing and payment of VAT is systematically monitored by most Member States, however, modern and automatic follow-up processes for late (or non-)filing and payment (e.g. automatic reminders, immediate estimated assessment in case of non-filing) are lacking in a significant number of them (AT, BE, BG, CY, CZ, DE, EE, ES, FI, FR, HU, IT, LV, LT, NL, PL, PT, RO, SE, SI and SK).

All Member States apply sanctions for late (or non-)filing and payment, but the interest and penalty schemes vary significantly between Member States. Current data do not provide any guarantee that such sanctions have an effective impact and penalize taxpayers with an overall cost that is higher than what would have been incurred as part of third-party financing.

The timeliness of VAT refunds has in general improved over the period 2009-2011. In most Member States, a request for a VAT refund is subject to a deadline (AT, BE, BG, CZ, DE, DK, EE, EL, ES, FR, HU, IE, IT, SI, LT, LV, MT, NL, PL, RO and UK) and the effective period of refund is generally within the deadline, being between 30-45 days. There are, however, some Member States where timely refunds remain problematic. A number of Member States do not pay interest in case of late refunds (AT, CY, LU, NL, and UK<sup>24</sup>).

### **3.5. VAT collection and recovery**

#### *3.5.1. Benchmarks*

*The stock of tax debt is stable at less than 10 per cent of annual tax revenues. The backlogs of old debts are regularly reviewed for collectability and appropriate write-off policies are in place. Debt collection operations are conducted by a full time work force of specialized collection staff. The function is highly automated and includes: (i) automated notifications, reminders and warrants; (ii) automatic identification of assets based on third party information and (iii) automatic offsetting of tax credit entitlements against outstanding debts. Debtor profiling tools assist in targeting the most effective means of VAT collection. Out-bound telephone call centres make early contact with new debtors. The administration has a structured and transparent approach for instalments schemes and there is an automatic identification system of assets based on third party information and debtor profiling tools. A holistic government approach is taken to coordinating collection of tax and social security contribution debts.*

#### *3.5.2. Current situation*

There is a growth in VAT arrears (by an average of 15 per cent in most Member States) which can be, at least partly, explained by the recession. However, the level of write-offs is low and

<sup>21</sup> In Spain, electronic filing of VAT returns is obligatory for certain groups of taxpayers, e.g. large taxpayers.

<sup>22</sup> In the Czech Republic, electronic filing of VAT returns is obligatory as of 1 January 2014.

<sup>23</sup> In France, electronic filing of VAT returns is obligatory as of 1 January 2014.

<sup>24</sup> The UK does not automatically pay interest in all cases of late refunds, but the UK does pay repayment supplement where HMRC delay (excluding reasonable enquiry time) resulted in late refunds in relation to VAT return repayment claims.

even close to zero in a number of Member States (BG, CY, EL, FI and MT) which makes it difficult to compare the stock of collectable debts. Debts proven uncollectable at a reasonable cost should be subject to a flexible write-off procedure. Without an on-going write-off programme, the tax administration risks wasting valuable resources pursuing uncollectable amounts as attention is diverted from collectible debt.

In a significant number of Member States the debt collection function is not managed from an end-to-end perspective. A coherent approach is required which manages the debt collection process from the time the debt is established until it is extinguished.

Efforts have been made in most Member States to increase the efficiency of debt collection. There is a clear trend towards non-sequential debt collection processes (AT, BE, BG, DE, ES, FR, HU, IE, LT, LU, LV, PT, SE and UK) as well as to combine tax and social security contribution debts (AT, BG, DK, EE, ES, FI, HU, IE, LV, NL, RO, SE, SI and UK). Around half of Member States have implemented fully or partly integrated recovery processes supported by automatic identification of assets based on internal or third party information (BE, BG, CZ, DK, ES, FI, HU, IE, IT, LT, PT, SI, and SE).

### **3.6. VAT audit and investigation**

#### *3.6.1. Benchmarks*

*The audit programme includes a range of audit approaches that, together with taxpayer services, provides a balanced approach to promoting voluntary compliance. A risk based management system is in place for the selection of taxpayers to be audited and allocating audit resources according to the taxpayers' risk. The tax administration has an appropriate number of staff with adequate training. There is a separation of duties throughout the audit process with checks and balances in place to minimize opportunities for corrupting. An annual operational plan is developed, implemented, and monitored to achieve a suitable level of operational performance. Auditors have access to guidance on technical and procedural topics to ensure consistent and equitable decisions in the field and are equipped with modern audit tools.*

#### *3.6.2. Current situation*

The majority of Member States (except for EL, ES, LU, PT, and RO) apply a risk-based strategy for the selection of taxpayers to be audited and increasingly carry out targeted audits. A number of Member States have however an obligation to audit certain taxpayers for all years (AT, DE, FI, IE, IT, PL, and SI). Even if this obligation only applies to large taxpayers, it prevents Member States from having the flexibility to allocate audit resources to taxpayers that represent higher risk.

There are substantial differences between Member States in the percentage of taxpayers that are subject to field audits and in the amount of VAT additionally assessed as a result of the audit. However, a few Member States does not have performance indicators to assess the effectiveness of their audits (CY, DK, FI, LU and MT). With a large number of staff involved in audit tasks, tax administrations have to assess the effectiveness of their audit work regularly in order to allocate resources accordingly.

E-auditing is well developed in a large majority of Member States. Accordingly, auditors receive e-audit trainings (except for IT and MT) and the means to analyse data that is provided in computer-based systems. At the same time, there are rules in place that require

taxpayers to provide data in computer-based systems during tax audits (AT, BE, BG, CZ, CY, DK, EE, EL, ES, FI, FR, HU, IE, LV, LT, LU, NL, PL, PT, RO, SE, SK, SI and UK). Nevertheless, most Member States do not require the use of a Standard Audit File which would further increase the efficiency and effectiveness of audit work.

In most Member States auditors are provided access to a wide range of categories of third party information (e.g. real estate register, vehicle register, information from social security and from financial institutions), but not always in an automated manner. The majority of Member States frequently request information from other Member States, but there are still significant obstacles (legal, speed, quality of reply and language) that hamper the effectiveness of this tool.

The majority of Member States have specialized VAT anti-fraud units (except for AT, CZ, EE, EL, FI, HU, LV, RO and SI). This is important because the investigation of potential fraud cases needs to be performed by trained investigators integrated in teams that are able to analyse fraud trends and to identify signs of fraudulent activity.

### **3.7. Tax dispute resolution system**

#### *3.7.1. Benchmarks*

*The taxpayer can appeal against decisions by the tax administration in a codified, transparent, fast and low-cost tax dispute resolution system. This system includes a compulsory administrative appeal process, independent of the original decision-maker, before addressing the dispute to the Courts. This administrative appeal process must ensure that only cases of legislative substance are submitted to the judicial appeal process. The tax administration collects management information on the dispute resolution and adjusts its practices as a preventive measure to avoid unnecessary appeals. Payment of the disputed tax is required when a request for judicial review is made and there is minimal backlog of unheard cases. Therefore, there are specialized units and officers specially trained in dealing with tax disputes in or outside the tax administration. The tax administration is able to manage the tax dispute resolution system based on management information data. These data allow the tax administration if needed to adjust their practices.*

#### *3.7.2. Current situation*

Most Member States have a compulsory administrative dispute resolution process, which includes deadlines for making the decisions. Such an approach focusses on the efficiency of the appeal procedure and contributes to reducing the number and the length of appeals. In around half of the Member States the first stage in the tax dispute resolution process is an obligatory administrative appeal procedure within the tax administration.

The number of appeals varies but is high in certain Member States as well as the percentage of decisions made in favour of the taxpayer. However, many Member States do not monitor and collect (sufficient) management information on their tax dispute resolution process and do not feed the outcome of the appeals into preventive measures. In order to minimise unnecessary disputes, all aspects of the appeal procedure should be monitored whereby the outcome of the appeals feeds back into dispute preventive measures and gives rise to adjustments to the taxpayers' services, clarifications of laws and regulations, etc.

In the majority of the Member States the disputed amounts remain fully or partly collectable during the appeal procedure (AT, BE, BG, CY, CZ, DE, DK, EE, EL, ES<sup>25</sup>, FI, FR<sup>26</sup>, HU, LU, LT, LV, MT, NL, PL, RO, SE, SI, SK and UK<sup>27</sup>). This is good practice that safeguards revenue and avoids abuse of the appeal procedure.

### **3.8. VAT compliance**

#### *3.8.1. Benchmarks*

*The tax administrations follow a Compliance Risk Management Strategy, intervening to promote compliance and preventing non-compliance based on the knowledge of taxpayer behaviour. There is a risk based segmentation of taxpayers, allowing tax administration to interact with taxpayers according to their risk pattern. Tax administration provide appropriate taxpayer services, making it easier for taxpayers that want to comply to fulfil their tax obligations and enhance voluntary compliance by influencing behaviour of taxpayers.*

#### *3.8.2. Current situation*

In most Member States there is a trend towards developing and implementing a compliance risk management strategy (AT, BE, BG, CY, CZ, DK, EE, EL, ES, FI, FR, HU, IE, IT, LV, LT, LU, MT, NL, PT, SK, SI, SE and UK). These strategies segment taxpayers according to their risk profile and manage them accordingly in order to promote voluntary compliance. However, only a few Member States assess the outcome of such strategies and measures implemented. Furthermore, very few Member States currently estimate the amount of VAT gap (EE, IT, PL, SK and UK). Without knowing how the VAT gap evolves, it is not possible to evaluate the effectiveness of measures put in place to tackle fraud and evasion. Significant efforts are, therefore, required to improve the monitoring and assessment of performance.

Most Member States also make increased use of information from third parties for audit selection, taxpayer segmentation and debt collection. This can nevertheless be significantly improved in particular for taxpayer segmentation and debt collection.

## **4. CONCLUSIONS**

### **4.1. Modernisation of VAT administration**

Since the beginning of the recession and financial crisis in 2008, the VAT gap has grown, being estimated at around 1.5% of the GDP of EU-26 in 2011. However, there are great disparities in the VAT gaps of individual Member States. In particular,, Member States that are harder hit by the crisis have been struggling with a larger VAT gap and have not been able to improve their situation substantially over time.

As the VAT gap also constitutes an indicator of the efficiency and effectiveness of VAT administration, Member States will have no choice but to modernise VAT administration in order to reduce the VAT gap. This is not only important from the perspective of VAT revenue and own resources, but also from the perspective of businesses and governments when

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<sup>25</sup> In Spain, in case of a tax dispute, the debt collection is generally not postponed. However, it can be postponed if the debtor guarantees the amount of the debt by the endorsement of a credit institution or by a mortgage.

<sup>26</sup> In France, the debtor can request the postponement of the payment of the disputed amount.

<sup>27</sup> In the UK, the taxpayer does not have to pay the VAT in dispute prior to the appeal if either HMCR or the appeal tribunal on appeal are satisfied that payment would result in hardship.

dealing with administrative costs. As concluded in the 2013 study of Paying Taxes, there is a link between compliance costs for businesses and economic growth. Reducing the administrative burdens on businesses appears to benefit economic growth. At the same time, reducing the costs of tax administration by improving its efficiency and effectiveness will provide some relief for the budgetary constraints on governments and help in redressing public finances.

In the current economic and financial climate, modernisation of VAT administration is crucial and inevitable for those Member States that are hardest hit by the financial crisis and that have difficulties handling their budgetary deficits. If these Member States are willing to change established administrative practices and to improve their administrative processes, they can gain substantial benefits from modernisation. It is therefore important that these Member States are supported in their efforts including if requested, by technical assistance.

#### **4.2. Actions to be taken by Member States**

The recommendations of this report are addressed to Member States with the aim of improving their tax administrations and reducing the VAT gap in consequence. The most important recommendations are summarised below by subject area.

In the area of **VAT identification, registration and deregistration**, Member States need to improve the quality of the information available in foreign languages on the requirements and process of VAT registration. At the same time, they also need to (further) develop an end-to-end process for registration, especially by implementing post-registration monitoring programs for risky traders (BG, CY, DE, DK, EL, IE, LT, PT, RO and SK) and fast-track deregistration processes for missing traders (AT, CY, EL, HU, IE, PT and RO). As up-to-date, complete and accurate data available in the VIES system is a prerequisite to enhance legal certainty for legitimate business activities and mutual trust between tax authorities in the EU, a number of Member States will have to improve the quality of their data contained in VIES (BE, EL, ES and PT).

With regard to **Customs Procedure 42**, Member States should ensure that the VAT identification numbers (of both the importer and the customer) are systematically checked (BE, BG, DE, EE, HU, IE, IT, LV, LU, NL, PL, PT, SE and UK) and that all information on the transaction is transmitted domestically to the tax administration (EL, IT, NL, PL and SK). A minority of Member States also needs to identify Customs Procedure 42 as an additional risk in domestic risk analysis systems and reinforce the exchange of information on fraudulent transactions and traders, inter alia by actively participating in Eurofisc (DE, DK, NL, PL and RO). Furthermore, about half of the Member States could consider using licenses or guarantees for risky traders in order to prevent abuse (BE, BG, CY, CZ, DE, FI, FR, EL, IE, LT, LV, PL, PT, SE, SI and UK).

In the area of **filing VAT returns and payment**, most Member States still need to implement a systematic approach to monitor late and non-filing and payment of VAT, embracing automatic processes such as automatic reminders and immediate estimated assessment in case of non-filing (AT, BE, BG, CY, CZ, ES, DE, FI, FR, IT, LU, LV, MT, NL, PL, PT, RO, SE, SI and SK). A few Member States are still expected to ensure a standard effective period for VAT refund of between 30-45 days (AT, BE, EL, ES, CY, FI, IT, LU, MT and SE). Finally, Member States are strongly recommended to investigate the efficiency of their interest and penalties schemes for late and non-filing and payment of VAT.

Concerning **VAT collection and recovery**, in general, half of the Member States must implement write-off procedures for debts proven uncollectable at a reasonable cost (BG, CY, EE, EL, IE, FI, MT and SK). Without an on-going write-off programme, the tax administration risks wasting valuable resources pursuing uncollectable amounts. Additionally, Member States should develop non-sequential and integrated debt collection processes (AT, CY, CZ, DE, DK, EE, EL, FI, IT, LV, LU, MT, NL, PL, RO, SI, SK and UK).

In the area of **VAT audit and investigation**, the recommendations include, on one hand, the abolishment of obligatory audits of certain taxpayers for all years and, on the other hand, the application of risk-based systems (AT, FI, DE, IT, NL, PL and SI). At the same time, e-audit should (further) be promoted and VAT anti-fraud units should be established (AT, CZ, EE, EL, FI, HU, LV, RO and SI).

In the area of **tax dispute resolution system**, a number of Member States should consider the implementation of a compulsory independent administrative dispute resolution process whereby the disputed amounts remain fully or partly collectable during the appeal procedure (BE, BG, CY, EE, EL, FI and IT). Member States are furthermore strongly advised to monitor all aspects of the appeal procedure and to create an environment that minimises unnecessary disputes (AT, BG, CY, HU, IT, LU, LV, NL, RO and SK).

With regard to **VAT compliance**, Member States need to (further) develop and implement compliance risk management strategies and to assess the outcome of the measures implemented in order to identify best strategies to influence behaviour of taxpayers to voluntarily comply with their tax obligations (BE, CY, CZ, DE, DK, FI, FR, IE, IT, LU, MT, NL, PL, PT, SE, SI and SK). Additionally, the use of third party information can be improved significantly in particular for taxpayer segmentation and debt collection.

#### **4.3. Actions to be taken by the Commission**

The Commission will continue to use the Article 12 arrangements to evaluate the functioning of VAT administrations in order to stimulate improvements in VAT administration of Member States. In a modern tax administration evaluation cycles have an important role as they can be used to improve the quality of administration. Proper evaluations require indicators that enable to monitor progress from period to period. The VAT-gap can be seen as such an indicator.

The Commission will continue to facilitate the exchange of information on administrative practices and will pool such information in order identify best practices. Identifying best practices can contribute to streamlining the VAT system and thus to reducing compliance costs, while securing VAT revenue at the same time.

The Commission will support Member States in their efforts to modernise VAT administration and enhance compliance. A more efficient and effective VAT administration will not only contribute towards increasing VAT revenue, but also towards equal treatment of all Member States in respect of their contributions to the budget of the Union.

The Commission will coordinate and facilitate any requests for technical assistance received from Member States. As mentioned before, modernisation of VAT administration is crucial and inevitable for those Member States that are hardest hit by the financial crisis and have difficulties handling their budgetary deficits.