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Proposal for a

COUNCIL IMPLEMENTING DECISION

**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**

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 16 February 2017, the Italian Republic requested authorisation to continue to derogate from Articles 206 and 226 of the VAT Directive with regard to value added tax (VAT) payment and invoicing requirements for supplies of goods and services made to public authorities. Italy also requested to broaden the scope of the authorisation and apply the derogation from Articles 206 and 226 of the VAT Directive for supplies of goods and services to companies controlled by central and local public authorities and a list of companies listed on the stock exchange. In accordance with Article 395(2) of the VAT Directive, the Commission informed the other Member States by letter dated 15 March 2017 of the request made by the Italian Republic. By letter dated 16 March 2017, the Commission notified the Italian Republic that it had all the information necessary to consider the request.

1. CONTEXT OF THE PROPOSAL

• Reasons for and objectives of the proposal

Following the introduction of a system of statistical checks, Italy discovered considerable VAT fraud in relation to supplies of goods and services to public authorities. To put an end to these practices Italy requested in 2014 that, for supplies to public authorities, the VAT due would no longer be paid to the supplier, but to a separate and blocked bank account of the tax authorities.

The derogation was authorised by Council Implementing Decision (EU) 2015/1401¹ until 31 December 2017. It authorised Italy to derogate from Article 206 of the VAT Directive regarding VAT payment and from Article 226 of the VAT Directive regarding the invoicing rules.

The derogation was requested by Italy for a limited period allowing it to organise and implement adequate control policy measures and to fully benefit from the data available via electronic invoicing. The implementation of the obligation of electronic invoicing for supplies to public authorities, allowing the possibility of real-time control of individual transactions and the exact amounts of VAT which public authorities are due to pay on their purchases, should allow Italy to audit the sector concerned on the basis of conventional control techniques without the need to derogate from the VAT Directive.

According to information submitted by Italy, the introduction of electronic invoicing for supplies to public authorities provided tax authorities considerable information regarding the flow of invoices allowing the control of transactions and corresponding VAT amounts. However, another element of the effective control system – the obligation to communicate data of all invoices issued and received to the tax authorities – was only introduced as from 1 January 2017. It is still much in the start-up phase and more time is required for the measure to be effective and to effectively induce taxpayers to improve their compliance with tax obligations. Consequently, Italy will not be in a position to finalise the organisation and implementation of adequate control policy measures before the expiry of the current

¹ OJ L 217, 18.8.2015, p. 7–8.

derogation measure, i.e. 31 December 2017. By letter registered with the Commission on 16 February 2017 Italy requested to prolong the current derogation from Articles 206 and 226 of the VAT Directive on supplies to public authorities until end of 2020.

Additionally, Italy discovered tax evasion in the sector of supplies to companies controlled by public authorities and to a small group of 40 companies that are listed on the stock exchange. In order to fight this tax evasion and to ensure no further VAT losses for public revenues, Italy, by letter registered with the Commission on 16 February 2017, requested to broaden the scope of the derogation from Articles 206 and 226 of the VAT Directive to supplies of goods and services made to the above mentioned entities which are considered by Italy as reliable as public authorities. These entities are both companies controlled by central and local public authorities and a list of around 40 companies listed on the stock exchange adding up to a total of around 2.400 companies. Italy expects that extending the split payment measure to these companies will tackle tax evasion in the form of non-payment of VAT by the suppliers to the entities concerned and consequently will increase the VAT revenues.

In June 2016, Italy presented a report in accordance with Article 3(2) of the Council Implementing Decision (EU) 2015/1401. According to this report, the split payment measure introduced in Italy increased VAT revenues and this increase was higher than the estimates made at the time of the introduction of the measure. Furthermore, the report stated that the measure had no negative impact on the VAT refunds of the suppliers. It has, according to Italy, proven to be an effective measure to radically tackle any form of tax evasion resulting from the non-payment of the VAT by suppliers to public authorities.

According to information submitted by Italy, as from 1 January 2017, additional control measures are applied in Italy. These are the optional accounting system known as 'electronic invoicing' and an obligation of reporting to tax authorities of invoices issued and received which will apply to companies for which the broadening of the scope of the derogation is requested and to their suppliers. They will allow the Italian tax authorities to cross-check the different operations declared by the operators and monitor the payments of VAT made. However, these control measures are in a start-up phase and more time is required to assess their effectiveness in inducing taxpayers to comply with their tax obligations. In the subsequent years the effectiveness of these measures will be assessed by Italy, as well as the need for a continued application of the derogating measure.

One of the effects of the measure is the fact that suppliers being taxable persons are not able to offset the VAT paid on their input with the VAT received on their supplies. They may constantly be in a credit position and may need to ask for an effective refund of this VAT from the tax administration. On the other hand, under certain conditions Italy authorises these suppliers to offset the VAT they did not receive from their customers with other taxes due in Italy, thus limiting the cash flow problem that otherwise may arise for businesses liable for paying their taxes in Italy.

At the time of application for the existing derogation, Italy reformed its system of VAT refund². In the report presented in June 2016 as required by Article 3(2) of the Council Implementing Decision (EU) 2015/1401, Italy states that its system of VAT refunds works properly and that although it is not possible to accurately estimate the average duration of the refund procedures, it can reasonably be said that the average period for VAT refunds does not exceed 3 months. Moreover, according to information provided by Italy, suppliers to public authorities are covered by a priority procedure in which case the period of refund is even

² The Italian VAT refund system was reformed in response to the infringement procedure n° 2013/4080, which is still on-going as some issues remain open, e.g.: the repayment of guarantee costs.

shorter. According to Italy, the new rules that have been in force are expected to properly manage any possible increase of VAT refunds.

Given the broader scope of the derogation and the concerns of businesses in respect of the VAT refunds, 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 situation of VAT refunds for the taxable persons covered by the derogation. Italy is therefore requested to provide a report on the VAT refund procedure with regard to the situation of suppliers (taxable persons) covered by the derogation fifteen months after its entry into force. This report should, in particular, provide statistics as regards the average time needed to effectively refund the VAT to these taxable persons and outline particular problems that might have occurred in this context. This report should also indicate the effectiveness of the measures installed in combatting the tax evasion for the supplies covered by the derogation.

It is proposed to authorise the derogation as from 1 May 2017 until 30 April 2020.

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

According to Article 206 of the VAT Directive, the taxable person liable for payment of VAT must pay the net amount of the VAT when submitting the VAT return. By requesting that VAT on the supplies made is paid by customers (public authorities, entities controlled by central and local public authorities and companies listed in the stock exchange), it is necessary to derogate from this Article. It is also necessary to derogate from Article 226 of the VAT Directive regarding the maximum invoice details that can be requested from taxable suppliers as to allow the introduction of a special additional mentioning on the invoice indicating that the amount of VAT has to be paid to that separate account and not to the supplier.

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. Italy requested the derogating measure to fight tax evasion in the sectors of supplies to public authorities, companies controlled by central and local public authorities and companies listed on the stock exchange. Based on the elements provided by Italy, the derogation is consistent with the existing policy provisions.

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 proposal falls under the exclusive competence of the Union. The subsidiarity principle therefore 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.

Given that the derogation is limited in time and restricted to the public sector, to companies that are state-controlled and to companies listed on the stock exchange, the scope is targeted to a sector that poses considerable problems of tax evasion. Therefore, the special measure is proportionate to the aim pursued, i.e. to combat tax evasion.

To address the concerns of businesses regarding the VAT refunds, Italy is requested to provide a report on the VAT refund procedure with regard to the situation of suppliers (taxable persons) covered by the derogation fifteen months after its entry into force. Italy also assured that suppliers covered by the derogation can use priority procedure for refunds. Detailed information and statistical data regarding the number of refund requests made by taxable persons covered by this derogation as well as the time it took for these persons to effectively obtain the refund should be provided.

Finally, Italy is in contact with the Commission regarding the VAT refund procedure and a number of measures to improve the process of refunds have already been taken by Italy and are to be implemented. Italy assured the Commission that the situation of suppliers covered by the split payment is of particular concern to Italian authorities.

- **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.

Since the scope and time period for the requested derogation would overlap with the current derogation granted to Italy through Council Implementing Decision (EU) 2015/1401, the latter will be repealed and replaced with this new Implementing Decision.

3. RESULTS OF EX-POST EVALUATIONS, STAKEHOLDER CONSULTATIONS AND IMPACT ASSESSMENTS

- **Impact assessment**

The proposal for a Council Implementing Decision aims at prolonging the application of the derogation from Articles 206 and 226 of the VAT Directive for supplies to public authorities for additional 3 years. It further aims at broadening the scope of the derogating measure for supplies to companies controlled by central and by local authorities and to a list of around 40 companies listed on the stock exchange, a total of around 2.400 companies. The prolonged measure with broadened scope covers approximately 640.000 suppliers. By imposing that the VAT due is paid to a separate bank account of the tax administration, the proposal for a Council Implementing Decision aims in the first place at combating tax evasion in the form of non-payment of VAT by suppliers to the listed entities. The measure currently applied by Italy for supplies to public authorities appeared to be an effective tool for this aim.

However, as suppliers under this system do not receive the VAT from their clients, they will more often have to ask for an effective refund of the VAT, in case they cannot offset this VAT with other taxes due in Italy. To avoid a negative impact on these taxable persons, even more so if the suppliers are not established in Italy, it is essential that the refund procedure is functioning properly and timely. According to Italy, its system of VAT refunds works properly and the average period for VAT refunds does not exceed 3 months. Furthermore, the new rules that have been in force are expected to properly manage any possible increase of VAT refunds. Moreover, according to information provided by Italy, suppliers to public authorities are covered by a priority procedure in which case the period of refund was even shorter than the 3 months mentioned above.

4. BUDGETARY IMPLICATIONS

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

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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 tax³, and in particular Article 395(1) thereof,

Having regard to the proposal from the European Commission,

Whereas:

- (1) By Council Implementing Decision (EU) 2015/1401⁴, Italy is authorised to require that value added tax (VAT) due on supplies to public authorities is to be paid by the latter to a separate and blocked bank account of the tax authorities. The measure constitutes a derogation from Articles 206 and 226 of Directive 2006/112/EC in relation to VAT payment and invoicing rules.
- (2) By letter registered with the Commission on 16 February 2017, Italy requested to prolong that authorisation. At the same time Italy requested to broaden the scope of the derogation for supplies of goods and services made to companies controlled by central and local public authorities and to a list of companies listed on the stock exchange.
- (3) The Commission informed the other Member States of the request made by Italy by letter dated 15 March 2017. By letter dated 16 March 2017, the Commission notified Italy that it had all the information it considered necessary for appraisal of the request.
- (4) Italy introduced additional control measures allowing tax authorities to cross-check the different operations declared by the operators and to monitor the payments of VAT made on the blocked state accounts. However, these control measures are in a start-up phase and more time is required to assess their effectiveness in inducing taxpayers to comply with their tax obligations. Thus, Italy is not in the position to finalise the organisation and implementation of adequate control policy measures before the expiry of Implementing Decision (EU) 2015/1401, i.e. before 31 December 2017. Therefore, Italy requested the prolongation of that derogation.
- (5) Italy detected fraud with regard to supplies of goods and services to other entities controlled by central and local public authorities and a number of companies listed on the stock exchange. To tackle the tax evasion in the form of non-payment of VAT by the suppliers to the entities concerned, Italy requests to derogate from Article 206 of

³ OJ L 347, 11.12.2006, p. 1.

⁴ Council Implementing Decision (EU) 2015/1401 of 14 July 2015 authorising Italy to introduce a special measure derogating from Articles 206 and 226 of Directive 2006/112/EC on the common system of value added tax (OJ L 217, 18.8.2015, p. 7).

Directive 2006/112/EC and to require that also VAT due on supplies of goods and services to these companies controlled by central and local public authorities and to the 40 companies listed on the stock exchange is paid by those entities to the separate and blocked account of the tax authorities. In addition, it is also necessary to derogate from Article 226 of Directive 2006/112/EC as to allow for a special remark on the invoice that VAT has to be paid onto that special account.

- (6) One of the effects of the measure is the fact that suppliers being taxable persons are not able to offset the VAT paid on their input with the VAT received on their supplies. They may be constantly in a credit position and may need to ask for an effective refund of this VAT from the tax administration. In the report presented in June 2016 as required by Article 3(2) of Implementing Decision (EU) 2015/1401, Italy demonstrated that its system of VAT refunds works properly and that the average period for VAT refunds does not exceed 3 months. Moreover, according to information provided by Italy, suppliers to public authorities were covered by a priority procedure in which case the period of refund was even shorter. According to Italy, the new rules that have been in force are expected to properly manage any possible increase of VAT refunds.
- (7) In 2014, Italy has introduced an obligation of electronic invoicing for supplies of goods and services to public authorities. That should allow for a proper control of the sector concerned in the future when an adequate control policy will have been developed and deployed on the basis of electronically available data. As from 1 January 2017, additional control measures are applied in Italy. These are the optional accounting system (known as 'electronic invoicing') and an obligation of reporting to tax authorities of invoices issued and received which would apply to companies for which the derogation is requested and to their suppliers. They would allow the Italian tax authorities to cross-check the different operations declared by the operators and monitor the payments of VAT made. Once this system is fully implemented, there should be no more need to derogate from Directive 2006/112/EC. Therefore, Italy has offered assurance not to seek renewal of the derogating measure.
- (8) The derogation requested should be limited in time to allow an assessment whether the special measure is appropriate and effective.
- (9) To guarantee the necessary follow-up within the framework of this derogation and in particular the impact on the situation of VAT refunds of taxable persons covered by the derogation, Italy should be required to submit a report to the Commission within 15 months after the entry into force of the derogating measure in Italy regarding the overall situation of, and in particular the average time needed for, VAT refunds to taxable persons and on the effectiveness of the measures introduced in reducing the tax evasion in the sectors concerned. Italy should continue the reforms to ensure a smooth and timely VAT refund procedure.
- (10) The derogating measure is proportionate to the objectives pursued since it is limited in time and restricted to sectors which pose considerable problems of tax evasion. In addition, the derogating measure does not give rise to the risk that fraud would shift to other sectors or other Member States.
- (11) 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.
- (12) The Implementing Decision (EU) 2015/1401 should be repealed,

HAS ADOPTED THIS DECISION:

Article 1

By way of derogation from Article 206 of Directive 2006/112/EC, Italy is authorised to provide that the VAT due on supplies of goods and services to the following entities has to be paid by the recipient to a separate and blocked bank account of the tax administration:

- public authorities;
- companies controlled by public authorities within the meaning of Article 2359 of the Italian Civil Code (Codice Civile);
- companies listed on the stock exchange, the list of which will be published by Italy in the Italian Official Journal (Gazzetta Ufficiale) after the entry into force of this Decision and revised annually if necessary.

Article 2

By way of derogation from Article 226 of Directive 2006/112/EC, Italy is authorised to require that invoices, issued in relation to supplies of goods and services to the entities listed under Article 1 include a special remark that VAT has to be paid to that separate and blocked bank account of the tax administration.

Article 3

Italy shall notify the national measures referred to in Articles 1 and 2 to the Commission.

Within 15 months after the entry into force in Italy of the measures referred to in Articles 1 and 2, Italy shall submit a report to the Commission on the overall situation of VAT refunds to taxable persons affected by these measures and, in particular, on the average duration of the refund procedure and on the overall effectiveness of this measure to reduce VAT avoidance in the sectors concerned.

Article 4

Implementing Decision (EU) 2015/1401 is repealed with effect from 1 May 2017.

Article 5

This Decision shall apply from 1 May 2017 to 30 April 2020.

Article 6

This Decision is addressed to the Italian Republic.

Done at Brussels,

*For the Council
The President*