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**PROPOSAL**

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| From: | Secretary-General of the European Commission, signed by Mr Jordi AYET PUIGARNAU, Director |
| date of receipt: | 22 June 2020 |
| To: | Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union |
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| Subject: | Proposal for a COUNCIL IMPLEMENTING DECISION amending Implementing Decision (EU) 2017/784 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 |

Delegations will find attached document COM(2020) 242 final.

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EUROPEAN
COMMISSION

Brussels, 22.6.2020
COM(2020) 242 final

2020/0119 (NLE)

Proposal for a

**COUNCIL IMPLEMENTING DECISION**

**amending Implementing Decision (EU) 2017/784 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[1] ('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 4 December 2019, the Italian Republic requested authorisation to continue to derogate from Articles 206 and 226 of the VAT Directive with regard to VAT payment and invoicing requirements for supplies of goods and services made to public authorities. That request implied a reduction of the scope of the derogating measure in force, granted by Council Implementing Decision (EU) 2017/784[2], which also applied to supplies of goods and services to companies controlled by central and local public authorities and to a list of companies listed on the stock exchange.

However, by letter registered with the Commission on 27 March 2020, Italy changed its request, asking that the scope of the authorisation should remain identical to that granted by Council Implementing Decision (EU) 2017/784, and therefore requesting to apply the derogation from Articles 206 and 226 of the VAT Directive for supplies of goods and services made to public authorities, to companies controlled by central and local public authorities and to 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 5 May 2020 of the request made by the Italian Republic. By letter dated 6 May 2020, 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. This mechanism is commonly referred to as a type of ‘split payment’, as the payment which is usually transferred in full by the customer to the supplier (consideration in exchange for the supply plus VAT) is split into: (i) on the one hand, the consideration which is paid to the supplier of the goods or services; and, (ii) on the other hand, the VAT due is paid to a blocked bank account of the tax authorities.

The derogation was authorised by Council Implementing Decision (EU) 2015/1401[3] 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.

[1] OJ L 347, 11.12.2006, p. 1.
[2] OJ L 118, 6.5.2017, p. 17.
[3] OJ L 217, 18.8.2015, p. 7–8.

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 in order to apply the split payment measure.

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. More time was required for the measure to be effective and to effectively induce taxpayers to improve their compliance with tax obligations. Consequently, Italy requested to prolong the derogation from Articles 206 and 226 of the VAT Directive on supplies to public authorities.

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 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 were 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 expected that extending the split payment measure to these companies would tackle tax evasion in the form of non-payment of VAT by the suppliers to the entities concerned and consequently would increase the VAT revenues.

The extension of the derogation with its widened scope was authorised by Council Implementing Decision (EU) 2017/784 until 30 June 2020.

In October 2018, Italy presented a report in accordance with second paragraph of Article 3 of the Council Implementing Decision (EU) 2017/784. 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 increase in VAT credit for the suppliers of the companies within the scope of the split payment, which results from the implementation of the measure, can be easily controlled and managed and that the situation of VAT refunds had not worsened.

The split payment mechanism is part of a package of measures introduced by Italy in order to counter tax fraud and evasion. This package of measures involves amongst others electronic invoicing and the electronic transmission of data on daily charges. Electronic invoicing was introduced as of 1 July 2018 in respect to certain sectors, and as of 1 January 2019 in a generalised form. This obligation was authorised by Council Implementing Decision (EU) 2018/593[4]. The electronic transmission of data on daily charges requires taxpayers engaged in

4 Council Implementing Decision (EU) 2018/593 of 16 April 2018 authorising the Italian Republic to introduce a special measure derogating from Articles 218 and 232 of Directive 2006/112/EC on the common system of value added tax, OJ L 99, 19.4.2018, p. 14-15.

the retail trade and similar activities (not involving invoicing obligations) to store data on daily charges electronically and transmit them electronically to the *Agenzia delle Entrate*. This latter obligation became applicable on 1 January 2020 and, for taxpayers with a turnover of over EUR 400 000, on 1 July 2019. This package of measures has replaced other control measures, and allows the Italian tax authorities to cross-check the different operations declared by the operators and to monitor their VAT payments. The latest legislative changes introduced an obligation to make the data on VAT transactions from electronic invoices, cross-border transactions and electronic charges immediately available to taxpayers in order to simplify their compliance; it will lead to VAT returns being pre-completed by the *Agenzia delle Entrate* and to the preparation of regular VAT assessments, which taxpayers will be able to accept or supplement. According to recital 7 of the abovementioned Decision 2017/784, once this system is fully implemented, there should be no need to further derogate from Directive 2006/112/EC in order to apply the split payment measure.

However, according to the Italian authorities, at this moment it would not be convenient to remove altogether the measure on split payment. According to their estimates, the measures implemented through the anti-fraud package reduce the time needed by the tax administration to become aware of the existence of a potential case of evasion or fraud to three months, compared to the 18 months that were originally necessary. Nevertheless, in the absence of split payment, the recovery from the tax evaders or fraudsters once the check has been carried out could prove to be impossible if they are insolvent. The split payment mechanism, as an ex ante measure, provides a much higher effectiveness.

The Commission still considers that the full implementation of the package of anti-fraud measures designed by Italy should end the need for further derogations from the VAT Directive in order to apply the split payment. However, it is still early to fully assess the effectiveness of those measures due to their recent implementation. The generalised mandatory e-invoicing only entered into force on 1 January 2019 while the electronic transmission of data on daily charges was fully implemented on 1 January 2020. Therefore, the evaluation of these measures and their impact in the detection of VAT fraud and the collection of the tax cannot be carried out extensively. Thus, in the absence of the full implementation of the anti-fraud package, it is advisable to extend the measure for an additional period, as its removal could have significant negative effects in the fight against tax evasion and the collection of VAT in relation to the sectors covered by the scope of the measure. Further, in case the measure will not be extended, the companies applying the split payment mechanism would have to change their invoicing systems to accommodate the changes. The tax administration would have to implement similar adaptations to its systems. Due to the difficulties caused by the COVID-19 outbreak, that Italy is experiencing it does not seem appropriate to request businesses and tax administration to undertake these changes at this moment.

One of the effects of split payment 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.

According to the information submitted by Italy, the refund procedure has been speeded up. Requests for refund are processed on average within 67 days and the average time for actual payment to the beneficiary is 7 days. At the time of the introduction of the split payment measure, it was envisaged that the taxable persons who carry out transactions subject to the split payment scheme, within the limit of the credit deriving from such transactions, are entitled to receive the payment of the relevant VAT credits as a priority. This practice implies that refund requests related to the split payment mechanism are processed with priority both during preliminary investigation and during the payment of sums due vis-à-vis non-priority refunds.

The request submitted by Italy and registered with the Commission on 4 December 2019, implied a reduction of the scope of the derogating measure in force, as it was requested authorisation to continue to derogate from Articles 206 and 226 of the VAT Directive only with regard to VAT payments and invoicing requirements for supplies of goods and services made to public authorities. However, by letter registered with the Commission on 27 March 2020, Italy changed its request, asking that the scope of the authorisation should remain identical to that granted by Council Implementing Decision (EU) 2017/784, and therefore requesting to apply the derogation from Articles 206 and 226 of the VAT Directive for supplies of goods and services made to public authorities, to companies controlled by central and local public authorities and a list of companies listed on the stock exchange.

The reason for changing the scope was that in the meantime the definitive data on the effectiveness of the measure became available, showing that the effectiveness of the measure was higher than indicated in previous reports. The request for extension submitted in December 2019 was modified by requesting the extension of the derogating measure authorised by Council Implementing Decision (EU) 2017/784.

Given the broad scope of the derogation and the fact that the concerns of businesses in respect of the VAT refunds still persist, 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 eighteen 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 different measures implemented to combat the tax evasion for the supplies covered by the derogation, their date of entry into force, as well as an evaluation of their effectiveness.

Even though Italy requested the authorisation to be prolonged until 31 December 2023, it is proposed to authorise the derogation as from 1 July 2020 until 30 June 2023. That period should be sufficient to make a complete evaluation of the effectiveness of the measures implemented aimed to reducing tax evasion in the sectors concerned. Further, by then businesses and tax administration will be in a better position to undertake the necessary adaptations in their systems.

- **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. Italy requested the derogating measure to fight tax evasion in the sectors in which VAT fraud has been detected for years and, according to the data provided by Italy, the measure has been effective to improve tax collection and curb VAT fraud in the sectors targeted. The derogation is consistent with the existing policy provisions.

By Council Implementing Decision (EU) 2019/310[5] Poland was granted a similar derogation to apply the split payment mechanism. The Polish split payment system comprises a voluntary and a mandatory split payment mechanism. This mandatory split payment system affects supplies of goods and services paid by electronic bank transfers, carried out between taxable persons in areas particularly exposed to VAT fraud and in which fraud has been detected for years. In the Polish mandatory split payment system, the bank acts as a splitting agent, transferring the amount paid by the customer to the relevant accounts of the supplier, i.e. the taxable amount to the regular account of the trader and the VAT amount to the trader's blocked VAT account. Funds on the blocked VAT account are owned by the taxable person, however, his possibility to dispose of the funds is limited in principle to the payment of VAT due to the tax authority or to the payment of VAT resulting from invoices received from suppliers.

Also Romania applied for derogation to apply the split payment mechanism to supplies by certain taxable persons. The Romanian split payment mechanism raised serious concerns regarding its proportionality and its compatibility with the Treaty. Consequently, the Commission objected to the Romanian request.[6]

## 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 it is based, the proposal falls under the exclusive competence of the European Union. Hence, the subsidiarity principle does not apply.

### • Proportionality

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.

### • Choice of the instrument

The instrument proposed is a Council Implementing Decision.

Under Article 395 of the VAT Directive, a derogation from the common VAT rules is only possible upon authorisation by the Council, which is acting unanimously on a proposal from

[5] Council Implementing Decision (EU) 2019/310 of 18 February 2019 authorising Poland to introduce a special measure derogating from Article 226 of Directive 2006/112/EC on the common system of value added tax, OJ L 51, 22.2.2019, p. 19.

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

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**

No stakeholder consultation has been conducted. The present proposal is based on a request made by Italy and concerns only this particular Member State.

- **Collection and use of expertise**

There was no need for external expertise.

- **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, to companies controlled by central and by local authorities and to a list of around 40 companies listed on the stock exchange. 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 appeared to be an effective tool for this aim.

According to the data provided by Italy, the implementation of the measure in its initial scope has entailed an increase in payments of about EUR 3.5 billion in the year 2015. This amount was determined by the *Agenzia delle Entrate*, by considering that for the suppliers of the *Pubblica Amministrazione* (PA), for the same transactions, the sum of the lower output VAT actually paid following the introduction of split payment mechanism, net of the increase in compensations and refunds, is lower than the payments made by the PA relating to the same transactions. Further analysis made by Italy conclude that this effect has remained stable in subsequent years. According to this analysis, the broadened scope of the measure (suppliers of companies controlled by central and local authorities and companies listed on the stock exchange) has reported an additional increase in payments of EUR 1.08 billion. Again, this initial effect of the measure has remained stable in subsequent years of its application. Therefore, the total effect due to the application of the measure amounts to EUR 4.58 billion per year.

Another effect that should be taken into account is that suppliers under this system do not receive the VAT from their clients. Therefore, 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 processing VAT refunds has been reduced to 67 days, plus 7 days for the actual payment to the beneficiary. 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, at the same time of the introduction of the split payment measure, it was envisaged that the taxable persons who carry out transactions subject to the split payment scheme, within the limit of the credit deriving from such transactions, are entitled to receive the payment of the relevant VAT credits as a priority. This provision implies that refund requests related to the split payment mechanism are processed with priority both during preliminary investigation and during the payment of sums due by comparison to non-priority refunds.

- **Fundamental rights**

The proposal does not have any consequences for the protection of fundamental rights.

## 4. BUDGETARY IMPLICATIONS

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

2020/0119 (NLE)

Proposal for a

# COUNCIL IMPLEMENTING DECISION

## amending Implementing Decision (EU) 2017/784 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

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 valued added tax[1], and in particular Article 395(1) thereof,

Having regard to the proposal from the European Commission,

Whereas:

(1) By Council Implementing Decision (EU) 2015/1401[2], Italy was authorised until 31 December 2017 to require that value added tax (VAT) due on supplies to public authorities was to be paid by those authorities to a separate and blocked bank account of the tax authorities. That special measure constituted a derogation from Articles 206 and 226 of Directive 2006/112/EC in relation to VAT payment and invoicing rules.

(2) By Council Implementing Decision (EU) 2017/784[3] Italy was authorised to apply the special measure until 30 June 2020. Furthermore, the scope of the special measure was broadened, to include supplies to companies controlled by public authorities within the meaning of Article 2359 of the Italian Civil Code (*Codice Civile*) and to companies listed on the stock exchange that are included in the Financial Times Stock Exchange Milano Indice di Borsa ('FTSE MIB') index.

(3) By letter registered with the Commission on 4 December 2019, Italy requested this authorisation to be prolonged until 31 December 2023 and that the scope of the special measure be reduced for supplies of goods and services to public authorities only. By letter registered with the Commission on 27 March 2020, Italy requested that the scope of the measure for supplies of goods or services be broadened to apply both to companies controlled by central and local public authorities and to listed companies included in the FTSE MIB index. As a result, Italy requests that the special measure to be prolonged with identical scope of the authorisation granted by Implementing Decision (EU) 2017/784.

[1] OJ L 347, 11.12.2006, p. 1.
[2] OJ L 217, 18.8.2015, p. 7–8.
[3] OJ L 118, 6.5.2017, p. 17.

(4) By letter dated 5 May 2020, the Commission informed the other Member States, pursuant to Article 395(2), the second subparagraph, of Directive 2006/112/EC, of the request made by Italy. By letter dated 6 May 2020, the Commission notified Italy that it had all the information it needed to appraise the request.

(5) This measure is part of a package of measures introduced by Italy in order to counter tax fraud and evasion. As of 1 July 2018 in respect to certain sectors, and as of 1 January 2019 in a generalised form, an electronic invoicing obligation has been introduced. The obligation was authorised by Council Implementing Decision (EU) 2018/593[4]. That package of measures, including electronic invoicing, has replaced other control measures, and allows the Italian tax authorities to cross-check the different operations declared by the operators and to monitor their VAT payments.

(6) Italy explains in its request that, even though the package of measures implemented reduces the time needed by the tax administration to become aware of the existence of a potential case of evasion or fraud to three months, compared to the eighteen months that were originally necessary, in the absence of split payment the recovery from the tax evaders or fraudsters once the check has been carried out could be impossible if they are insolvent. The split payment mechanism, as an ex ante measure, provides a much higher effectiveness. The definitive data on the effectiveness of the measure show that the measure has been even more effective than expected.

(7) 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. According to the information submitted by Italy, requests for refund are processed on average within 67 days and the average time for actual payment to the beneficiary is 7 days. At the time of the introduction of the split payment measure, it was envisaged that taxable persons carrying out transactions subject to the split payment scheme, within the limit of the credit deriving from such transactions, are entitled to receive the payment of the relevant VAT credits as a priority. This practice implies that refund requests related to the split payment mechanism are processed with priority both during preliminary investigation and during the payment of sums due vis-à-vis non-priority refunds.

(8) According to recital (7) of Implementing Decision (EU) 2017/784, once the system composed by the package of control measures Italy intended to apply was fully implemented, there should be no more need to derogate from Directive 2006/112/EC in order to apply the split payment. Therefore, Italy offered assurance that it would not seek to renew the derogation allowing the application of the split payment mechanism. However, given that it is still early to fully assess the effectiveness of these measures due to their recent implementation, and in view of the time of difficulties that Italy is experiencing due to the COVID-19 outbreak, which makes it more difficult for taxable persons to implement the changes required in their invoicing systems, and for the tax administrations to adapt theirs, the removal of the measure could have significant negative effects in the fight against tax evasion and the collection of VAT, as well as on the administrative costs for taxable persons under the current circumstances.

[4] Council Implementing Decision (EU) 2018/593 of 16 April 2018 authorising the Italian Republic to introduce a special measure derogating from Articles 218 and 232 of Directive 2006/112/EC on the common system of value added tax, OJ L 99, 19.4.2018, p. 14-15.

(9) The requested derogation should be limited in time to allow an assessment whether the special measure is appropriate and effective. Even though Italy requested the authorisation to be prolonged until 31 December 2023, it should not be prolonged further than 30 June 2023. That period should be sufficient to make a complete evaluation of the effectiveness of the measures implemented aimed to reducing tax evasion in the sectors concerned.

(10) To guarantee the necessary follow-up within the framework of this derogation and, in particular, the impact on VAT refunds to taxable persons covered by the derogation, Italy should submit a report to the Commission, within 15 months after the prolongation of the special measure takes effect, on the overall situation of, and, in particular, the average time needed for, VAT refunds to taxable persons, and on the effectiveness of this special measure and others implemented aimed to reducing tax evasion in the sectors concerned. The report should include a list of the different measures implemented together with their date of entry into force.

(11) The special 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 special measure does not give rise to the risk that evasion would shift to other sectors or other Member States.

(12) 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.

(13) Implementing Decision (EU) 2017/784 should therefore be amended accordingly,

HAS ADOPTED THIS DECISION:

*Article 1*

Council Implementing Decision (EU) 2017/784 is amended as follows:

(1) In Article 3, the second subparagraph is replaced by the following:

'By 30 September 2021, Italy shall submit a report to the Commission on the overall situation of VAT refunds to taxable persons affected by the measures referred to in Articles 1 and 2 and, in particular, on the average duration of the refund procedure and on the effectiveness of this measure and others implemented aimed at reducing tax evasion in the sectors concerned. This report shall include a list of the different measures implemented together with their date of entry into force';

(2) In Article 5, the date '30 June 2020' is replaced by the date '30 June 2023'.

*Article 2*

This Decision is addressed to the Italian Republic.

Done at Brussels,

*For the Council*
*The President*