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COMMUNICATION FROM THE COMMISSION TO THE COUNCIL

in accordance with Article 395 of Council Directive 2006/112/EC

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1. BACKGROUND

Pursuant to Article 395 of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (the VAT Directive), the Council, acting unanimously on a proposal from the Commission, may authorise any Member State to introduce special measures for derogation from the provisions of this Directive, in order to simplify the procedure for collecting VAT or to prevent certain forms of tax evasion or avoidance. As this procedure provides for derogations from the general principles of VAT, in accordance with the consistent rulings from the European Court of Justice, such derogations should be proportionate and limited in scope.

By letter registered with the Commission on 7 January 2013, Hungary has requested to be authorised to introduce a measure derogating from Article 193 of the VAT Directive. In accordance with the second paragraph of Article 395 of that Directive, the Commission informed the other Member States by letter dated 12 February 2013 of the request made by Hungary. By letter dated 13 February 2013, the Commission notified Hungary that it had all the information it considered necessary for appraisal of the request.

Hungary requests to be authorised to apply the reverse charge mechanism in relation to a number of agricultural goods, mainly those produced and supplied in the pig-farming and animal fodder industry. The particular goods covered by the Hungarian request are listed in detail below under point (3).

Hungary was most recently given the authorisation to apply the reverse charge mechanism to supplies of certain cereals and oilseeds¹.

This derogation was granted by the Council under very specific circumstances, under which Hungary committed itself to implement, during the application period of the said derogation, appropriate and effective control measures and reporting obligations which would make it possible to revert to the normal system after this transitional period of time. Hungary is obliged to notify the Commission of the introduction of those measures and obligations. Hungary has not yet fulfilled this obligation.

This approach was notably justified by the risk of fraud moving to other Member States in a sector whose economic importance is quite substantial in several Member States.

It should be recalled that during recent Council negotiations of similar types of derogation, a number of Member States have expressed their concern, stressing that any derogation from the system of fractionated payment cannot be more than a last resort and an emergency measure in proven cases of fraud, and must offer guarantees as to the necessity and exceptional nature of the derogation granted, the duration of the measure and the specific nature of the products concerned. Moreover, those Member States have pointed out that the reverse charge mechanism always entails a risk of the fraud being transferred to other Member States and recalled that the

¹ Council Implementing Decision 2012/624/EU of 4 October 2012 authorising Hungary to introduce a special measure derogating from Article 193 of Directive 2006/112/EC on the common system of value added tax (OJ L 274, 9.10.2012, p. 26)

reverse charge procedure shall not be used systematically to make up for inadequate surveillance by a Member State's tax authorities.

Hungary confirmed its acceptance of these conditions. This engagement was in particular mentioned in the first recital of the Council Implementing Decision 2012/624/EU of 4 October 2012 where it is stated that Hungary "has said that it will not seek renewal of this authorisation".

2. REVERSE CHARGE

The person liable for the payment of VAT pursuant to Article 193 of the VAT Directive is the taxable person supplying the goods or services. The purpose of the reverse charge mechanism is to shift that liability onto the taxable person to whom the supplies are made.

Missing trader fraud occurs when traders evade paying VAT to the tax authorities after selling their products. Their customers, however, are entitled to a tax deduction as they are in possession of a valid invoice. In the most aggressive cases of such tax evasion the same goods or services are, via a "carousel" scheme (which involves the goods or services being traded between Member States) supplied several times without payment of VAT to the tax authorities. By designating the person to whom the goods or services are supplied as the person liable for the payment of VAT in such cases, the reverse charge mechanism has particularly been found to eliminate the opportunity to engage in that form of tax evasion.

3. THE REQUEST

Hungary requests, under Article 395 of the VAT Directive, that the Council, acting upon a proposal of the Commission, authorises Hungary to apply a special measure derogating from Article 193 of the VAT Directive as regards the application of the reverse charge mechanism in relation to supplies of the following goods:

CN Code ²	Description
0103 1000	Pure-bred breeding live swine
0103 9110	Domestic species of live swine weighting less than 50 kg
0103 9211	Sows having farrowed at least once, of a weight of not less than 160 kg, weighting 50 kg or more
0103 9219	Other domestic species of live swine weighting 50 kg or more
0203 1110	Fresh or chilled carcasses and half-carcasses of domestic swine
0203 2110	Frozen carcasses and half-carcasses of domestic swine
1103	Cereal groats, meal and pellets
2302	Bran, sharps and other residues, whether or not in the form of pellets, derived from the sifting, milling or other working of cereals or of leguminous plants
2304	Oilcake and other solid residues, whether or not ground or in the form of pellets, resulting from the extraction of soya-bean oil
2306	Oilcake and other solid residues, whether or not ground or in the form of pellets, resulting from the extraction of vegetable fats or oils, other than those of heading 2304 or 2305
2309 90	Preparations of a kind used in animal feeding, other than dog or cat food put up for retail sale

²

Combined nomenclature code established by Regulation (EEC) No 2658/87

The current request has to be seen against the background of the derogation that was most recently granted to Hungary, pursuant to which it is already authorised to apply the reverse charge mechanism to supplies of certain cereals and oilseeds³.

The applicability of that derogation is limited in time for a period of 2 years. Moreover, Hungary has committed itself to introduce appropriate and effective control measures and reporting obligations with respect to taxable persons that supply goods to which that special measure applies and to notify the Commission of the introduction of the corresponding measures and obligations.

Hungary has informed the Commission that it has observed a number of fraudulent activities with respect to supplies of the goods listed in the table above which have resulted in high amounts of unpaid VAT. According to the information supplied by Hungary, the detection of those cases of VAT fraud is also a result of a significant increase of the number of tax inspections carried out in Hungary.

Hungary is however of the opinion that those inspections are usually highly time-consuming and therefore seeks authorisation to establish that the transactions in question shall be subject to the reverse charge mechanism in order to prevent VAT fraud.

4. THE COMMISSION'S VIEW

When the Commission receives requests in accordance with Article 395 of the VAT Directive, these are examined to ensure that the basic conditions for their granting are fulfilled, i.e. whether the proposed specific measure simplifies procedures for taxable persons and/or the tax administration or whether the proposal prevents certain types of tax evasion or avoidance. In this context, the Commission has always taken a limited, cautious approach to ensure that derogations do not undermine the operation of the general VAT system, are limited in scope, necessary and proportionate.

In the first place, it is the Commission's view that the type of the various goods in question – as listed above in detail – are of a nature which should make auditing possible through conventional control means without the need to implement the reverse charge mechanism. The derogation recently granted to Hungary concerning cereals and oilseeds⁴ was granted in exceptional circumstances in order to give time to Hungary to implement certain reforms to combat the fraud.

Secondly, the measure concerning cereals and oilseeds was never intended to be a long term solution or to compensate for inadequate surveillance of taxable persons in these extremely valuable markets. The derogation was justified as part of a package of measures to be undertaken by Hungary while, at the same time, being restricted to a limited period in time. The very same conditions were included in the derogation granted to Romania⁵.

Hungary has not yet notified the Commission of the introduction of the appropriate and effective control measures and reporting obligations concerning the supplies of the goods covered by the derogation recently granted. Given the strictly limited

³ See footnote (1)

⁴ See footnote (1)

⁵ Council Implementing Decision 2011/363/EU of 20 June 2011 authorising Romania to introduce a special measure derogating from Article 193 of Directive 2006/112/EC on the common system of value added tax (OJ L 163, 23.6.2011, p. 26)

nature of that derogation, the Commission takes the view that – at this stage – it is not justified to extend the list of goods subject to the reverse charge mechanism to a considerable extent as now requested by Hungary. Applying the reverse charge mechanism to the long list of goods as requested by Hungary in addition to the list of goods already authorised would result in a situation where a considerably high number of supplies made in the agricultural sector would fall out of the normal VAT rules. The Commission has reason to doubt that such a global approach could still be regarded as a “special measure” within the meaning of Article 395 of the VAT Directive.

Moreover, the detailed information submitted by Hungary together with the request for derogation shows that Hungary has already successfully started taking the necessary steps to effectively counteract the observed fraudulent activities in the sectors involved. The statistics Hungary has shared with the Commission underline that in 2012 Hungary had almost doubled the number of tax inspections carried out in comparison to 2011 and had also managed to increase the effectiveness of the inspections performed in the most affected sectors in terms of the detection of fraudulently unpaid VAT. The Commission acknowledges the efforts taken and encourages Hungary to carry on with those measures which the Commission thinks are appropriate in terms of preventing the observed cases of VAT fraud.

The Commission also considers that the so-called conventional measures designed to tackle Carrousel fraud should first be fully implemented. Against this background, it stands ready to assist Hungary in fully implementing such measures. Given this situation, the Commission takes the view that the introduction of a further transitional measure based on Article 395 of the VAT Directive to allow for the application of the reverse charge mechanism is not the right approach.

Also, the reverse charge mechanism could have in this sector an adverse impact on fraud at the retail level. Contrary to cereals where transformation is almost always done at an industrial stage, the transformation of carcasses of animals into meat is also often carried out in the same place as where it is sold to private consumers. The risk of transferring the whole VAT liability to the last chain is therefore much higher.

Lastly, indications are that fraud in these sectors has shifted to, in particular, other Member States in South–East Europe. Against this background, applying the reverse charge to an extended number of goods in the agricultural sectors concerned would represent a fraud risk for those Member States, a risk which cannot be underestimated given the importance of these sectors in the region.

5. CONCLUSION

On the basis of above-mentioned elements, the Commission objects to the request made by Hungary.