

Manuscript

PRINCIPLE OF PROPORTIONALITY AND THE PREVENTION OF EVASION,
AVOIDANCE OR ABUSE

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HARM 53 Master Thesis - European and International Tax Law - Indirect Taxation

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TABLE OF CONTENTS

Abbreviations	3
1. Introduction	4
1.1 Background.....	4
1.2 Purpose, problem and hypothesis	4
1.3 Questions	5
1.4 Method and material	5
1.5 Limitation	5
1.6 Outline	5
2. Principle of proportionality	6
2.1 Introduction	6
2.2 Principle of proportionality in general.....	7
2.3 Principle of proportionality in VAT	7
2.4 Framework proportionality in VAT	8
2.4.1 Evasion, avoidance or abuse	8
2.4.2 Fundamental principles and objectives of the common system of VAT	9
2.5 Conclusion	9
3. Powers of Member States to prevent evasion, avoidance or abuse based on the jurisprudence of the Court of Justice.....	10
3.1 Introduction	10
3.2 Power to deny the exemption for the intra-Union supply of goods.....	10
3.2.1 Transport Service NV	10
3.2.2 R.....	11
3.3 Power to deny the right of deduction of input VAT.....	12
3.3.1 Sudholz	12
3.3.2 Kittel and Recolta Recycling	12
3.4 Power to deny national legislation aimed at simplifying VAT declarations and payments.....	13
3.5 Power to adjust the taxable amount.....	14
3.6 Power to require the issuing of a corrected invoice and repayment of VAT to the beneficiary	14
3.7 Power to request security of payment of VAT	15
3.8 Conclusion	15
4. Commission's coordinated strategy to fight tax fraud	17
4.1 Introduction	17
4.2 Directive 2008/117/EC and Regulation No 37/2009.....	17
4.3 Directive 2009/69/EC	18
4.4 Directive 2010/23/EU	18
4.5 Directive 2010/24/EU and Regulation (EU) No 904/2010	18
4.6 Directive 2010/45/EU.....	19
4.7 Other proposed or discussed measures to fight tax fraud.....	19
4.7.1 Valid invoice to exercise right of deduction	19
4.7.2 Joint and several liability	19
4.8 Conclusion.....	20

5. Proportionality of the powers of Member States to prevent evasion, avoidance or abuse...	21
5.1 Introduction	21
5.2 Transport Service NV	21
5.3 R.....	22
5.4 Sudholz	23
5.5 Kittel	24
5.6 Ampliscientifica and Amplifin	25
5.7 Direct Cosmetics.....	25
5.8 Stadeco.....	26
5.9 Federation of Technological Industries and Others.....	26
5.10 Frequency of recapitulative statements	27
5.11 Exemption of intra-Union supply linked with importation	27
5.12 Reverse charge for certain domestic supplies.....	27
5.13 Other proposed measures to fight tax fraud.....	28
5.13.1 Valid invoice to exercise right of deduction in case of reverse charge procedure.....	28
5.13.2 Joint and several liability	28
5.13.2.1 Proposal of 1 December 2008	29
5.13.2.2 Presidency proposal of 6 May 2009	29
5.14 Conclusion	30
6. Conclusion.....	31
List of literature	33
List of cases	36
List of opinions.....	38
Appendix	39

ABBREVIATIONS

CoJ, Court, Court of Justice	Court of Justice of the European Union
COM	Communication
Commission	European Commission
ECR	European Court Reports
P.	Page
Par.	Paragraph
Sixth Directive	Council Directive 77/388/EC
SME	Small and Medium sized Enterprise
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
VAT	Value Added Tax
VAT Directive, Directive	Council Directive 2006/112/EC

1. INTRODUCTION

1.1 Background

VAT fraud exists in different forms, ranging from the black economy to internal fraud and carousel fraud if intra-Union transactions are involved. It affects the financial interest of both the Member State in question and the European Union within the meaning of Article 325 TFEU.¹ Both Member States and the Commission take measures to prevent the potential tax evasion or avoidance and abuse of law. Recently, the Court of Justice decided in *R*² about a measure taken by Germany in a case considering VAT fraud.

On 7 December 2010 the Court of Justice delivered its judgement. The Court ruled that the Member State of departure of the intra-Union supply, may, although an intra-Union supply of goods has actually taken place, pursuant to its powers under the first part of the sentence in Article 28c(A) of the Sixth Directive³ (now: Article 131 of the VAT Directive⁴) refuse to allow an exemption of a transaction in case the supplier concealed the identity of the true purchaser in order to enable the latter to evade payment of VAT. However, comparison of the judgement of the Court and the Opinion⁵ of Advocate General Cruz Villalón raises the question whether this judgement is in conformity with the principle of proportionality. Are there any other judgements that raise the similar question?

Moreover, on 31 May 2006 the Commission presented a Communication⁶ concerning the need to develop a coordinated strategy to improve the fight against fiscal fraud. Because of the absence of political agreement on more far reaching measures, the Commission presented a Communication⁷ on 1 December 2008 with more conventional measures to fight against VAT fraud. Besides that, the Commission presented on the same date a Proposal for a Council Directive⁸ amending Directive 2006/112/EC by introducing, among other things joint and several liability for the supplier performing an intra-Union supply. However, the legislative resolution of the European Parliament calling the Commission to alter its proposal on joint and several liability questions the proportionality of the proposed and adopted measures.⁹

1.2 Purpose, problem and hypothesis

The purpose of my research is to analyse what powers Member States have to prevent evasion, avoidance or abuse, based on jurisprudence of the Court of Justice and the proposed measures by the Commission to fight tax fraud and whether these powers are in conformity with the principle of proportionality. In my opinion these powers are, after the recent judgement in *R*, disproportional to the objectives pursued. Therefore, the hypothesis for the thesis is:

The powers of Member States in connection with the prevention of potential evasion, avoidance or abuse are disproportional.

¹ COM (2006) 254 final, p. 4

² Case C-285/09, Criminal proceedings against R

³ Sixth Council Directive of 17 May 1977

⁴ Council Directive 2006/112/EC of 28 November 2006

⁵ Opinion of Advocate General Cruz Villalón, Case C-285/09, Criminal proceedings against R, par. 104-108

⁶ COM (2006) 254 final

⁷ COM (2008) 807 final

⁸ COM (2008) 805 final

⁹ European Parliament legislative resolution of 24 April 2009 on the proposal for a Council directive amending Directive 2006/112/EC

1.3 Questions

In order to find an answer to this problem, the questions of the thesis are:

1. What is the principle of proportionality?
2. Which powers do Member States derive from the jurisprudence of the Court of Justice and the measures proposed by the Commission and adopted by the Council to prevent potential evasion, avoidance or abuse?
3. Are these powers in conformity with the principle of proportionality?

1.4 Method and material

The method and material used to answer these questions are by analysis of jurisprudence of the Court of Justice, the documentation on the proposed measures by the Commission, the adopted Directives and Regulations by the Council and legal writing.

1.5 Limitation

This thesis is limited to the proportionality of measures taken by Member States to prevent potential evasion, avoidance or abuse in European VAT. Due to the absence of harmonisation of European Union legislation in the field of sanctions the question of proportionality of sanctions falls outside the scope of this thesis.¹⁰ Furthermore, only the proposed measures by the Commission and adopted measures by the Council to fight against tax fraud are considered for evaluation. Therefore, Council Decisions granting Member States to impose measures to prevent evasion or avoidance are outside the scope, except in case the Court of Justice ruled about it.

1.6 Outline

In the next chapter the principle of proportionality in general and its application to VAT is elaborated. Chapter 3 consists the jurisprudence in which the Court of Justice decided that particular measures taken by Member States to prevent potential evasion, avoidance or abuse are proportional. In other words: the powers of Member States to prevent evasion, avoidance or abuse according to the Court of Justice. The measures proposed by the Commission and adopted by the Council to fight tax fraud are described in chapter 4. Finally, in chapter 5 the question is answered whether these powers are proportional. Chapter 6 contains the conclusion.

¹⁰ Case C-188/09, Profaktor Kulesza, Frankowski, Józwiak, Orłowski, par. 29

2. PRINCIPLE OF PROPORTIONALITY

2.1 Introduction

"The principle of proportionality has been developed by the Court of Justice of the European Union deriving from the rule of law and requires in particular that the individual should not have his freedom of action limited beyond the degree necessary in the public interest."¹¹ It appeared for the first time in a judgement of the Court in *Fédéchar*.¹² However, it was not until the judgement in *Internationale Handelsgesellschaft*¹³ that proportionality was expressly relied on by the Court.¹⁴ Since the Treaty of Amsterdam of 1997 the principle is incorporated in the Treaty on European Union.¹⁵

The principle of proportionality is enshrined in Article 5 TEU:

"1.The limits of Union competences are governed by the principle of conferral. The use of Union competences is governed by the principles of subsidiarity and proportionality.

2.Under the principle of conferral, the Union shall act only within the limits of the competences conferred upon it by the Member States in the Treaties to attain the objectives set out therein. Competences not conferred upon the Union in the Treaties remain with the Member States.

3.Under the principle of subsidiarity, in areas which do not fall within its exclusive competence, the Union shall act only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States, either at central level or at regional and local level, but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level.

The institutions of the Union shall apply the principle of subsidiarity as laid down in the Protocol on the application of the principles of subsidiarity and proportionality. National Parliaments ensure compliance with the principle of subsidiarity in accordance with the procedure set out in that Protocol.

4.Under the principle of proportionality, the content and form of Union action shall not exceed what is necessary to achieve the objectives of the Treaties.

The institutions of the Union shall apply the principle of proportionality as laid down in the Protocol on the application of the principles of subsidiarity and proportionality."

The principle of proportionality is applicable to Union measures (both determining the competence or legislative capacity of the Union and the legitimacy of the burdens imposed on those subject to Union law) and to national measures of Member States when they act in the scope of Union law.¹⁶ In *Garage Molenheide*¹⁷ the Court held that the principle of

¹¹ Tridimas, T., *The General Principles of EC Law*, p. 136

¹² Case 8/55, *Fédération charbonnière de Belgique v ECSC High Authority*, p. 299

¹³ Case 11/70, *Internationale Handelsgesellschaft mbH / Einfuhr- und Vorratsstelle für Getreide und Futtermittel*, par. 2

¹⁴ Tridimas, T., *op.cit.*, p. 141

¹⁵ Usher, J.A., *General Principles of EC Law*, p. 37 - 40

¹⁶ *Ibid.*, p. 37

proportionality is applicable to national measures which are adopted by Member States in the exercise of its powers relating to VAT. Moreover, from *FTI*¹⁸ it follows that Member States must comply with the general principles, such as the principle of proportionality, which form part of the Union legal order when they exercise the powers conferred on them by Union directives. The principle of proportionality therefore also applies to measures taken by Member States to prevent evasion, avoidance or abuse in the sphere of VAT.¹⁹ In the next paragraph the general application of the principle of proportionality by the Court is described. Paragraph 2.3 outlines the application of the principle of proportionality in VAT. In paragraph 2.4 the framework of the principle of proportionality in VAT is developed. Paragraph 2.5 contains the conclusion.

2.2 Principle of proportionality in general

"The principle of proportionality requires that action undertaken must be proportionate to its objectives."²⁰ It is based on the concern to protect individuals against the State and on the assumption that regulatory intervention must be suitable to achieve its aims.²¹ The measure in question must be appropriate and necessary to achieve its objectives. Therefore, the principle of proportionality can be divided into two tests: a test of suitability and a test of necessity. The former referring to the relationship between means and the end. In other words: the means must be suitable to achieve its objectives. The latter is a test of weighting competing interests.²² "The essential characteristic of the principle is that the Court performs a balancing exercise between the objectives pursued by the measure in issue and its adverse effects on individual freedom."²³

In the literature it is even suggested that the principle of proportionality entails a three-part test.²⁴ At first, the test of suitability. The second test is the least restrictive alternative test. Following this test it is established whether there are other less restrictive means available to come to a comparable result. In case there is no less restrictive measure, it must be decided whether the measure does not have an excessive effect on the applicant's interest. This is known as proportionality *stricto sensu*. However, in practice the Court does not distinguish between the second and third test.²⁵

Another issue that arises is whether the principle of proportionality should be applied by the Court of Justice or the national courts. This depends on the situation. When the Court is in possession of the necessary facts and has the necessary technical expertise it may be preferable for the Court to make the ultimate assessment itself.²⁶

2.3 Principle of proportionality in VAT

In *Gemeente Leusden and Holin Groep*²⁷ the Court stipulated that from the wording of the Directive it follows that the prevention of possible tax evasion, avoidance and abuse is an

¹⁷ Case C-286/94, *Garage Molenheide and others v Belgische Staat*, par. 48

¹⁸ Case C-384/04, *Federation of Technological Industries and others*, par. 29

¹⁹ See also: Craig, P., *EU Administrative Law*, p. 701

²⁰ Tridimas, T., *op.cit.*, p. 136

²¹ Schwarze, J., *European Administrative Law*, p. 679

²² Tridimas, T., *op.cit.*, p. 139

²³ *Ibid.*, p. 139

²⁴ Burca, de G., *The Principle of Proportionality and its application in EC Law*, p. 113

²⁵ Tridimas, T., *op.cit.*, p. 139

²⁶ Jacobs, F.G., *Recent Developments in the Principle of Proportionality in EC Law*, p. 19, 20

²⁷ CoJ judgement of 29 April 2004, C-487/01, *Gemeente Leusden and Holin Groep*, [2004], ECR p. I-5337, par. 76

objective recognised and encouraged by the Directive. Moreover, it follows from *Garage Molenheide* that preservation of the rights of the Treasury is a legitimate reason for the measures adopted by the Member States. However, in the same case the Court stated that if the measures go further than necessary in order to attain their objective, the principles of the common system of VAT would be undermined. In the present case the right of deduction of input VAT. Member States must, in accordance with the principle of proportionality, employ means which are the least detrimental to the objectives and the principles laid down by the relevant Union legislation. In order for national measures to comply with the principle of proportionality, it must both be ascertained whether the means employed are suitable and whether those means do not go beyond what is necessary to attain the objectives of the rules.²⁸

Therefore, the principle of proportionality in VAT requires an acceptable balance between the detriment of fundamental principles and objectives of the common system of VAT and the power of Member States to prevent potential evasion, avoidance or abuse. In the next chapter the cases are described in which this balance is found to be proportional according to the jurisprudence of the Court of Justice. In the next paragraph the framework for the application of this definition is elaborated.

2.4 Framework proportionality in VAT

The aforementioned definition of the principle of proportionality in VAT consists of two elements. In this paragraph these elements are shortly reviewed. A thorough elaboration of these concepts falls outside the scope of this thesis. First of all, the measure must be aimed at the prevention of potential evasion, avoidance or abuse. In other words: there must be a situation of evasion, avoidance or abuse. This is described in paragraph 2.4.1. Secondly, the detriment of fundamental principles and objectives must be proportional to the measure. In paragraph 2.4.2 the fundamental principles and objectives of the common system of VAT are described.

2.4.1 Evasion, avoidance or abuse

From *Halifax*²⁹ it follows that an abusive practice can only be found to exist if:

- "first, the transactions concerned, notwithstanding formal application of the conditions laid down by the relevant provisions of the Sixth Directive and the national legislation transposing it, **result in the accrual of a tax advantage** the grant of which would be **contrary to the purpose of those provisions**.
- Second, it must also be apparent from a number of **objective factors** that the **essential aim of the transactions concerned is to obtain a tax advantage.**" [emphasises added BM]

The principle of prohibiting the abuse of rights intends to ensure that Union legislation is not extended to cover practices carried out not in the context of normal commercial operations, but solely for the purpose of wrongfully obtaining advantages. It prohibits wholly artificial arrangements which do not reflect economic reality and are set up with the sole aim of

²⁸ Case C-205/07, *Gysbrechts and Santurel Inter*, par. 51

²⁹ Case C-255/02, *Halifax and Others*, par. 74, 75

obtaining a tax advantage.³⁰ Regarding the difference between evasion and avoidance, the Court stipulates in *Direct Cosmetics Ltd*³¹ that intention, which constitutes an essential element of evasion, is not required as a condition for the existence of avoidance. In *Emsland-Stärke*³² the Court held that a finding of abuse must not lead to a penalty, but rather to an obligation to repay. Furthermore, it follows from *Halifax* that transactions involved in an abusive practice must be redefined so as to re-establish the situation that would have prevailed in the absence of the abusive practice.

2.4.2 Fundamental principles and objectives of the common system of VAT

In VAT cases the Court has referred to numerous principles, for example: the principle of legal certainty,³³ the right to deduction,³⁴ free movement of goods,³⁵ the prohibition of double taxation³⁶ and the prohibition of the accumulation of tax.^{37,38} Moreover, in many of its judgements the Court of Justice referred to Article 1(2) of the Directive which lays down the principle of neutrality:³⁹

"The principle of the common system of VAT entails the application to goods and services of a general tax on consumption exactly proportional to the price of the goods and services, however many transactions take place in the production and distribution process before the stage at which the tax is charged.

On each transaction, VAT, calculated on the price of the goods or services at the rate applicable to such goods or services, shall be chargeable after deduction of the amount of VAT borne directly by the various cost components. The common system of VAT shall be applied up to and including the retail trade stage."

In its judgements the Court has recognised many more principles. These principles are, if applicable used to analyse the powers of Member States to prevent evasion, avoidance or abuse in chapter 5.

2.5 Conclusion

The principle of proportionality is enshrined in Article 5 TEU and is also applicable in the sphere of VAT. It requires an acceptable balance between the detriment of fundamental principles and objectives of the common system of VAT and the power of Member States to prevent potential evasion, avoidance or abuse.

³⁰ Case C-196/04, *Cadbury Schweppes and Cadbury Schweppes Overseas*, par. 55

³¹ Joined cases 138/86 and 139/86, *Direct Cosmetics Ltd / Commissioners of Customs and Excise*, par. 22

³² Case C-110/99, *Emsland-Stärke*, par. 56

³³ Case 326/85, *Netherlands v Commission*

³⁴ Case C-286/94, *Garage Molenheide and others v Belgische Staat*, par. 48

³⁵ Case C-409/04, *Teleos and others*, par. 64

³⁶ Case C-155/01, *Cookies World*, par. 60

³⁷ Terra, B., Kajus, J., *A Guide to the European VAT Directives 2010*, p. 64

³⁸ *Ibid.* p. 35, footnote 37

³⁹ *Ibid.* p. 63

3. POWERS OF MEMBER STATES TO PREVENT EVASION, AVOIDANCE OR ABUSE BASED ON THE JURISPRUDENCE OF THE COURT OF JUSTICE

3.1 Introduction

In this chapter the powers of Member States in connection with the prevention of potential evasion, avoidance or abuse based on jurisprudence of the Court of Justice are described. In other words: which measures taken by Member States to prevent evasion, avoidance or abuse are proportional according to the Court. These powers are described in paragraph 3.2 to 3.7. Paragraph 3.8 contains the conclusion.

3.2 Power to deny the exemption for the intra-Union supply of goods

Title IX of the Directive stipulates the exemptions. According to Article 138 Member States shall exempt the supply of goods dispatched or transported to another Member State. It follows from Article 131 that Member States shall lay down conditions for the purpose of preventing any possible evasion, avoidance or abuse. The first case to be mentioned in this context is *Transport Service NV*.⁴⁰

3.2.1 Transport Service NV

Transport Service NV (hereinafter Transport) sold two vehicles to Mr Schellinck residing in Luxembourg. However, doubts arose whether the cars were really delivered to Luxembourg. The Belgian State submitted to the Court of First Instance of Belgium that the supply of cars did not take place between Transport and the customer in Luxembourg, but between Transport and another Belgium company, Bea Cars, and the exemption was therefore not applicable. Furthermore it stated that Transport was liable to pay VAT on its supplies. However, Bea Cars had paid in the VAT to the Belgian State on the sale of the cars. The Rechtbank van eerste aanleg te Antwerpen referred the following question for a preliminary ruling:

"Does the principle of the neutrality of value added tax preclude a Member State from claiming additional VAT from a taxable person which has issued an invoice, correctly or otherwise, in accordance with the VAT exemption applicable to intra-Community supplies (Article 39(a) of the Belgian VAT Code) where it is evident that the VAT has been paid by the end user and transferred to the Member State by the person who drew up the invoice issued to that end user?"

First of all, the Court recognised that Union law does not prevent Member States from treating the issuing of irregular invoices as attempted tax evasion. It is for the national court to decide whether the supply of the cars meets the conditions of an intra-Union supply of goods or not. If not, the principle of the common system of VAT consists that VAT applies to each transaction of the production or distribution stage and the supply is subject to VAT under Article 2(1)(a) of the Directive. Member States must lay down the conditions under which the tax authorities may recover VAT, however it must be in accordance with Article 273 of the Directive. Therefore, the Court answered that a Member State is not precluded from recovering VAT from a taxable person which has wrongly invoiced the supply of goods as

⁴⁰ Order in case C-395/02, *Transport Service*

exempt. It is irrelevant, whether the VAT on the later sale of the goods is paid in to the public purse or not.

Thus, according to this ruling, Member States can deny the exemption of an intra-Union supply and recover the VAT from the taxable person if the requirements for an intra-Union supply of goods are not fulfilled, even though the Member State did not suffer a tax loss. The next case is *R*,⁴¹ in which the Court deals with a situation in which the requirements for an intra-Union supply of goods were fulfilled, but the supplier knew he was participating in a transaction aimed at evading VAT.

3.2.2 R

On 7 December 2010 the Court of Justice delivered its judgement in *R*. Mr R, a Portuguese national, was the manager of a German company engaged in luxury car trade. The buyers were, for the most part, established in Portugal. From 2002 Mr R carried out series of manipulations to evade payment of VAT in Portugal using fictitious purchasers who appeared as recipients of the supplies. The real purchasers sold the cars without declaring that there had been a prior intra-Union acquisition and without paying VAT in respect of this acquisition. Mr R referred these transactions as intra-Union supplies in his statements to the tax authorities. The Supreme Court of Germany referred the question to the Court whether a supply of goods in the meaning of Article 28c(A)(a) of the Sixth Directive (now Article 138) is to be refused exemption from VAT when the supplier knew that he was participating in a transaction aimed at evading VAT by his supply or in case he took actions aimed to enable the receiver or a third person evade VAT.

The Court reiterated that the exemption of the intra-Union supply of goods only becomes applicable when the right to dispose of the goods as owner has been transferred to the purchaser and the goods have physically left the territory of the Member State of supply. Due to the abolition of border controls between Member States it has been difficult for the authorities to check whether this requirement is fulfilled. Therefore, the evidence provided by the taxable persons and their statements are the basis to carry out the necessary checks. However, there are no provisions in the Directive specifically laying down the evidence required and it falls therefore under the competence of the Member States. The presentation of false invoices, declarations or any other manipulation of evidence prevents the correct collection of tax and compromises the functioning of the common system of VAT.

It follows that in circumstances at issue in this case the Member State of supply may refuse to apply the exemption. Moreover, it is required to refuse to grant the exemption and require the supplier to pay the tax subsequently in order to ensure the transaction in question does not escape taxation altogether. The principle of proportionality does not preclude a supplier who participates in tax evasion from being obliged to pay the VAT on his intra-Union supply.

This case differs from the previous case. Member States can deny the exemption and require the supplier to pay the tax even though the goods have actually physically left the Member State of supply, because the supplier concealed the identity of the true purchaser, enabling the latter to evade payment of VAT. Does the Court's judgement make the knowledge test, developed in *Kittel and Recolta Recycling* (see paragraph 3.3.2) applicable to exemptions for

⁴¹ Case C-285/09, Criminal proceedings against R

intra-Union supplies? According to the Green Paper⁴² presented by the Commission, the knowledge test can be applied to exemptions. However, according to the Opinion of Advocate General Cruz Villalón it does not seem appropriate to apply, by analogy, the knowledge test to the exemption for an intra-Union supply.

3.3 Power to deny the right of deduction of input VAT

The right to deduct input VAT is stipulated in Title X of the Directive. In *Sudholz*⁴³ the Court ruled about a measure introduced by Germany which limited the right to deduction to 50% in particular circumstances.

3.3.1 Sudholz

On 28 February 2000, the Council authorised Germany, by adopting Decision 2000/186⁴⁴ to derogate from Articles 6 and 17 of the Sixth Directive. By this Decision Germany was allowed to limit to 50% the right to deduct of the VAT charged on expenditure on vehicles not used exclusively for business purposes and not to treat as supplies of services for consideration the use for private purposes of vehicles belonging to a taxable person's business. The derogating measure was aimed both at preventing evasion or abuse and to simplify the system of taxation.

First, it needed to be determined whether the flat-rate limit was valid. The Court stipulated that due to the difficulty to verify the exact use of the vehicle, proving the precise use and the discovery of irregularities in almost all the cases where verification is carried out the imposition of a flat limitation would limit the risk of tax evasion or avoidance and simplify the system of charging VAT. Secondly, the Court had to decide whether the limit of 50% is proportionate to the objective pursued. Following the fact that, 50% is considered to be the average use, other Member States, as well as the Commission in a proposal for Directive 77/388, apply the same limit suggests that such a limit is reasonable. Notwithstanding, those persons that intend to use their vehicle for more than 50% cannot deduct the corresponding proportion of VAT. This is inherent in the measure for simplification. The derogating measure does therefore not infringe the principle of proportionality.

In *Kittel and Recolta Recycling*⁴⁵ the Court had to decide whether a rule of national law which causes the taxable person to lose the right to deduct input VAT is precluded under the Sixth Directive.

3.3.2 Kittel and Recolta Recycling

Both Computime, represented by its receiver Kittel, and Recolta were recipients of a supply of goods that was part of a fraud committed by the seller. Under Belgian law the contract of sale was void and as a consequence the Belgian authorities refused the right to deduct input tax. However, both taxable persons did not and could not know that the transaction concerned was part of a fraud committed by the seller.

⁴² COM (2010) 695 final, Green Paper, p. 12

⁴³ Case C-17/01, *Sudholz*

⁴⁴ Council Decision of 28 February 2000

⁴⁵ Joined cases C-439/04 and C-440/04, *Kittel and Recolta Recycling*

The Court stated that traders who take every precaution which could reasonably be required of them to ensure that their transactions are not connected with fraud, must be able to rely on the legality of those transactions without losing the right to deduct input VAT. On the other hand, if a taxable person knew or should have known that he was taking part in a transaction connected with fraud, it must be regarded as a participant of that fraud, irrespective whether he profited by the resale of those goods or not. This is known as the knowledge test. The authorities can refuse entitlement to the right to deduct input VAT where it is ascertained that the taxable person knew or should have known that, by his purchase he was participating in VAT fraud even though the transaction meets the objective criteria.

3.4 Power to deny national legislation aimed at simplifying VAT declarations and payments

On the basis of Article 395 of the Directive (Article 27(1) of the Sixth Directive) the Council may authorise Member States to introduce special measures derogating from the provisions of the Directive in order to simplify the procedure for charging tax or to prevent certain types of tax evasion or avoidance. In *Ampliscientifica and Amplifin*⁴⁶ the Court of Justice ruled about a simplification measure introduced by Italy.

This case concerns tax declarations submitted by Ampliscientifica for 1990 and by Amplifin for 1990 and 1991, both companies incorporated under Italian law and part of the Amplifon group. More than 50% of the share capital of Amplifon, which was formed in February 1989, was subscribed by Amplaid SpA, 99% of which in turn was controlled by Amplifin. For the 1990 tax year, Amplifin submitted a declaration to apply the simplified procedures under the 1979 Decree, which enables the parent company to act, to a certain extent, on behalf of its subsidiary company or companies. However, the tax authorities took the view that Amplifin was not entitled to submit the declarations, because for the simplification procedures to be applicable the subsidiary must have existed from the beginning of the calendar year of the year before the declaration was made (in this case the beginning of 1989). Among other things the Corte Suprema di Cassazione referred the following question:

"... is the imposition of a temporal restriction – in the sense that the link must have existed for a significant period of time – as a precondition for the application of the scheme, where the persons concerned are not permitted to demonstrate that there is a valid economic reason for the link being forged, disproportionate in relation to the objectives of the directive and to the need for compliance with the principle prohibiting the abuse of rights? (ii) Is that legislation to be regarded in any event as contrary to the principle of the neutrality of VAT?"

Regarding the proportionality of the time-limit laid down in national legislation the Court stipulated that a time-limit between one and two years in order for taxpayers to make use of the simplified procedures is proportional in the light of the objective of combating tax evasion and bogus legal arrangements. Moreover, if no time-limit would have been imposed such national legislation is likely to encourage abuse and evasion, which is contrary to one of the objectives pursued by Union law. Thus, Member States are allowed to impose certain time-limits in order to prevent potential evasion, avoidance or abuse. In my opinion this judgement can be interpreted more broadly in the meaning that Member States are allowed to limit the

⁴⁶ Case C-162/07, *Ampliscientifica and Amplifin*

applicability of certain special schemes to specific situations when in the absence of this limitation it is likely to encourage avoidance and abuse.

3.5 Power to adjust the taxable amount

In *Direct Cosmetics Ltd*⁴⁷ the Court considered the power to adjust the taxable amount. Direct Cosmetics Limited and Laughtons Photographs Limited both applied sales schemes with the result that the final taxable base for the purposes of VAT is not the final value of the sale to the consumer. Therefore no VAT is paid on the difference between the final price and price previously charged. The United Kingdom applied a derogating measure for which it received authorisation on the basis of Article 27 of the Sixth Directive. On the basis of this derogation the authorities were allowed to adjust the taxable amount to the open market value on a sale by retail.

The Court pointed out that the objective of the measures is to prevent a systematic loss of tax revenue, resulting from the sale scheme applied consistently by undertakings of a certain size. In the light of this objective it cannot be claimed that the measure is disproportionate to the aim. Furthermore, the absence of such a measure would maintain the distortion of competition, which is in disadvantage of undertakings whose sales schemes are structured differently.

3.6 Power to require the issuing of a corrected invoice and repayment of VAT to the beneficiary

In *Stadeco*⁴⁸ the Court ruled about the requirement to issue a corrected invoice in order to receive a refund of VAT imposed by the Dutch tax authorities.

Stadeco is a company established in the Netherlands, which provided its services in Germany and third countries for the Economische Voorlichtingsdienst (hereinafter: EVD), a body governed by public law, established in the Netherlands. The EVD used the services for activities not subject to VAT in the Netherlands and is not, as a public body entitled to deduct that tax. Stadeco invoiced the EVD with Dutch VAT for the services performed in Germany, which was subsequently paid by EVD. In 1996 the authorities informed that Stadeco was not liable to pay VAT in the Netherlands and reimbursed the amount subject to the correction of the invoices. However, Stadeco did not issue any credit notes to EVD and the authorities issued a supplementary tax notice for the reimbursed amount. The Hoge Raad asked the Court whether the principle of neutrality precludes a Member State from making a reimbursement subject to the issuing of a corrected invoice if there is no risk of tax loss for the revenue.

On 18 June 2009 the Court decided case. It stated that the requirement to issue a corrected invoice can in principle ensure the elimination of the risk of loss of tax revenue. In addition, it does not make the reimbursement dependent on the discretion of the authorities. The risk of loss of tax revenue was only eliminated because of the status of the EVD as a public body and the fact that it used the services provided by Stadeco only for activities not subject to VAT in the Netherlands. However, complex circumstances and legal relations can make it difficult for the authorities to find that the right to deduct in such a situation is precluded. In this case, making the refund subject to the requirement that a new invoice is issued does not go further

⁴⁷ Joined cases 138/86 and 139/86, *Direct Cosmetics Ltd / Commissioners of Customs and Excise*

⁴⁸ Case C-566/07, *Stadeco*

than necessary to eliminate all risk of a loss of tax revenue. Moreover, Member States may also make the refund subject to the requirement that incorrectly paid tax is paid by the issuer of the invoice to the beneficiary of the services performed. Union law does not prevent a national legal system, from disallowing payment in case this would lead to unjust enrichment of the recipient.

Member States can make a refund subject to the requirement that the taxable person issues a corrected invoice when complex circumstances and legal relations make it difficult for the authorities to find, in sufficient time, that the risk of a loss of tax revenue is eliminated. Furthermore, it may require the issuer to repay the tax to the beneficiary in order to prevent unjust enrichment.

3.7 Power to request security of payment of VAT

In *Federation of Technological Industries and Others*⁴⁹ the Court was asked to give a preliminary ruling on the compatibility of national legislation that makes the taxable person joint and several liable in case he knew at the time of the supply or had reasonable grounds to suspect that some or all of the VAT payable in respect of that supply, a previous or subsequent supply of goods would go unpaid. Besides that, the legislation gives the authorities the possibility to require a taxable person to provide security for the payment of the VAT which is or could become payable by the taxable person to whom he supplies those goods or services or by whom they are supplied to him.

On 11 May 2006 the Court delivered its judgement. The Court held that while Article 21(3) of the Sixth Directive (now Article 205 of the VAT Directive) allows a Member State to make a person jointly and severally liable if the person knew or had reasonable grounds to suspect the VAT would go unpaid. However, such presumptions may not be formulated in such a way that it is impossible or excessively difficult to prove the contrary. Those presumptions would introduce a system of strict liability, which is going beyond what is necessary to preserve the public exchequer's rights. Member States may within the limits of the general principles of Union law introduce joint and several liability. In that case, if the taxable person is declared joint and several liable it can also be required to provide security for the payment of VAT due.

Thus, in case the system of jointly and severally liability based on Article 205 of the Directive is proportional the taxable person may be required, on the basis of Article 273 of the Directive to provide security for the payment of VAT due.

3.8 Conclusion

From the jurisprudence of the Court of Justice it follows that Member States have the power to deny the exemption of an intra-Union supply and recover the VAT if the requirements for the intra-Union supply are not fulfilled, even though there is no tax loss for the Member State. On the other hand, if the requirements are fulfilled, but the supplier knew he was participating in fraud, the Member State can also deny the exemption and require the supplier to pay the tax. In other words: when the supplier is in bad faith. This also applies to the right of deduction. According to *Kittel and Recolta Recycling*, authorities can refuse entitlement to the

⁴⁹ Case C-384/04, *Federation of Technological Industries and others*

right to deduct input VAT where it is ascertained that the taxable person knew or should have known that, by his purchase he was participating in VAT fraud. This is known as the knowledge test. The Commission states in the Green Paper that, after the judgement in *R*, the knowledge test is also applicable to the exemption for intra-Union supplies. However, according to Advocate General Cruz Villalón it does not seem appropriate to apply this by analogy.

Furthermore, Member States can introduce measures that limit the right of deduction in order to prevent evasion or avoidance when the measure is also aimed at simplifying the system of taxation even if the taxable person's right to deduct input VAT is limited in the absence of evasion or avoidance. Besides that, Member States can impose certain time-limits for special schemes in order to prevent abuse and avoidance, adjust the taxable amount to the open market value in particular circumstances and may require a taxable person that is declared joint and several liable to provide security for the payment of the VAT due.

From *Stadeco* it follows that Member States can make a refund subject to the issue of a corrected invoice and/or the actual repayment of the incorrectly invoiced VAT to the beneficiary in case of unjust enrichment.

4. COMMISSION'S COORDINATED STRATEGY TO FIGHT TAX FRAUD

4.1 Introduction

On 31 May 2006 the Commission presented a Communication⁵⁰ concerning the need to develop a coordinated strategy to improve the fight against fiscal fraud. Because of the absence of political agreement on more far reaching measures, the Commission presented a Communication⁵¹ on 1 December 2008 with more conventional measures to fight against VAT fraud in the European Union. The proposed measures can be grouped into three categories. A first category aims at preventing potential fraudsters from abusing the VAT system, the second one provides tools for the detection of fraud and the third category aims at improving the possibilities for the collection of tax lost as a result of fraud and punishment of fraudsters. Several Directives and Regulations have been proposed by the Commission and adopted by the Council to improve the fight against VAT fraud. The Council adopted the following Directives and Regulations;

- Directive 2008/117/EC⁵² and Regulation No 37/2009⁵³ on 16 December 2008,
- Directive 2009/69/EC⁵⁴ on 25 June 2009,
- Directive 2010/23/EU⁵⁵ on 16 March 2010,
- Directive 2010/24/EU⁵⁶ on 16 March 2010,
- Directive 2010/45/EU⁵⁷ on 13 July 2010 and
- Regulation (EU) No 904/2010⁵⁸ on 7 October 2010.

These Directives and Regulations are described in paragraph 4.2 to 4.6. In paragraph 4.7 other measures proposed by the Commission to fight VAT fraud are elaborated. Paragraph 4.8 contains the conclusion.

4.2 Directive 2008/117/EC and Regulation No 37/2009

One of the causes of tax evasion are the shortcomings of the intra-Union VAT arrangements, and in particular the system for the exchange of information on supplies of goods within the Union. The time that elapses between a transaction and the corresponding exchange of information is an obstacle for the effective use of that information to tackle fraud. Both the amendments of the VAT Directive and Regulation (EC) No 1798/2003⁵⁹ concern measures to strengthen the intra-Union VAT system. The amendments increase the frequency of recapitulative statements of intra-Union transactions and decreases the deadline for exchange of information between tax administrations to one month. Besides that, the requirement to submit a recapitulative statement has already been extended to services by the adoption of by Directive 2008/8/EC⁶⁰ on 12 February 2008.

⁵⁰ COM (2006) 254 final

⁵¹ COM (2008) 807 final

⁵² Council Directive 2008/117/EC of 16 December 2008 amending Directive 2006/112/EC

⁵³ Council Regulation (EC) No 37/2009 of 16 December 2008 amending Regulation (EC) No 1798/2003

⁵⁴ Council Directive 2009 of 25 June 2009 amending Directive 2006/112/EC

⁵⁵ Council Directive 2010/23/EU of 16 March 2010 amending Directive 2006/112/EC

⁵⁶ Council Directive 2010/24/EU of 16 March 2010

⁵⁷ Council Directive 2010/45 EU of 13 July 2010 amending Directive 2006/112/EC

⁵⁸ Council Regulation (EU) No 904/2010 of 7 October 2010

⁵⁹ Council Regulation (EC) No 1798/2003 of October 2003

⁶⁰ Council Directive 2008/8/EC of 12 February 2008 amending Directive 2006/112/EC

4.3 Directive 2009/69/EC

On 1 December 2008 the Commission presented a Communication⁶¹ with a proposal amending Directive 2006/112/EC on the common system of value added tax as regards tax evasion linked to import and other cross-border transactions. In this proposal two amendments are presented. The first one considers the exemption of an intra-Union supply under Article 143 of the Directive and was adopted by Council Directive 2009/69/EC. This is described in this paragraph. Secondly, the Commission presented joint and several liability for the supplier performing an intra-Union supply. This is discussed in paragraph 4.7.2.

This Directive is aimed to fight tax evasion linked with importation. Under Article 143(d) of the Directive the importation of goods that is followed by an intra-Union supply or transfer of the imported goods to a taxable person in another Member State shall be exempted. The abuse of this exemption has been identified as weakness of the rules in detected fraud schemes. Due to the fact that the conditions under which the exemption is granted were laid down by the Member States, divergences were exploited by traders to avoid payment of VAT on importation of goods. In order to prevent this exploitation a minimum set of conditions under which the exemption applies was introduced by Directive 2009/69/EC. As a result a second paragraph has been added to Article 143 per 1 January 2011

Thus, the amendments of the Directive impose more administrative obligations on the taxable person importing the goods from a third country. It provides the Member States with the possibility to deny the exemption of Article 143 if these administrative obligations are not fulfilled.

4.4 Directive 2010/23/EU

On 16 March 2010 the Council adopted Directive 2010/23/EU. The purpose of the Directive is to allow Member States the temporary application of the reverse charge mechanism to domestic supplies in order to combat fraud in relation to trade with emission certificates and to transactions involving certain fraud-sensitive goods. By this Directive Article 199a has been inserted into Directive 2006/112/EC.

4.5 Directive 2010/24/EU and Regulation (EU) No 904/2010

On 18 August 2009 the Commission presented a Communication⁶² for a recast of Council Regulation (EC) No 1798/2003 aiming at giving Member States the means to combat cross-border VAT fraud more effectively. Among other things, it intends to improve the exchange of information between Member States, by defining the cases in which Member States may not refuse a request for information, must exchange information spontaneously and must provide feedback. Directive 2010/24/EU aims at reinforcing and improving the recovery assistance between Member States. Both the recast Regulation (EC) No 1798/2003 and Directive 2010/24/EU do not impose any specific powers for Member States to take measures against taxpayers in order to prevent evasion, avoidance or abuse.

⁶¹ COM (2008) 805 final

⁶² COM (2009) 427 final

4.6 Directive 2010/45/EU

On 28 January 2009 the Commission presented two Communications. One on simplifying, modernising and harmonising the VAT invoicing rules.⁶³ The second contains a Proposal for a Council Directive amending Directive 2006/112/EC with regard to the rules of invoicing.⁶⁴ By Directive 2010/45/EU the Directive was amended regarding the issuance and contents of an invoice, e-invoicing and storage of invoices. Moreover, the amendment complements the amendment by Directive 2008/117/EC on shortening the timeframe for recapitulative statements by amending the rules on the chargeability to tax for intra-Union supplies. Article 222 requires that the invoice shall be issued no later than on the fifteenth day of the month following that in which the chargeable event occurs. This prevents the postponement of the declaration of recapitulative statements in case of intra-Union transactions.

4.7 Other proposed or discussed measures to fight tax fraud

The Commission presented and proposed a couple of measures that are not yet adopted by the Council. These measures are described in this paragraph.

4.7.1 Valid invoice to exercise right of deduction

In the same Communications as described in paragraph 4.6 the Commission stated that there should be equal treatment of the supplier and customer regarding the requirement to issue an invoice as evidence of the supply and the requirement to hold an invoice to exercise the right of deduction in case the reverse charge applies. At the same time that the supplier is required to issue an invoice to provide evidence of the supply, the customer should be required to hold an invoice to exercise his right of deduction. In the preamble of the Proposal⁶⁵ of 28 January 2009 of the Commission it was stated that rules should be introduced to allow Member States the right to require a valid VAT invoice in all cases where there is a right of deduction and a subsequent adjustment of the Directive was proposed by replacing point (f) of Article 178 by:

"(f) when required to pay VAT as a customer where Articles 194 to 197 or Article 199 apply, **he must hold an invoice drawn up in accordance with Sections 3 to 6 of Chapter 3 of Title XI and** he must comply with the formalities as laid down by each Member State." [emphasis added BM]

By the legislative resolution of the European Parliament of 5 May 2010 the proposed amendment of Article 178 point (f) was however deleted.⁶⁶ As a result, the aforementioned replacement of point (f) was not made by the adoption of Directive 2010/45/EU on 13 July 2010.

4.7.2 Joint and several liability

The second measure proposed by the Commission in COM (2008) 805 intends to impose joint and several liability on the taxable persons making the intra-Union supply, for the VAT due on the intra-Union acquisition of these goods in another Member State when certain

⁶³ COM (2009) 20 final

⁶⁴ COM (2009) 21 final

⁶⁵ Ibid., p. 12

⁶⁶ European Parliament legislative resolution of 5 May 2010 on the proposal for a Council directive amending Directive 2006/112/EC

(administrative) obligations are not fulfilled.⁶⁷ These conditions are that the supplier did not fulfil his obligation to submit the recapitulative statement and that the VAT was not declared by the person making the acquisition. As a result the Member State of acquisition is not informed that the goods arrived, which results in a VAT loss in this Member State. By making the supplier joint and several liable for the VAT due, the Member State of acquisition receives an additional legal base allowing them to collect the VAT due on the acquisition from a taxable person involved in fraud. However, by its legislative resolution of 24 April 2009 the European Parliament proposed amendments to the proposal of the Commission.⁶⁸ The final text of joint and several liability is therefore still under discussion.⁶⁹ The most recent version of the proposed legal text dates from 6 May 2009 and was published in a note from the Presidency to the Working Party on Tax Questions - Indirect Taxation (VAT).^{70,71}

4.8 Conclusion

The Commission's coordinated strategy to improve the fight against fiscal fraud has enlarged the powers of Member States to prevent evasion, avoidance or abuse in the sphere of VAT. By Directive 2008/117/EC and Regulation No 37/2009 the time for declaring intra-Union transactions has been reduced from three months to one month. This is complemented by Directive 2010/45/EU which requires that the invoice is to be issued no later than the fifteenth day of the month following that in which the chargeable event occurs. Directive 2009/69/EC gives Member States the possibility to reject the exemption of Article 143 if certain administrative obligations are not fulfilled. As a result of the insertion of Article 199a Member States may apply the reverse charge mechanism to domestic supplies in relation to trade with emission certificates and to transactions involving certain fraud-sensitive goods. Furthermore, the Commission has made a proposal on the need to have an invoice to exercise the right of deduction in case the reverse charge mechanism applies and a proposal on joint and several liability for the taxable person performing a intra-Union supply. However, both proposals have not resulted in an amendment of the VAT Directive up till now.

⁶⁷ See Appendix for the text of the proposal of 1 December 2008.

⁶⁸ European Parliament legislative resolution of 24 April 2009, *op.cit.*

⁶⁹ Terra, B., *The VAT package and anti-tax fraud measures*, p. 240

⁷⁰ Presidency compromise text for the proposal for a Directive dealing with joint and several liability of 6 May 2009

⁷¹ See Appendix for the text of the proposal of 9 May 2009.

5. PROPORTIONALITY OF THE POWERS OF MEMBER STATES TO PREVENT EVASION, AVOIDANCE OR ABUSE

5.1 Introduction

In this chapter the proportionality of the powers of Member States to prevent evasion, avoidance or abuse is examined by applying the definition formulated in chapter 2 and jurisprudence of the Court of Justice to the cases of chapter 3 and the proposed and adopted measures described in chapter 4.

5.2 Transport Service NV

The Court ruled that Belgium was allowed to deny Transport Service NV the exemption of an intra-Union supply and recover the VAT from the taxable person, because the requirements for a intra-Union supply of goods were not fulfilled, even though the Member State did not suffer a tax loss. In *Teleos and others*⁷² the Court ruled about a comparable situation.

Teleos and Others sold mobile telephones to a Spanish company in 2002. Under the contracts Teleos and Others were required to place the goods at the Spanish company's disposal at a warehouse in the United Kingdom. For each transaction they received a CMR consignment note from the Spanish company. Those documents were initially accepted by the authorities as evidence that the goods were exported from the United Kingdom and the supplies were therefore exempt from VAT. However, the authorities discovered that the destination stated on the notes were false and concluded therefore that the mobile telephones had never left the United Kingdom and assessed Teleos and Others to pay VAT on those supplies. Teleos and Others were in no way involved in any fraud. The Court ruled that Member States are precluded to require a supplier who acted in good faith to subsequently account for VAT, when the evidence submitted for the exemption is found to be false, without the involvement of the supplier in tax evasion being established and when the supplier took every reasonable measure to ensure that the intra-Union supply he was affecting did not lead to his participation in such evasion. By contrast, once the supplier has fulfilled his obligations regarding the evidence of an intra-Union supply and the contractual obligation to dispatch or transport the goods out of the Member State has not been satisfied by the purchaser, it is the latter who should be held liable for the VAT in that Member State. Thus, although there was no intra-Union supply within the meaning of the Directive, it is not possible to recover the unduly exempted VAT from the supplier who acted in good faith.

First of all, it is not clear from the case whether Transport Service NV acted in good faith or in bad faith. If Transport Service NV acted in good faith, took every reasonable measure to ensure the intra-Union supply took place and didn't participate in the fraud the situation is in my opinion comparable to *Teleos and others* and the Member State is therefore not allowed to deny the exemption and recover the unduly exempted VAT from the supplier. In this case the judgement is disproportional. The question arises what happens in case Transport Service NV is not in good faith. A contrario sensu to the Courts judgement in *Teleos and others*, if the supplier acted in bad faith, the amount of VAT should be recovered from him. However, it is not clear whether the mere existence of bad faith is enough to deny the exemption and to allow the Member States to recover the VAT from the supplier.⁷³ In this context *Schmeink &*

⁷² Case C-409/04, *Teleos and others*

⁷³ Opinion of Advocate General Cruz Villalón, Case C-285/09, *Criminal proceedings against R*, par. 93-94

*Cofreth*⁷⁴ needs to be mentioned. The Court had to answer the question whether the issuer of an invoice must have acted in good faith in order to obtain adjustment of VAT which has been improperly invoiced.

The Court ruled that in case the issuer of an invoice has in sufficient time wholly eliminated the risk of any loss in tax revenues, the principle of neutrality requires that VAT, which has been improperly invoiced can be adjusted without making the adjustment conditional to the good faith of the issuer. It is true that there is no tax loss for Belgium because the tax has been paid by the end user. However, this case differs from *Schmeink & Cofreth* in so far that it is not the issuer of the invoice that eliminated the tax loss, but the recipient. Without the act of the recipient there would still be tax loss for the Member State. It is therefore questionable whether this judgement can be applied to the current case. In my opinion the elimination of the risk of a loss in tax revenues should be emphasised, disregarding which person eliminated it. The most important thing is that the particular transaction did not result in a tax loss for the Member State. Therefore, if there is no tax loss, the Member State should not be allowed to deny the exemption and recover the unduly exempted VAT from the supplier.

5.3 R

Following this judgement Member States can deny the exemption for an intra-Union supply of goods and require to pay the tax subsequently in case the supplier concealed the identity of the true purchaser, enabling the latter to evade payment of VAT, even though the goods have actually physically left the Member State of supply.

First of all, the question arises whether this judgement is in conformity with the previous jurisprudence of the Court. In *Wilfried Lange*⁷⁵, *Fischer*⁷⁶ and *Linneweber and Akritidis*⁷⁷, the taxable persons in question all committed some kind of non-VAT related fraud. The Court decided that the Member States in question are not allowed to deny the exemption in this case. One could argue that R differs from these cases, because the acts of Mr R were aimed at avoiding the payment of VAT, however from *Kittel and Recolta Recycling*⁷⁸ it follows that the type of fraud is irrelevant. Apparently the Court is of the opinion that VAT fraud is more severe and should have comparable consequences. In my opinion this case is not different from the previous cases.

In *Collée*⁷⁹ the Court had to deal with a situation similar to R. The taxable person in this case did not produce the evidence of an intra-Union supply in time and was therefore refused to apply the exemption. As in R the intra-Union supply took actually place. Among other things, the Court ruled that when examining the right of exemption in relation to an intra-Union supply, the fact that the taxable person initially and knowingly concealed his supply should only be taken into account if there is a risk of a tax loss and this has not been wholly eliminated by the taxable person in question. If this is applied to R, the fact that Mr R knew he was participating in a transaction aimed at evading VAT should be neglected, because there is no tax loss in Germany. It is Portugal that suffers a tax loss. Moreover, it can be questioned whether there is a situation of evasion, avoidance or abuse in Germany.

⁷⁴ Case C-454/98, *Schmeink & Cofreth and Strobel*, par 60

⁷⁵ Case C-111/92, *Lange / Finanzamt Fürstenfeldbruck*

⁷⁶ Case C-283/95, *Fischer / Finanzamt Donaueschingen*

⁷⁷ Joined cases C-453/02 and C-462/02, *Linneweber and Akritidis*

⁷⁸ Joined cases C-439/04 and C-440/04, *Kittel and Recolta Recycling*, par 60

⁷⁹ Case C-146/05 *Collée*

According to Advocate General Cruz Villalón the acts of Mr R do not constitute an abuse of rights within the meaning of *Halifax*, because the sales made by Mr R were not fictitious transactions, with the sole purpose of obtaining a tax advantage but economically profitable transactions. Furthermore, if there is an abuse of rights, the transaction should be corrected to the situation with the absence of the abuse. However, in this case the transaction would still be qualified as intra-Union supply and still be exempt from VAT. Therefore, there is no causal link between the fraudulent declaration and the tax advantage obtained.

In the situation that the Portuguese authorities are able to collect the tax due on the intra-Union acquisition, double taxation will arise, which is contrary to the principle of neutrality. Besides that, the supplier is not able to pass on the VAT to its purchaser, which means that the VAT does not fall on the final consumer. The judgement also violates the principle of territoriality. From the logic of the transitional arrangements follows that Portugal, the country where the goods are consumed is allowed to fully tax this transaction. By not applying the exemption and requiring Mr R to pay the tax subsequently, Germany would collect tax which it is not entitled to. Using the VAT system for penalising an unlawful conduct and fraud is not allowed according to the Court's judgement in *Emsland-Stärke*.

Furthermore, the Advocate General is of the opinion that administrative cooperation and the exchange of information based on Regulation (EC) No 1798/2003 (now Regulation (EU) No 904/2010) provides a more appropriate method for combating fraud in relation to intra-Union transactions. Based on the aforementioned reasoning the judgement in *R* is in my opinion disproportional.

5.4 Sudholz

Germany was allowed to limit the right of deduction of input VAT to 50% on vehicles not used exclusively for business purposes. Taxable persons using their vehicles for more than 50% for business purposes were not entitled to deduct in accordance with the actual use. An indication about the proportionality of this judgement can be found in *Ampafrance and Sanofi*.⁸⁰

In this case the Court ruled about a measure introduced by France that excluded all expenditure in respect of accommodation, hospitality, food and entertainment from the right of deduct of input VAT. The Court of Justice stipulated that national legislation which excludes the right to deduct input VAT, without making any provision for the taxable person to demonstrate the absence of evasion or avoidance is not proportional to the objective of combating evasion and avoidance and has a disproportional effect on the objectives and principles of the common system of VAT.

This case is related to a complete exclusion instead of a flat-rate limit in *Sudholz*. However, both measures restrict the right of deduction and the taxable person must have the opportunity to demonstrate that there is no tax evasion or avoidance in his case.⁸¹ Furthermore, the Court held in *Ampafrance and Sanofi* that there is no risk of evasion or avoidance when it follows from objective evidence that the expenditure was incurred for strictly business purposes.⁸²

⁸⁰ Case C-177/99, *Ampafrance and Sanofi*, par. 62

⁸¹ Opinion of Advocate General Geelhoed of 24 October 2002, Case C-17/01, *Sudholz*, par. 59

⁸² Case C-177/99, *Ampafrance and Sanofi*, par. 56

Nevertheless, the Court decided that the measure is proportional because it is also aimed at simplifying the system of taxation. In my opinion this judgement is disproportional because the objective to prevent tax evasion or avoidance must be examined separately from the objective to simplify the system of taxation. Therefore, both objectives must be proportional to the fundamental principles and objectives of the common system of VAT. Based on *Ampafrance and Sanofi* the measure is considering its objective to prevent evasion or avoidance not proportional, because the taxable person's right of deduction is even in the absence of evasion or avoidance limited to 50%.

5.5 Kittel

In *Kittel and Recolta Recycling* the Court developed the knowledge test. If a taxable person knew or should have known that he was taking part in a transaction connected with fraud, it must be regarded as a participant of that fraud, irrespective whether he profited by the resale of those goods or not.

When should the taxable person have known from the fraud? From the judgement it follows that a trader who took every precaution which could reasonably be required from him to ensure his transactions are not connected with fraud, must be able to rely on the legality of those transactions, without the risk of losing the right to deduct. When did the taxable person know enough to be qualified as a person that took every reasonable precaution? It means that the taxable person must take every step which could reasonably be required of him to satisfy himself that the transaction which he is effecting does not result in his participation in tax evasion.⁸³ In *Netto Supermarkt*⁸⁴ the Court held that if the taxable person is in no position to recognise, even by exercising due commercial care, that the conditions for the exemption were not met, because the export proofs were forged by the purchaser he must be able to rely on the lawfulness of the transaction. See for a similar case *Teleos and others*, described in paragraph 5.2. It is however not clear when the taxable person took enough precaution. This has to be decided on a case by case basis, which causes insecurity for the taxable person.

Besides that, according to the Opinion⁸⁵ of Advocate General Ruiz-Jarabo Colomer the case in which the buyer knows about the fraud but does not participate in it or derives any benefit from it should not be treated different from the person that is in good faith. This follows from *Optigen and Others*⁸⁶ in which the Court of Justice held that an activity does not become financially unlawful because the taxable person knows that the other person has an unlawful purpose. Furthermore, the Court reiterated in *Optigen and Others* that the right to deduct is exercised regardless of whether the VAT on other previous or subsequent transactions has been paid or not. The same follows in my opinion from *Halifax* in which it was held that there is no evasion or avoidance in case there is no (tax) advantage for the taxable person. Moreover, the Advocate General stated that a disloyal taxpayer, who does not inform the Treasury of the fraud can have various consequences, but can never be deprived from its right of deduction, which is a fundamental rule of the VAT scheme. Therefore, regarding a taxable person participant of fraud in case he knew or should have known and thereby refusing the right to deduct input VAT is in my opinion disproportional if he did not profit from the fraud.

⁸³ Case C-409/04, *Teleos and others*, par. 60

⁸⁴ Case C-271/06, *Netto Supermarkt*, par. 27

⁸⁵ Opinion of Advocate General Ruiz-Jarabo Colomer, Joined Cases C-439/04 and C-440/04, *Kittel and Recolta Recycling*

⁸⁶ Joined cases C-354/03, C-355/03 and C-484/03, *Optigen and others*

5.6 Ampliscientifica and Amplifin

The national legislation under review in *Ampliscientifica and Amplifin* allows taxable persons to make VAT declarations and payments in accordance with simplified rules. As stated in paragraph 3.4 the judgement of the Court seems to imply that Member States are allowed to limit the applicability of certain special schemes to specific situations when in the absence of this limitation it is likely to encourage avoidance and abuse. The Court used this reasoning only in two other cases, namely in *Heintz van Landewijck*⁸⁷ and *BATIG*,⁸⁸ which both consider the use of excise stamps and tax markings in relation with excise goods.

In these cases the Court ruled that a national law which allows the purchaser of excise stamps to obtain reimbursement simply by claiming the excise stamps or goods to which tax markings have been affixed have gone missing would encourage abuse and evasion. As the Advocate General Poirares Maduro stated in its Opinion⁸⁹ in *Heintz van Landewijck*, the arrangement of allocating the risk of stamps gone missing to the person requesting those stamps is justified by the aim of the prevention of evasion, avoidance or abuse.

Does the absence of the time-limit of the special scheme increase the likelihood of evasion, avoidance or abuse? According to the Court if no time-limit is imposed the effect might have been to permit individual operations to be carried out justifying the ad hoc formation of legal structures. There seems to be a risk of evasion in absence of the time-limit. Furthermore, as held in *Ampafrance and Sanofi* taxable persons must have the opportunity to demonstrate that there is no risk of evasion or abuse. By imposing a time-limit the national legislation requires economic operators to demonstrate certain continuity in their operations and show that there is not simply an intention of obtaining a tax advantage. In my opinion this judgement is therefore in conformity with the principle of proportionality.

5.7 Direct Cosmetics

The Court ruled that the United Kingdom is allowed to adjust the taxable amount to the open market value. From *Heintz van Landewijck*⁹⁰ it follows that national measures derogating from the Sixth Directive on the basis of Article 27(5) of the Sixth Directive (now Article 394 of the VAT Directive), which are allowed in order to simplify the procedure for charging the tax or to prevent certain types of tax evasion or avoidance must be interpreted strictly. National measures may not derogate from the basis for charging VAT laid down in Article 11 of the Sixth Directive except within the limits strictly necessary for achieving that aim. Are the measures of the United Kingdom strictly necessary? In *Commission v Belgium*⁹¹ the Court decided on a measure imposed by Belgium providing a minimum taxable amount for the supply and importation of new cars. According to the Court the measure departed in a general and systematic way from the rules laid down in Article 11, because all price discounts and rebates were ignored. The measure under review in *Direct Cosmetics Ltd* applies, on the other hand, only to cases in which the whole or part of the taxable person's business consists in supplying persons not liable to tax with goods which they are intended to sell by retail. Furthermore, the Court acknowledged that the absence of the measures would create a distortion of competition, which is contrary to the general system of VAT. It could even

⁸⁷ Case C-494/04, *Heintz van Landewijck*

⁸⁸ Case C-374/06, *BATIG*

⁸⁹ Opinion of Advocate General Poirares Maduro, Case C-494/04, *Heintz van Landewijck*

⁹⁰ Case C-494/04, *Heintz van Landewijck*, par. 53

⁹¹ Case 324/82, *Commission / Belgium*

influence undertakings to change their trading methods, contrary to the principle of neutrality. The measure only applies to certain specific sale schemes which lead to an undesirable reduction of the basis of assessment and result in tax avoidance. Moreover, the measure is intended to deal only with undertakings which sell exclusively or essentially in the manner described.⁹² Therefore, the measure does not derogate further than strictly necessary and is in my opinion, subsequently not disproportionate to the fundamental objectives and principles of the common system of VAT.

5.8 Stadeco

Member States are allowed to make a refund subject to the issue of a corrected invoice and the actual repayment of the incorrectly invoiced VAT to the beneficiary in case of unjust enrichment.

However, it follows from *Reemtsma Cigarettenfabriken*⁹³ that if the reimbursement of VAT becomes impossible or excessively difficult Member States may be required to provide for the instruments and procedural rules necessary to enable the recovery of unduly invoiced tax by the taxable person. Furthermore, the reasoning of *Schmeink & Cofreth* can be understood that national legislation may, in case there is no risk of any tax loss not impose any further conditions on the refund.⁹⁴ Requiring a corrected invoice, in order to ensure there is no risk of tax loss is in my opinion not disproportionate. On the other hand, it could be contrary to the principle of proportionality to refuse a refund if replacement of the invoice is impossible.⁹⁵

Regarding the requirement to actual repayment of the incorrectly invoiced VAT to the beneficiary in case of unjust enrichment it follows from *Marks & Spencer*⁹⁶ that Union law does not prevent domestic legislation from disallowing repayment in case this would lead to unjust enrichment of the recipients. This is my opinion not disproportional, because it would result in a tax advantage for the supplier otherwise.

5.9 Federation of Technological Industries and Others

In this case the Court stipulated that a person that is jointly and severally liable for the payment of VAT can be required to provide security for the VAT due under Article 273 of the Directive. This provision states that:

"Member States may impose other obligations which they deem necessary to ensure the correct collection of VAT and to prevent evasion, subject to the requirement of equal treatment as between domestic transactions and transactions carried out between Member States by taxable persons and provided that such obligations do not, in trade between Member States, give rise to formalities connected with the crossing of frontiers.

The option under the first paragraph may not be relied upon in order to impose additional invoicing obligations over and above those laid down in Chapter 3."

⁹² Opinion of Advocate General Vilaça, Joined cases 138/86 and 139/86, *Direct Cosmetics Ltd / Commissioners of Customs and Excise*

⁹³ Case C-35/05, *Reemtsma Cigarettenfabriken*, par. 41

⁹⁴ Opinion of Advocate General Kokott, Case C-566/07, *Stadeco*, par. 25

⁹⁵ *Ibid.*, par. 28

⁹⁶ Case C-309/06, *Marks & Spencer*, par. 41

First of all, it follows from *Eismann*⁹⁷ that Member States can impose stricter formalities on internal transactions than those applying to intra-Union transactions. Therefore, if the requirement to provide security only applies to domestic transactions this is in conformity with Article 273. Both the Court and Advocate General Maduro by its Opinion⁹⁸ state that a person who is liable to pay VAT can be required to provide security for that payment. In my opinion this does not go further than necessary to prevent evasion, avoidance or abuse. Moreover, without providing security for the VAT due, the system of joint and several liability would in my opinion become meaningless. The proportionality of the system of jointly and severally liability is described in paragraph 5.13.2.

5.10 Frequency of recapitulative statements

The amendments by Directive 2008/117/EC and Regulation No 37/2009 impose more administrative obligations on the taxpayer by increasing the frequency of issuing recapitulative statements from every three months to every month. Moreover, the amendment of Article 222 by Directive 2010/45/EU requires taxpayers to provide the recapitulative statements within a shorter timeframe. On 15 November 2007 PricewaterhouseCoopers presented a study for the European Commission of the effects of the increase of the submission frequency on the administrative costs.⁹⁹ The study shows that by increasing the frequency the administrative costs rise, especially for SME's. However, because of the high threshold only a small proportion of the business are affected.¹⁰⁰ Furthermore, by Article 2 of Directive 2008/117/EC the Commission has a obligation to evaluate the impact and usefulness of Article 263 and, if necessary present appropriate proposals. In my opinion the increased frequency of recapitulative statements is therefore proportional.

5.11 Exemption of intra-Union supply linked with importation

The introduction of the second paragraph to Article 143 imposes more administrative obligations on the taxable person importing goods followed by an intra-Union supply. According to the Communication¹⁰¹ of the Commission the exemption of Article 143 is increasingly used in intra-Union fraud schemes. The taxable person's obligations are limited to providing his VAT identification number, the VAT identification number of his customer and evidence that the imported goods are intended to be transported or dispatched from the Member State of importation to another Member State. In my opinion these obligations are not disproportional to the objective pursued.

5.12 Reverse charge for certain domestic supplies

By introducing a reverse charge for emission certificates and other fraud-sensitive goods, such as mobile telephones and precious metals the Commission tries to remove the possibility to use these goods in a carousel fraud scheme. It cannot be disputed that the use of certain goods and services in a carousel fraud scheme results in a tax loss for the Member States. According to Europol, the fraudulent use of emission certificates alone resulted in a damage of 5 billion.¹⁰² Furthermore, a reverse charge will stop carousel fraud for these specific goods

⁹⁷ Case C-217/94, *Eismann Alto Adige / Ufficio IVA di Bolzano*

⁹⁸ Opinion of Advocate General Poiras Maduro, Case C-384/04, *Federation of Technological Industries and others*

⁹⁹ PricewaterhouseCoopers, Study in respect of introducing a change in the requirements to the recapitulative statements

¹⁰⁰ COM (2008) 147 final, p. 6

¹⁰¹ COM (2008) 805 final, p. 3

¹⁰² Press release Europol, Carbon Credit fraud causes more than 5 billion euros damage for European Taxpayer

and services.¹⁰³ On the other hand, the reverse charge mechanism can cause serious problems for enterprises, especially small enterprises.¹⁰⁴ It is therefore difficult to say whether the introduction of reverse charge mechanism for these goods is proportional to the prevention of evasion, avoidance or abuse. However, the second paragraph at point (b) requires Member States to evaluate the effect of the application of the reverse charge mechanism on fraudulent activities. Because of this evaluation requirement, measures introduced on the basis of Article 199a are in my opinion proportional.

5.13 Other proposed measures to fight tax fraud

Paragraph 5.13.1 contains the discussion on the proportionality of the proposal to make the right of deduction in case of a reverse charge procedure subject to the requirement to have an invoice. In paragraph 5.13.2 the proportionality of the initial proposal of joint and several liability of 1 December 2008 and the Presidency's proposal of 6 May 2009 is described.

5.13.1 Valid invoice to exercise right of deduction in case of reverse charge procedure

It is not clear why the European Parliament, by its legislative resolution, deleted the requirement of a valid invoice to exercise the right of deduction in case the reverse charge mechanism applies from the Proposal amending the Directive on the rules of invoicing. The answer to the question whether the requirement of an invoice is proportional can be found in the jurisprudence of the Court of Justice. In *Bockemühl*,¹⁰⁵ the Court had to answer whether,

"in a situation where the reverse charge procedure applies, the right to deduct of a taxable person, liable as the recipient of services for the VAT relating thereto, can be exercised only if that taxable person holds an invoice drawn up in accordance with Article 22(3) of the Sixth Directive [Article 220 of the VAT Directive BM]."

First of all, the Court ruled that regarding the interpretation of Article 18(1)(a) and (d) of the Sixth Directive (now Article 178(a) and (f)), only Article 18(1)(d) applies to the reverse charge procedure. Under this provision the imposition and extent of formalities to be complied with in order to exercise the right to deduct should not exceed what is strictly necessary for the purposes of verifying the correct application of the reverse charge procedure. If the authorities are able to establish that the recipient of the supply is liable to VAT, it cannot impose additional conditions which may have the effect of rendering the right of deduction ineffective for practical purposes. Requiring the taxable person to be in possession of an invoice in order to deduct would result in the situation that on the one hand, the taxable person is liable for the VAT in question and on the other hand bears the risk of not being able to deduct that tax. Therefore, in case the reverse charge applies, a taxable person who is liable for VAT cannot be obliged to have an invoice in order to exercise his right to deduct.

5.13.2 Joint and several liability

Although the European Parliament rejected the first proposal presented by the Commission to introduce joint and several liability for intra-Union transactions the Commission continued to

¹⁰³ Wolf, R.A., *The Sad History of Carbon Carousels*, p. 405

¹⁰⁴ Terra, B., Kajus, J., *Commentary – A Guide to the Recast VAT Directive*, Online Edition, par. 11.2.1.5

¹⁰⁵ Case C-90/02, *Bockemühl*, par. 47

work on it. Therefore, both the initial proposal and the Presidency version of 6 May 2009 are discussed in this section.

5.13.2.1 Proposal of 1 December 2008

On 24 April 2009 the European Parliament delivered its legislative resolution on the initial proposal of the Commission.¹⁰⁶ The proposed amendments clearly indicate that the European Parliament questions the proportionality of the proposal. For example, it proposes to amend recital 5 of the preamble by adding:

"In so doing, Member States should ensure that any measures to counter fraud are proportional and targeted at persons that have committed fraud."

It seems that the initial proposed provision of joint and several liability is based on the presumption that the person who makes an intra-Union supply and fails to properly report the transaction is engaged in fraud.¹⁰⁷ Contrary to what the Commission mentioned in its Communication, the proposal of joint and several liability of the supplier is not limited to cases where there is a tax loss in the Member State of destination.¹⁰⁸ If the customer has a full right of deduction, but fails to report the acquisition correctly, there is no real loss for the Member State of acquisition. In case the Member State of acquisition does not incur a loss of VAT revenues the supplier's liability is disproportional to the aim of combating VAT fraud.¹⁰⁹

Furthermore, it follows from *Federation of Technological Industries and Others* that the presumptions to make a person jointly and severally liable for the payment of VAT may not be formulated in such a way that is impossible or excessively difficult to prove the contrary. Traders who take every precaution required to ensure that their transactions are not part of a chain which includes a VAT fraudulent transaction must be able to rely on the legality of those transactions, without the risk being made jointly and severally liable to pay the VAT due by the other person. However, the proposal does not require that the authorities show that the supplier was aware or should have been aware of the VAT fraud in the next stage of the chain.

In my opinion the amendment of the proposal by the European Parliament was a right decision. The proposed joint and several liability is, based on the aforementioned reasoning, not proportional to the objectives pursued.

5.13.2.2 Presidency proposal of 6 May 2009

On the contrary, the Presidency proposal of 6 May 2009 stipulates that a person supplying the goods can only be held liable if there is a tax loss in the Member State of acquisition and the person knew or had reasonable grounds to suspect, that its customer intended to cause a tax loss in that Member State. Furthermore, if the supplier is in good faith it cannot be held jointly and severally liable for the VAT due.

¹⁰⁶ European Parliament legislative resolution of 24 April 2009, op.cit.

¹⁰⁷ Lejeune, I., Kotanidis, S., Cortvriend, E., Joint and Several Liability relating to Intra-Community Acquisitions, p. 365

¹⁰⁸ COM (2008) 805 final, p. 8

¹⁰⁹ Lejeune, I., Kotanidis, S., Cortvriend, E., op.cit., p. 365. See also the analyses in paragraph 5.2 about the proportionality of the Transport Service NV judgement.

This proposal is in line with case law on good faith, *Schmeink & Cofreth* and *Federation of Technological Industries and Others*. However, the proposal contains part of the knowledge test developed in *Kittel*. If there is a tax loss in the Member State of acquisition and the supplier knew or should have known that the acquirer would cause a tax loss it is held jointly and severally liable. However, in paragraph 3 of the proposal the situations in which this condition is fulfilled are described. It seems to me that the situations described are exhaustive, which means that the insecurity for the supplier is limited. In my opinion the Presidency's proposal is therefore in conformity with the principle of proportionality.

5.14 Conclusion

The power to deny the exemption of an intra-Union supply and recover the VAT if the requirements for the intra-Union supply are not fulfilled, irrespective of the fact that there is a tax loss in the Member State is following *Teleos and others* and *Schmeink & Cofreth* disproportional. This is also the case for the knowledge test developed in *Kittel and Recolta Recycling*. If a person knew or should have known, but did not participate in the fraud or derived any benefit from it, it should not be treated different from a person that acted in good faith. Even in the case the supplier is in bad faith, but the intra-Union supply took actually place refusal of the exemption is not proportional. The judgement in *R* infringes among other things the principle of neutrality and principle of territoriality. Moreover, more proportionate measures are available. Refusing a taxable person the right to deduct in the absence of abuse because a measure is also aimed at simplifying the system of taxation is in my opinion not proportional. Both objectives of the measure should be proportional. Based on *Ampafrance and Sanofi* the objective to prevent evasion, avoidance or abuse of the measure under review in *Sudholz* does not meet this requirement.

On the other hand, refusing a taxable person to make use of simplified rules seems proportional if this would have encouraged evasion and abuse otherwise. So is making a refund subject to the condition of the issue of a corrected invoice to ensure the risk that a loss of tax is wholly eliminated. As well as making it subject to the requirement that the actual incorrectly invoiced VAT is repaid to the beneficiary in case of unjust enrichment. Measures that allow Member States to adjust the taxable amount to the open market value in specific circumstances and requiring the taxable person to provide security for the VAT due if it's made joint and severally liable is also in conformity with the principle of proportionality.

Both the amendments on the frequency of recapitulative statements and the requirements of the exemption for an intra-Union supply linked with importation increase the (administrative) obligations for taxable persons. However, this seems to be proportional to the objectives pursued. So is Directive 2010/23/EU, which moreover provides a requirement for Member States to evaluate the effect of the application of the reverse charge procedure on fraudulent activities.

The proposals on the adoption of joint and several liability and the requirement to have an invoice in order to deduct are on the other hand disproportional. On the contrary the Presidency's proposal for jointly and severally liability is in conformity with the principle of proportionality.

6. CONCLUSION

As stated in the introduction, the aim of my research is to analyse what powers Member States have to prevent evasion, avoidance or abuse, based on jurisprudence of the Court of Justice, the proposed measures by the Commission and the adopted measures by the Council to fight tax fraud and whether these powers are in conformity with the principle of proportionality.

The principle of proportionality is enshrined in Article 5 of the Treaty on European Union and also applies to measures undertaken by Member States to prevent evasion, avoidance or abuse in the sphere of VAT. It requires an acceptable balance between the detriment of fundamental principles and objectives of the common system of VAT and the power of Member States to prevent potential evasion, avoidance or abuse. This definition consists of two elements. First of all,

- the measure must be aimed at the prevention of potential evasion, avoidance or abuse.
- Secondly, the detriment of fundamental principles and objectives of the common system of VAT must be proportional to this objective.

From *Transport Service NV* it follows that Member States have the power to deny the exemption for an intra-Union supply and recover the VAT if the requirements for the intra-Union supply are not fulfilled. Irrespective of the fact that there is tax loss in the Member State. However, it follows from *Teleos and others* that in case the requirements for the intra-Union supply are not fulfilled, but the supplier acted in good faith, Member States are not allowed to require a supplier to subsequently account for VAT. Good faith of the supplier is not required if the issuer of an invoice has in sufficient time wholly eliminated the risk of any loss in tax revenues according to the Court's judgement in *Schmeink & Cofreth*.

Considering the right of deduction the Court ruled in *Kittel and Recolta Recycling* that Member States have the power to deny this right if it is ascertained that the taxable person knew or should have known that, by his purchase he was participating in VAT fraud, irrespective of the fact he profited by the resale of those goods or not. This is known as the knowledge test. However, from *Optigen and Others* it follows that an activity does not become financially unlawful because the taxable person knows that the other person has an unlawful purpose. A person who knew or should have known, but did not participate in the fraud or derived any benefit from it should not be treated different from a person that acted in good faith.

In my opinion the powers based on the judgements in *Transport Service NV* and *Kittel and Recolta Recycling* are disproportional. The powers of Member States to prevent evasion, avoidance or abuse should be limited to the cases in which the taxable person acted in bad faith, gained a tax advantage from the fraud or caused a tax loss for the Member State concerned.

In *R* the Court decided that, in case a supplier knew he was participating in fraud the Member State has the power to deny the exemption and require the supplier to pay the tax, even though the requirements for an intra-Union supply were fulfilled. However, this judgement infringes the principle of neutrality and principle of territoriality. Moreover, more appropriate measures are available to combat fraud connected with intra-Union transactions.

Furthermore, from *Sudholz* it follows that a Member State can limit the right to deduct input VAT through a derogating measure if the measure is also aimed at simplifying the system of taxation. Notwithstanding the taxable person who is able to demonstrate that it is entitled to a higher deduction. This is, based on *Ampafrance and Sanofi* in my opinion disproportional. A taxable person should in the absence of evasion, avoidance or abuse be allowed to deduct input VAT in accordance with the use of the goods. Both objectives of the derogating measure must be proportional.

On the other hand, it follows from *Ampliscientifica and Amplifin* that refusing a taxable person to make use of simplified rules, by imposing a time-limit seems proportional if this would have encouraged evasion and abuse otherwise. So is making a refund subject to the condition of the issue of a corrected invoice to ensure the risk of a tax loss is wholly eliminated. As well as making it subject to the requirement that the actual incorrectly invoiced VAT is repaid to the beneficiary in case of unjust enrichment. This follows from *Stadeco*.

Member States are allowed to adjust the taxable amount to the open-market value if the measure goes not further than strictly necessary for achieving its aim. The measure under review in *Direct Cosmetics* is therefore proportional, because its only applicable to a specific sale scheme by undertakings of a certain size.

Following *Federation of Technological Industries and Others* Member States may require a taxable person that is declared joint and several liable to provide security for the payment of the VAT due. This is in my opinion proportional. Moreover, without providing security for the VAT due, the system of joint and several liability would be meaningless.

The Commission's coordinated strategy against VAT fraud gives Member States the power to take measures against different kind of fraud, especially carousel fraud. By Directive 2008/117/EC, Directive 2010/45/EU and Regulation No 37/2009 taxable persons are now in case of intra-Union transactions required to provide recapitulative statements at a higher frequency and a shorter timeframe. Following the amendment of the VAT Directive by Directive 2010/23/EU Member States are allowed to apply the reverse charge mechanism to domestic supplies in relation to trade with emission rights and certain fraud sensitive goods. By Directive 2009/69/EC Member States have the possibility to reject the exemption of Article 143 if certain administrative obligations are not fulfilled. In my opinion these amendments are proportional. It seems that legislative procedure of the European Union works as a good control mechanism to dismiss measures that are not in conformity with the principle of proportionality.

Based on the aforementioned it is difficult to give a clear answer to the hypothesis stated in the introduction.

On the one hand, the powers that Member States deriving from the amendments to the Directive are proportional. So are the powers following from the judgements in *Ampliscientifica and Amplifin*, *Stadeco*, *Direct Cosmetics* and *Federation of Technological Industries and Others*. On the other hand, the knowledge test, developed in *Kittel and Recolta Recycling* is disproportional. The same is in my opinion true for the Court's judgements in *Sudholz*, *Transport Service NV* and *R*. It seems therefore that the hypothesis is true in regard to the powers that Member States have in relation to the right of deduction and the exemption for intra-Union supplies.

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- C-285/09, *Criminal proceedings against R*, Opinion of Advocate General Cruz Villalón, not yet officially published, 29 June 2010

APPENDIX

Proposal joint and several liability 1 December 2008

Article 1

Directive 2006/112/EC is amended as follows:

...

(2) Article 205 is replaced by the following:

“Article 205

1. In the situations referred to in Articles 193 to 200 and Articles 202, 203 and 204, Member States may provide that a person other than the person liable for payment of VAT is to be held jointly and severally liable for payment of VAT.

2. In the situation referred to in Article 200, the person supplying goods in accordance with the conditions laid down in Article 138, shall be held jointly and severally liable for the payment of the VAT due on the intra-Community acquisition of those goods where he has not complied with the obligation provided for in Articles 262 and 263 to submit a recapitulative statement containing the information concerning the supply or the recapitulative statement submitted by him does not set out the information concerning this supply as required under Article 264.

However, the first subparagraph shall not apply in the following situations:

(a) the customer has, for the period during which the tax became chargeable on the transaction concerned, submitted a VAT return as provided for in Article 250 containing all the information on this transaction;

(b) the person supplying goods in accordance with the conditions laid down in Article 138 can duly justify to the satisfaction of the competent authorities his shortcoming referred to in the first subparagraph of this paragraph."

Proposal joint and several liability 9 May 2009

Article 1

Directive 2006/112/EC is amended as follows:

Article 205 is replaced by the following:

"Article 205

1. In the situations referred to in Articles 193 to 200 and Articles 202, 203 and 204, Member States may provide that a person other than the person liable for payment of VAT is to be held jointly and severally liable for payment of VAT.

2. In the situation referred to in Article 200, the person supplying goods in accordance with Article 138, shall be held jointly and severally liable for the payment of the VAT due on the intra-Community acquisition of those goods where [...] both the following conditions are fulfilled:

(a) the person acquiring goods caused, by omitting to fulfil of his legal obligations pursuant to this Directive in respect of transactions with the acquired goods, a tax loss in the Member State of acquisition;

(b) the person supplying goods knew or had reasonable grounds to suspect, at the time of the supply of goods, that the person acquiring those goods intended to cause the tax loss as referred to in point (a).

(3) For the purposes of paragraph 2(b), the person supplying goods shall be presumed to have known or to have had reasonable grounds to suspect that the person acquiring those goods intended to cause the tax loss if at least two of the following situations have occurred:

(a) the person supplying goods has not complied with the obligation provided for in Articles 262 and 263 to submit a recapitulative statement containing the information concerning the supply or the recapitulative statement submitted by him does not set out the information concerning the supply as required under Article 264;

(b) the supply of goods has been or is to be paid by means not typical for the relevant sector of business, such as payment in cash or by offset against monies due from the supplier;

(c) the nature of goods supplied differs from those typically supplied or acquired by the respective contractual party;

(d) the arrangements made for the transport of goods are not standard practice for the transaction concerned.

Paragraph 2 shall not apply if the person supplying goods provides proof that he has acted in good faith."