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Proposal for a

COUNCIL IMPLEMENTING DECISION

amending Implementing Decision (EU) 2019/310 authorising Poland to apply a special measure derogating from Article 226 of Directive 2006/112/EC on the common system of value added tax

EXPLANATORY MEMORANDUM

Pursuant to Article 395(1) of Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (hereafter 'the VAT Directive'), the Council, acting unanimously on a proposal from the Commission, may authorise any Member State to apply special measures for derogation from the provisions of that Directive in order to simplify the procedure for collecting VAT or to prevent certain forms of tax evasion or avoidance.

In accordance with Article 2 of Council Implementing Decision (EU) 2019/310[1], Poland submitted a report to the Commission on its overall impact on the level of VAT fraud and on the taxable persons concerned on 29 April 2021 and registered on 5 May 2021.

By letter registered with the Commission on 26 July 2021 Poland requested an authorisation to continue to derogate from Article 226 of the VAT Directive with regard to value added tax (VAT) invoicing requirements and to introduce the mandatory split payment mechanism for supplies of goods and services susceptible to fraud covered generally by the reverse charge mechanism and joint and several liability in Poland. In accordance with Article 395(2) of the VAT Directive, the Commission informed the other Member States by letter dated 27 October 2021 of the request made by Poland. By letter dated 28 October 2021, the Commission notified Poland that it had all the information necessary to consider the request.

1. CONTEXT OF THE PROPOSAL

• Reasons for and objectives of the proposal

Poland introduced the voluntary split payment mechanism on 1 July 2018. Following Council Implementing Decision (EU) 2019/310, Poland introduced the mandatory split payment mechanism for the payment of VAT for certain supplies of goods and services susceptible to fraud. The mandatory split payment mechanism is based on the same principles of the voluntary split payment mechanism. Both models of split payment mechanism (i.e. voluntary and obligatory) exist in parallel, and they usually supplement each other. This implies that both models are based on the same system of bank accounts and refer to transactions between businesses (B2B) where, the payment is made by electronic bank transfer. When a taxable person carries out supplies within the scope of the split payment provisions, they are obliged to have, in addition to his regular bank account, a separate blocked VAT account. The bank will act as a splitting agent and perform the activities with the aim of transferring the amount paid by the customer to the relevant accounts of the supplier, i.e. the taxable amount to the regular account of the trader; and the VAT amount to the trader's blocked VAT account. Funds on the blocked VAT account are owned by the taxable person. However, it is only possible to dispose of the funds in relation to the payment of the VAT due to the tax authority or VAT resulting from invoices received from suppliers.

By imposing that the VAT due is paid to a blocked VAT bank account of the supplier, the measure aims at combating tax fraud in the form of non-payment of VAT liability by suppliers of goods and services which are susceptible to fraud. Since the amount of VAT deposited on a separate VAT account of a taxable person can only be used for restricted purposes, namely for the payment of the VAT liability to the tax authority or the payment of VAT on invoices received from suppliers, it is better guaranteed that the tax authorities will receive the whole VAT amount which should be transferred by the taxable person in favour of the State Treasury.

[1] Council Implementing Decision (EU) 2019/310 of 18 February 2019 authorising Poland to introduce a special measure derogating from Article 226 of Directive 2006/112/EC on the common system of value added tax (OJ L 51, 22.2.2019, p. 19–27).

The split payment mechanism becomes mandatory when at least one item specified on the invoice whose total gross amount (including VAT) exceeds PLN 15,000 and refers to the goods or services susceptible to fraud included in the scope of the derogating measure listed in the annex.

These supplies cover economic sectors such as steel, scrap, electronical equipment, gold, non-ferrous metals, fuels and plastics which were generally subject to the reverse charge mechanism and to joint and several liability in Poland prior to the implementation of the mandatory split payment (the list of supplies to be covered by the split payment mechanism was included in Annex to Council Implementing Decision (EU) 2019/310).

The Republic of Poland notes that upon the entry into force of the so-called new "VAT rates matrix" on 1 July 2020, the method for classifying goods and services has changed for the purposes of applying the mandatory split payment mechanism, consisting in replacing the Polish Classification of Goods and Services of 2008 (PKWiU 2008) with the Polish Classification of Goods and Services of 2015 (PKWiU 2015). The transition to PKWiU 2015 did not cause any changes in the scope of goods and services covered by the mandatory split payment mechanism upon Decision 2019/310. It should therefore be emphasized that the scope of goods and services listed in the Annex to Decision 2019/310 will remain valid. In some items of PKWiU 2015, only the symbols of the statistical classification or the editorial names of goods and services were modified in relation to the PKWiU 2008, on which the Annex to Decision 2019/310 is based. However, it did not cause any changes in the scope of goods and services covered by the mandatory split payment mechanism. For the sake of legal certainty, the Annex to Decision 2019/310 should be updated to reflect the changes brought to PKWiU 2008 by PKWiU 2015.

The derogating measure requires that any invoices issued for the supply of goods and services between VAT payers, within the scope of the split payment mechanism, include a special statement that VAT shall be paid to the separate blocked VAT bank account of the supplier.

Under the general rules applicable in Poland, in case of the surplus of input tax over the output tax recognised by the taxable person in the VAT return as a VAT refundable amount, such refund will be carried out within 60 days to taxable person's regular account. To reduce the effects of the split payment model on traders' cash flow, a faster procedure is foreseen by Poland for the refund of the input tax surplus. At the request of the taxable person the refund will take place within 25 days. Nevertheless, according to the information provided by Poland, such requests are treated in a much shorter period of time (as it stems from the assessment of the obligatory split payment mechanism the applications for releasing funds were decided on within less than 16 days during December 2020).

According to Poland, the costs of operating the split payment system should not be significant and will mostly be connected to the implementation of the system, its servicing and to managing the bank account.

The mandatory split payment mechanism is one of the key elements of the complementary measures that are aimed at reducing VAT fraud and modernizing the Polish tax system, which have been introduced by Poland in recent years[2].

[2] The most relevant connected measures are: the Single Audit File (JPK_VAT); the electronic system for analysing cash flows (STIR); the accurate and reliable electronic register of VAT payers (White List); the system of online cash registers for monitoring the retail sector; the new VAT rates matrix which

Taking into account the above, the Commission is of the view that the mandatory split payment mechanism for supplies of goods and services susceptible to fraud and listed in the Annex can bring effective results in the fight against tax fraud. Therefore, it is proposed to grant the derogation as from 1 March 2022 until 28 February 2025.

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

The derogation can be authorised based on Article 395 of the VAT Directive in order to simplify the procedure for collecting VAT or to prevent certain forms of tax evasion or avoidance. Poland requested the derogating measure to fight tax evasion in the sectors in which VAT fraud has been detected for years. The derogation is consistent with the existing policy provisions.

By Council Implementing Decision (EU) 2020/1105[3] Italy was authorised to extend a similar derogation to apply the split payment mechanism. Under the Italian split payment system, the VAT due is paid to the blocked VAT account at the tax authorities. The scope of the Italian derogation is limited to supplies to public authorities, entities controlled by public authorities and a number of companies listed on the stock exchange.

2. LEGAL BASIS, SUBSIDIARITY AND PROPORTIONALITY

- **Legal basis**

Article 395 of the VAT Directive.

- **Subsidiarity (for non-exclusive competence)**

Considering the provision of the VAT Directive on which the proposal is based, the subsidiarity principle does not apply.

- **Proportionality**

The proposal complies with the proportionality principle for the following reasons.

The Decision concerns an authorisation granted to a Member State upon its own request and does not constitute any obligation.

The derogation is limited in time and restricted to specific supplies, the scope is targeted to sectors which pose considerable problems of tax fraud.

Given the broad scope of the derogation, a report on the functioning and the effectiveness of the measure on the level of VAT fraud and on the taxable persons (regarding the refunds of VAT, the administrative burden, costs for taxable persons etc.) is to be submitted by Poland in case Poland requests to prolong the special measure.

Therefore, the special measure is proportionate to the aim pursued, i.e. to combat tax evasion and simplify tax collection.

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simplified the application of reduced VAT rates and increased the certainty of the taxable persons as to the correct application of the VAT rates through introduction of the binding rate information which is a decision issued at the request of the taxable person to set out the correct rate for goods/services; advanced big data analysis by the revenue administration; the digitalization of the revenue administration.

[3] Council Implementing Decision (EU) 2020/1105 of 24 July 2020 amending Implementing Decision (EU) 2017/784 authorising the Italian Republic to apply a special measure derogating from Articles 206 and 226 of Directive 2006/112/EC on the common system of value added tax (OJ L 242, 28.7.2020, p. 4–6).

- **Choice of the instrument**

Proposed instrument: Council Implementing Decision.

Under Article 395 of the VAT Directive, derogation from the common VAT rules is only possible upon authorisation of the Council acting unanimously on a proposal from the Commission. A Council Implementing Decision is the most suitable instrument since it can be addressed to an individual Member State.

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

- **Stakeholder consultations**

This proposal is based on a request made by Poland and concerns only this Member State.

- **Collection and use of expertise**

There was no need for external expertise.

- **Impact assessment**

The proposal for a Council Implementing Decision authorises Poland to derogate from Article 226 of the VAT Directive and to introduce the mandatory split payment mechanism for the payment of VAT on specific supplies of goods and services.

In accordance with Article 2 of Decision 2019/310, Poland was obliged to submit a report to the Commission on the overall impact of the mandatory split payment mechanism on the level of VAT frauds and on the taxable persons concerned within 18 months after the entry into force of the measure referred to in Article 1 of the Decision. As this measure applies from 1 November 2019, the aforementioned report was submitted to the Commission on 29 April 2021 and registered by the Commission on 5 May 2021.

The assessment of the functioning of the mandatory split payment mechanism made by Poland, shows in particular that this measure is complementing other key measures to reduce tax evasion[4]. The implemented complementary measures to the mandatory split payment mechanism, have contributed to reducing the scale of VAT frauds, including carousel frauds and VAT extortions. Poland has recorded a significant shrinkage of the VAT gap that fell below the EU average within a short time. According to the CASE's estimates for the European Commission, it fell down to approx. 9.7% in 2019 (marking a decrease by 0.2 pp against 2018)[5], while the VAT gap was equal to approx. 14% in 2017. Due to the economic crisis caused by the pandemic, the economic situation in Poland deteriorated significantly in 2020 and consumption demand weakened. However, the preliminary estimates of the Ministry of Finance included in the Multiannual State Financial Plan for the years 2021-2024 indicate that the VAT gap shrank by further 1.3 pp during 2020 irrespective of the recession and accounted for approx. 10.8% of the potential inflows.

The funds on the blocked VAT account cannot be disposed of by the taxable person unless it is for the payment of VAT due to the tax authority or VAT resulting from invoices received

4 See list of measures in footnote 2

5 Study and Reports on the VAT Gap in the EU-28 Member States 2020 Final Report, CASE – Center for Social and Economic Research (Project leader) September – 2020.

from suppliers impacting thus traders' cash flow. To diminish the negative impact, in case of the surplus of input tax over the output tax recognised by the tax authorities, a faster procedure is foreseen by Poland for the refund of the input tax surplus. At the request of the taxable person the refund will take place within 25 days from the submission date of the tax return, instead of 60 days under the normal procedure. During the preliminary phase of the voluntary split payment mechanism (starting from 1 July 2018), it took the tax authorities an average of 27.56 days to process an application, while the same proceeding has taken only 15.90 days in December 2020. This means that the applications for releasing funds are processed by the tax authorities in an increasingly efficient way. This is especially important during the current situation caused by the COVID-19 pandemic, for businesses that have problems with continuous financial liquidity.

Furthermore, Poland underlined in the request that ensuring effective and timely performed tax refunds will be treated as priority. It will accelerate the refund of the surplus of input tax over output tax to the VAT account on preferential terms within a maximum period of 25 days from the submission date of the settlement (tax return).

Suppliers that are not established in Poland are also covered by the mandatory split payment mechanism when carrying out the supplies of goods or services subject to the mandatory split payment in Poland. These traders have to hold a bank account operated pursuant to Polish Banking Law. Poland reported to the Commission, that the non-established traders do not incur any additional costs relating to the obligation of opening the bank account in Poland, since these taxable persons will be able to open and hold the bank account in Poland free of charge. As at present, the taxable persons not established in Poland do not incur any additional costs in relation to the obligation to open a bank account in Poland and keep a VAT account. The VAT Act provides for a special system of compensations in case such entities would be charged by their banks for keeping the aforementioned accounts. In such a situation, the incurred costs are reimbursed by the competent tax authority at the request of the foreign taxable person.

Another significant advantage is that the taxable persons applying the split payment mechanism cannot , as a rule, be imposed the so-called VAT sanction in the form of an increased VAT liability, to be established by the tax authority (equivalent to 20%, 30% or 100% of the difference between the amount established by the tax authority and the original amount incorrectly declared by the taxable person). Furthermore, the entrepreneur applying the split payment mechanism cannot be charged with default interest for VAT debts at an increased rate (equivalent to 150%), accrued during the reporting period in which it used the mechanism to pay for at least 95% of its purchase invoices.

The so-called discount improves the financial liquidity of the taxable persons applying the split payment mechanism. It allows reducing the amount of VAT liability in case it will be paid in total from the VAT account before the final payment date. The discount amount is calculated according to a special formula. Such discount should not have an adverse impact on the Union’s own resources accruing from VAT.

Before the implementation of the special measure, there were 3,507 proceedings initiated due to the offences related to VAT extortions in 2018 and 3,389 proceedings in 2019 (a decrease by 118 year to year). In 2020, when the mandatory split payment mechanism became fully operational, the number of such proceedings amounted to 2,973, i.e. 416 less compared to the preceding year.

Before the entry into force of the mandatory split payment mechanism, the amount of budget losses due to VAT extortion was equal to PLN 5,168,779,146 in 2018 and PLN 4,716,202,928 in 2019 (a decrease by PLN 452,576,218 year to year). In 2020, the budget losses amounted to PLN 3,533,646,348, i.e. PLN 1,182,556,580 less compared to the preceding year (a decrease by nearly 25.1%).

Before the implementation of the derogating measure, the number of the initiated proceedings concerning VAT carousel fraud was 558 in 2018 and 277 in 2019 (a decrease by 281 year to year). In 2020, when the mandatory split payment mechanism was operational, the number of such proceedings amounted to 207, i.e. 70 less compared to the preceding year. It was also recorded during the analysed period that the identified budget losses due to VAT carousel frauds were on a gradual decrease. Before the entry into force of the mandatory split payment mechanism, the amount of the respective budget losses amounted to PLN 4,496,602,940 in 2018 and PLN 2,468,437,745 in 2019 (a decrease by PLN 2,028,165,195 year to year). In 2020, such losses amounted to PLN 1,107,992,201, i.e. PLN 1,360,445,544 less than in the preceding year (a decrease by almost 55.1%).

In 2019, the VAT revenue amounted to PLN 180,891.8 million (an increase by PLN 5,944.7 million compared to 2018). The preliminary data on the performance of the state budget in 2020 indicates that the revenue from the tax on goods and services went up compared to the preceding years irrespective of the spread of COVID-19 pandemic. In 2020, the VAT revenue amounted to PLN 184,551.9 million and were by PLN 3,660.1 million (by 2%) higher compared to the VAT revenue in 2019 , and accordingly by PLN 9,604.8 million (by 5.5%) higher compared to 2018 (PLN 174,947.1 million).

4. BUDGETARY IMPLICATIONS

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

5. OTHER ELEMENTS

The proposal includes a sunset clause; an automatic time limit.

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THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax[1], and in particular Article 395(1) thereof,

Having regard to the proposal from the European Commission,

Whereas:

(1) By letter registered with the Commission on 26 July 2021 Poland requested an authorisation to continue to derogate from Article 226 of the VAT Directive with regard to value added tax (VAT) invoicing requirements and to introduce the mandatory split payment mechanism for supplies of goods and services susceptible to fraud and generally covered by the reverse charge mechanism and joint and several liability in Poland. Poland requested the extension of the special measure for a period of three years, from 1 March 2022 to 28 February 2025.

(2) In accordance with Article 395(2) of the VAT Directive, the Commission informed the other Member States by letter dated 27 October 2021 of the request made by Poland. By letter dated 28 October 2021, the Commission notified Poland that it had all the information necessary to consider the request.

(3) Pursuant to Article 2 of Council Implementing Decision (EU) 2019/310[2], Poland submitted a report to the Commission on its overall impact on the level of VAT fraud and on the taxable persons concerned by letter dated 29 April 2021.

(4) Although Poland has taken numerous measures to fight fraud (e.g. the introduction of the reverse charge mechanism and of the joint and several liability by the customer, the introduction of the Standard Audit File, tighter rules for VAT registration and de-registration of taxable persons, increased number of audits, etc.), it considers that those measures are still insufficient to prevent VAT fraud.

(5) Poland introduced the voluntary split payment mechanism on 1 July 2018 and the mandatory split payment mechanism on 1 March 2019.

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[1] OJ L 347, 11.12.2006, p. 1.

[2] Council Implementing Decision (EU) 2019/310 of 18 February 2019 authorising Poland to introduce a special measure derogating from Article 226 of Directive 2006/112/EC on the common system of value added tax (OJ L 51, 22.2.2019, p. 19–27).

(6) The goods and services in the scope of the special measure are listed in the Annex in accordance with the Polish Classification of Goods and Services of 2015 (PKWiU 2015) which has replaced the Polish Classification of Goods and Services of 2008 (PKWiU 2008) from 1 July 2020. In PKWiU 2015 the symbols of the statistical classification and the editorial names of certain goods and services that appear in the Annex to Implementing Decision (EU) 2019/310 have been modified. That Annex should therefore be updated and replaced by the Annex to this Decision.

(7) The mandatory split payment model will continue to apply to the supplies between taxable persons, business-to-business (B2B) supplies, of goods and services listed in the Annex and will cover only electronic bank transfers. The obligatory split payment mechanism will continue to be applicable to all traders, including those traders who are not established in Poland.

(8) The report submitted by Poland confirmed that the mandatory split payment mechanism for supplies of goods and services susceptible to fraud brings effective results in the fight against tax fraud.

(9) Derogations are in general granted for a limited period of time to allow an assessment whether the special measure is appropriate and effective. The special measure should therefore be extended until 28 February 2025.

(10) Given the broad scope of the derogation, a report on the functioning and the effectiveness of the measure on the level of VAT fraud and on the taxable persons (regarding the refunds of VAT, the administrative burden, costs for taxable persons etc.) is to be submitted by Poland with in case of request to prolong the derogating measure.

(11) The special measure will not negatively affect the overall amount of tax revenue collected at the stage of final consumption and will have no adverse impact on the Union's own resources accruing from VAT.

(12) Implementing Decision (EU) 2019/310 should therefore be amended accordingly,

HAS ADOPTED THIS DECISION:

Article 1

Implementing Decision (EU) 2019/310 is amended as follows:

(1) in Article 2, the second subparagraph is replaced by the following:

'Where Poland considers that the extension of the measure referred to in Article 1 is necessary, Poland shall submit a request for extension to the Commission, together with a report on its overall impact on the level of VAT fraud and on the taxable persons concerned'.

(2) in Article 3, the date '28 February 2022' is replaced by the date '28 February 2025'.

(3) the Annex is replaced by the Annex to this Decision.

Article 2

This Decision is addressed to the Republic of Poland.

Done at Brussels,

For the Council
The President