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COMMUNICATION FROM THE COMMISSION TO THE COUNCIL

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

1. BACKGROUND

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

By letter registered with the Commission on 28 November 2017, Romania requested to introduce a special measure derogating from Title XI of the VAT Directive for the implementation of the VAT split payment mechanism for certain categories of persons. A number of exchanges took place between the Commission and Romania whereby the Commission asked for further clarifications and pointed Romania to a number of elements that the Commission considered disproportionate and difficult to justify. At the same time the Commission invited Romania to modify its request for derogation taking into account the concerns raised by the Commission. Romania, however, indicated it could not agree with the arguments and concerns presented by the Commission and refused to adapt its derogation request.

In accordance with Article 395(2) of the VAT Directive, the Commission transmitted the Romanian request to other Member States by letter dated 4 July 2018. By letter dated 5 July 2018, the Commission notified Romania that it had all the information it considered necessary for the appraisal of the request.

2. THE ROMANIAN REQUEST AND THE SPLIT PAYMENT MECHANISM

Romania submitted a request for derogation from Title XI of the VAT Directive to be authorized to impose a mandatory split payment mechanism on taxable persons and public institutions which have tax arrears or which are subject to insolvency proceedings. The split payment mechanism should apply to B2B transactions and should not apply to taxable persons falling under the exemption for SMEs. The split payment applies if the tax arrears are above RON 15 000 (around EUR 3 200) for large taxpayers, above RON 10 000 (around EUR 2 150) for medium taxpayers and RON 5 000 (around EUR 1 080 EUR) for other taxpayers and they are unpaid after 60 working days from the due date.

Romania started applying the split payment mechanism on 1 January 2018 without awaiting the Commission reply to its request.

The split payment mechanism is an alternative VAT collection system. Under the standard procedure, for a given transaction, a VAT taxable person collects the payment of the taxable base and VAT (if applicable) from its client (or a third party). The VAT taxable person then reports this transaction in its periodical VAT return. Depending on the outcome of the VAT return, VAT is due by the taxable person or it could be refunded. If VAT is due, the VAT taxable person pays the VAT to the tax

authorities of its Member State on a defined periodical basis (monthly, quarterly, etc.).

The use of the split payment introduces a change as a split is made between the payment of the VAT amount due and the taxable amount. In case of Romania, the purchaser pays the taxable amount to the supplier, whereas it pay the VAT due on this supply not directly to the supplier but to a VAT account at the Romanian Treasury or at a Romanian financial institution.

According to Romania, the special measure is requested in order to increase the collection of VAT and to combat VAT evasion, by increasing the voluntary compliance to VAT payment by taxable persons. Romania considers that the application of the VAT split payment will stop the fraud whereby some economic agents do not transmit the VAT received from customers to the tax authorities.

3. THE COMMISSION'S VIEW

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

The split payment mechanism is not a common system of payment of VAT but rather a novelty. There is a growing interest in the mechanism among Member States who regard it as a tool to help them in the fight against VAT fraud. Different designs of such split payment model are possible and every model needs to be assessed separately in order for the Commission to conclude that it can be justified based on Article 395 of the VAT Directive.

The Commission takes the view that certain elements of the Romanian split payment model raise serious concerns regarding their proportionality.

The Romanian split payment system is applicable to taxable persons and public institutions which have tax arrears above given thresholds or which are subject to insolvency proceedings. The Commission considers that defining the thresholds at a fixed level for three categories of taxable persons does not ensure the equal treatment of taxable persons within the same category. It is a fact that the threshold of RON 15 000 would not have the same impact for all large taxpayers or the threshold of RON 5 000 will not have the same impact for all small taxable persons given the differences within these groups. The Commission therefore considers that the proportionality of such system of fixed thresholds cannot be justified and that a threshold linked to a percentage of the turnover could be a better criterion.

Furthermore under the Romanian split payment system the customer is obliged to verify the register of taxable persons to which the split payment applies and act accordingly, meaning split the net amount and the VAT amount. At the same time the notification about the inclusion in the register is sent by the tax authorities to the

supplier and not to the customers. Romania does not consider it necessary that the supplier informs the customer of the necessity to apply the split payment mechanism by including an appropriate mention on the invoice. Moreover, if the customer does not apply the split payment mechanism and pays VAT to another account than the VAT account of the supplier, a penalty of 0.06% per day of the amount wrongly paid is imposed on the customer, if not corrected within 30 working days. However, it is the supplier (and not the customer) who can correct the situation and transfer the sum in question from its main account to its VAT account and inform his customer of this, thereby avoiding any sanctions on the customer. Romania clarified that such transfer by the supplier is only a possibility, not an obligation, as the responsibility for paying VAT into the correct VAT account remains with the customer.

Such split payment system puts an unjustifiable and disproportionate burden on the customer. Even if the obligation for the customer to consult the register of taxable persons falling under the split payment mechanism were maintained, the supplier should at least be obliged to inform the customer of the obligation to apply the split payment mechanism by including a mention on the invoice. Since Article 226 of the VAT Directive enumerates the details which are to be included on the invoice, the inclusion of an additional mention requires a derogation from this Article. However, by letter of 17 May 2018 Romania informed the Commission that it considers unnecessary the inclusion on the invoice of a reference to the application of the split payment mechanism.

The penalty imposed on the customer in case of the non-application of the split payment is in the Commission's view disproportionate, in case the supplier remains liable for the payment of VAT[1]. Such penalty should rather be imposed on the supplier, particularly in the view that the supplier can at any time correct the mistake by transferring the VAT received to his VAT account.

It should be noted that Article 273 of the VAT Directive allows Member States to impose other obligations which they deem necessary for the correct collection of VAT and for the prevention of evasion. However, the proportionality test also applies to the measures adopted under that Article.

In light of the above, the Commission considers that the Romanian split payment mechanism is not proportionate to the objectives pursued, namely those of ensuring the correct collection of VAT and preventing tax evasion.

The Commission informed Romania that the obligation for non-established traders to open a bank account with a Romanian financial institution would not be compatible with Article 56 TFEU on the free movement of services. The Commission also suggested that Romania could instead oblige such traders to open an account with the Treasury, but that would need to be available also in foreign currency. By its reply, Romania restated that it is not possible to make payments in foreign currency by using a Treasury account.

The Commission requested Romania to address its concerns on the proportionality of the above elements of the split payment system and to modify the split payment

[1] Romania informed the Commission that there is no change of liability and it is the supplier who remains liable for the payment of VAT.

mechanism accordingly. However, Romania did not react positively to the Commission's requests.

4. CONCLUSION

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