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4 January 2013

Mr. Donato Raponi
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VAT and other turnover taxes – Unit C1
Rue Joseph II 79, Office J79 05/093
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Via email: Donato.Raponi@ec.europa.eu

Subject: **VAT refunds in the EU**

Dear Mr. Raponi,

With alarming and increasing frequency a number of Member States have refused to refund VAT to businesses that are in a repayment position. This failure threatens the neutrality of the VAT system in the EU, violates provisions of Directive 2006/112/EC (the VAT Directive), and negatively affects the cash flow of companies doing business in Europe by disrupting their supply chains. Tax Executives Institute urges the Commission to communicate the concerns of international businesses described in this letter to the authorities of the relevant Member States and to take appropriate measures to ensure these Member States comply with their obligations under the EU VAT regulations, respect fundamental VAT principles, and refrain from conduct that undermines the proper functioning of the Internal Market. This letter amplifies TEI's comments on the Commission's Green Paper, *On the future of VAT: Towards a simpler, more robust and efficient VAT system*, which were submitted on 31 May 2011.

Tax Executives Institute

Tax Executives Institute (TEI) was founded in 1944 to serve the professional needs of in-house tax professionals. In 1999, TEI chartered a chapter in Europe, which encompasses a cross-section of European and multinational companies. Today the organisation has 55 chapters throughout the world. As the preeminent international association of business tax professionals, TEI has a significant interest in promoting sound tax policy, as well as in the fair and efficient administration of the tax laws, at all levels of government. Our nearly

7,000 members represent 3,000 of the largest companies in Europe, the United States, Canada, and Asia.

TEI members are accountants, lawyers and other corporate and business employees responsible for the tax affairs of their employers in an executive, administrative, or managerial capacity. The Institute espouses organisational values and goals that include integrity, effectiveness and efficiency, and dedication to improving the tax system for the benefit of taxpayers and tax administrators alike.

Background on the Right to a Refund of Overpaid VAT

VAT is a transaction-based tax designed to tax final consumption. The fundamental principle of the VAT is that it is borne by the final consumer rather than any of the intermediaries in the supply chain. Thus, to the extent businesses act as the tax collector on behalf of governments (rather than as a consumer), neutrality is critical. This principle of neutrality is codified in EU law at Title X of the VAT Directive and also serves as an international norm for VAT (*e.g.*, the OECD's International VAT/GST Neutrality Guidelines, which were approved by the Committee on Fiscal Affairs of the OECD in July 2011). The principle of neutrality is also critical to the proper functioning of the Internal Market.

The right of businesses to recover VAT incurred on their purchases of taxable business inputs (as well as on imports and intra-EU acquisitions) ensures the neutrality of the VAT system. The European Court of Justice has recognized the importance of VAT neutrality, holding that it "is a fundamental principle of the common system of VAT established by the relevant European Union legislation."[1] Subject to certain limitations and conditions, EU law grants the right to recover VAT on business inputs both to businesses VAT-registered in the country where the VAT is incurred and to businesses VAT-registered (or assimilated) in other countries.

Specifically, article 167 of the VAT Directive gives businesses the right to immediately deduct input VAT. And, when those deductions exceed the amount of VAT otherwise due (*i.e.*, creating a VAT-credit position), article 183 requires Member States to permit registrants to carry the excess deductions forward to the following period, or issue a refund under conditions determined by those Member States. The European Court of Justice has consistently interpreted article 183 as requiring Member States to refund overpaid VAT within a reasonable period of time by a payment in liquid funds or equivalent means without any financial risk for the businesses entitled to refunds.[2]

Member States clearly have a legitimate need to review VAT claims before issuing a refund to combat tax evasion, especially when the refund is claimed by a foreign business with little connection to that Member State. At the same time, under the doctrine of proportionality, Member States are obliged to employ procedures to identify fraud and

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[1] Case C-588/10, *Poland v. Kraft Foods Polska SA* [2012], *citing* Case C-330/95 *Goldsmiths* [1997] ECR I-3801, paragraph 21; Case C-566/07 *Stadeco* [2009] ECR I-5295, paragraph 39 and the case-law cited therein; and Case C-489/09 *Vandoorne* [2011] ECR I-0000, paragraph 27.

[2] Case C-78/00 *Commission v Italy* [2001] ECR I-8195, paragraphs 33 and 34; Case C-25/07 *Sosnowska* [2008] ECR I-5129, paragraph 17; and Case C-107/10 *Enel Maritsa Iztok 3* AD [2011] ECR I-0000, paragraph 33.

evasion that do not undermine other overarching objectives of EU law, such as the principle of neutrality. As the European Court of Justice recently stated, "In particular, such conditions must enable the taxable person, in appropriate circumstances, to recover the entirety of the credit arising from that excess VAT."[3]

Although the VAT Directive does not define what constitutes a reasonable period of time to issue a refund, a fair interpretation of the VAT rules requires that the refund occur within a few months. The European Court of Justice has validated that reading of the VAT Directive on numerous occasions. Thus, when no shorter deadline is provided for in the Member State's law, TEI submits that the timeframes in articles 19 to 22 of Directive 2008/9/EC, which vary between 4 and 7 months (depending on whether the refunding Member State needs to request additional information to substantiate the refund request) should be considered as a maximum allowable period for the refund of any VAT credit.

EU law also prohibits Member States from creating unreasonable administrative hurdles that effectively bar or significantly delay the payment of VAT refunds. These unjustifiable obstructions and the outright refusal by Member States to issue refunds undermine the principle of neutrality. As the European Court of Justice has observed, "It is also apparent from case-law that measures to prevent tax evasion or avoidance…must have as little effect as possible on the objectives and principles of the VAT Directive and may not therefore be used in such a way that they would have the effect of undermining VAT neutrality."[4]

The refusal to pay refunds of overpaid VAT (or to unreasonably delay such payments) interferes with the principle of neutrality critical to the effective functioning of the EU VAT system and thus erodes the confidence of businesses in the administration of the VAT by the Member States. These negative effects are often amplified as a result of the reverse charge mechanism. Non-registered, non-resident suppliers are confronted with VAT refund positions if they make local purchases or non-EU imports in combination with sales on which they cannot charge VAT. This situation has caused businesses to alter their business decisions to minimize activities in, and thus exposure to, recalcitrant Member States. This obviously constitutes a serious infringement of the rights granted by the VAT Directive and inhibits the proper functioning of the Internal Market.

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[3] Case C525/11, *Mednis SIA v Valsts ieņēmumu dienests* [2012] ECR I-0000, paragraph 24. *See also*, Case C-274/10 *Commission v. Hungary* [2011] ECR I-0000, paragraph 45:

> As regards the possibility, under Article 183 of the VAT Directive, of providing that excess VAT is to be carried forward to the following tax period or refunded, the Court has made it clear that, the conditions for the refund of excess VAT cannot undermine the principle of fiscal neutrality by making the taxable person bear the burden of the VAT in whole or in part. In particular, such conditions must enable the taxable person, in appropriate circumstances, to recover the entirety of the credit arising from that excess VAT. This implies that the refund is made within a reasonable period of time by a payment in liquid funds or equivalent means, and that, in any event, the method of refund adopted must not entail any financial risk for the taxable person. (Citations omitted.)

[4] Case C-588/10, *Poland v. Kraft Foods Polska SA* [2012], paragraph 28.

TEI members who work for businesses with operations throughout the EU experience significant delays in obtaining refunds of overpaid VAT, even when there is no question that the refunds are due and payable. These delays can last for years with significant effects on the cash flow of those businesses. To illustrate how the actions of Member States have impeded the proper functioning of the VAT system in the EU, TEI members have prepared the following examples divided into two groups: (1) situations where the Member States have delayed payment of VAT refunds; and (2) the creation by Member States of over-burdensome administrative requirements for claiming refunds.

Selected Examples from Businesses Experiencing Extreme Delays in Obtaining Recovery of Overpaid VAT from Member States

Delays by Member States in Issuing Refunds

Below are some examples of situations where multinational businesses employing TEI members have faced unreasonable delays in obtaining VAT refunds with respect to claims that have been duly filed and not rejected:

Greece: Businesses not established in Greece have still not received refunds of VAT credits for claims timely filed between 2008 and 2011 that have never been rejected or challenged by the Greek revenue authorities.

Greece: Businesses established in Greece have had to wait up to six years to obtain refunds of Greek VAT credits, even after the businesses satisfactorily addressed numerous questions raised by the Greek authorities about the claims.

Italy: Businesses not established in Italy but having a VAT registration in Italy have waited more than three years to obtain a refund of their Italian VAT credits. The Italian revenue authorities allow these businesses to file quarterly VAT refund claims for the first three quarters of the calendar year and to claim the VAT credit for the fourth quarter together with the annual VAT return. These businesses report that Italian revenue authorities routinely engage in a detailed audit of every quarterly refund claim even when the taxpayer had an untarnished record of compliance. This unnecessarily granular review of businesses with low risk profiles delays refunds between six and eight months. Additionally, businesses routinely wait two and three years for refunds claimed for VAT credits in the last calendar quarter.

Italy: Businesses not established in Italy reclaiming VAT via the 8th or the 13th Directive have waited more than three years before the Italian revenue authority issued refunds of their Italian VAT credits in Italy.

Over-Burdensome Processes and Conditions Related to Applications for Refunds

Below are some examples of unreasonable administrative conditions imposed on businesses that make it excessively difficult to obtain VAT refunds from Member States:

General: Some Member States (*e.g.*, Austria, Hungary, Poland, and Romania) correspond exclusively in their own language, and require all documentation submitted to substantiate VAT claims to be translated by a certified translator. This

requirement complicates communication and disproportionately increases the costs of compliance in relation to the risk of fraud and evasion.

Germany: German tax authorities have rejected refund claims because they were not convinced that the persons signing the VAT refund claim on behalf of the business had authority to do so. In this respect, TEI welcomes the Commission's recent reasoned opinion requesting that Germany change its rules for VAT refunds under the 13th Directive, more particularly the rule requesting VAT refund applications be personally signed.

Hungary: The Hungarian tax authorities have requested that the taxpayer produce all contracts related to the transactions underlying a VAT refund claim, as well as statements from both the supplier and its client regarding the purposes of the supplies. The authorities also informed the business that the claim would have a better chance of being accepted if the taxpayer translated all the agreements into Hungarian.

Italy: Italian law allows non-established businesses that are VAT registered in Italy to file quarterly VAT refund claims for the first three quarters of the calendar year, and to file VAT refund claims for the fourth quarter together with the annual VAT return. Regrettably, businesses utilizing this procedure have experienced that every quarterly refund claim is audited (regardless of a business's compliance history). These audits can last between six and eight months resulting in significant delays in the payment of related refunds. Moreover, the revenue authority systematically requests bank guarantees, which creates additional and sometimes disproportionate costs in relation to the application of VAT refunds.

Poland: The Polish tax authorities rejected a VAT refund claim solely because the invoices underlying the claims were issued in the name of a division of a company rather than the formal name of the company appearing in the commercial register. Polish revenue authorities have rejected another claim because they did not understand the way in which signatures were authorized in the country where the taxable person was established. In these cases, the tax authorities have required a signature from one of the people listed as a representative of the company in the commercial register even though the person who originally signed the return had clear authority to do so.

Romania: The Romanian tax authorities have rejected refund claims because the taxpayer filed its request for reconsideration on a document entitled a "request for reconsideration" instead of "appeal."

Request

The Member States identified in the prior section have deprived businesses of their right to a refund of overpaid VAT by refusing to timely pay refunds and imposing burdensome administrative procedures to significantly delay the issuance of refunds. These actions violate the principle of neutrality and interfere with the proper functioning of the Internal Market. TEI acknowledges the efforts of the Commission over the years to encourage Member States to correctly apply the EU rules governing the right to recover

overpaid VAT, such as the actions of the Commission against Luxembourg (Case C-90/05), Italy (Case C-287/91), and Spain (Case C-16/95).

TEI urges the Commission to once again take necessary actions against Member States that do not respect the fundamental right of businesses to recover overpaid VAT. TEI remains at the disposal of the Commission to elaborate on the problems encountered by businesses.

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This letter was prepared by TEI's European Indirect Tax Committee. If you have any questions about TEI's comments, please contact Daniel B. De Jong of the Institute's legal staff at +1 202 638 5601 (or ddejong@tei.org).

Respectfully submitted,

Tax Executives Institute

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