VAT ENFORCEMENT BY THE ROMANIAN TAX AUTHORITIES IN THE CONTEXT OF THE UNIFORM IMPOSITION OF VAT IN THE EUROPEAN UNION

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Abstract

VAT enforcement by the Romanian tax authorities has recently been discussed by the European Court of Justice in a preliminary ruling concerning the correct imposition of VAT and the taxpayers' rights in challenging the said decision to impose. Since Romania is a member of the European Union it is obliged to comply with the European regulations in place, in this case being the Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax, as it was modified by the Council Directive 2010/45/EU of 13 July 2010 amending Directive 2006/112/ EC on the common system of value added tax as regards the rules on invoicing. The Romanian tax authorities, when controlling taxpayers, if the latter request a VAT reimbursement, have the right to impose a control on the taxpayers' activity that generated the said reimbursement. Furthermore, when controlling the activity of a taxpayer, the National Agency for Fiscal Administration has the right to extend the said control to any and all activities and reports that entail and are relevant to the imposition. While the context is understandable, and a larger control is sometimes required in order to prevent possible tax evasion and an illegal VAT reimbursement, one must understand that such a control must not, in any circumstance lead to an abusive control or an abusive imposition.

Keywords: *VAT, Council Directive 2006/112/EC, Council Directive 2010/45/EU, European Court of Justice, National Agency for Fiscal Administration (NAFA).*

JEL Classification: K33, K34

1. Introduction

The value added tax (VAT) was first regulated in 1954. By the initiative of Maurice Laure, France was the first state in what is now known as the European Union that implemented VAT, and thus was the first to experience the effects of the application of this tax in economy. Later, starting with the year 1967, VAT was introduced in other countries of the old continent, by a common taxation project, and replacing the old "tax on the turnover" of companies.

The main cause why different taxes perceived on the turnover were replaced with the unique tax of the VAT was the goal to use one, unique tax that was to be perceived in all stages of production, and that was to be implemented by the suppliers and latter could be deduced.

VAT is qualified as one of the most fast-growing taxes in the world, as it has been adopted in over 120 countries and is a key source of government revenue. In early 2000, VAT affected about 4 billion people, then about 70% of the world's population, and raised roughly one-quarter of all government revenue[2].

The European legislator wished first for the harmonizing of the regulations regarding the applicability of the VAT regime in all ex-communist countries and today regulates a common VAT standard, implemented by Directive 2006/112/CE and Directive 2010/45EU, for all member states.

In Romania, the Văcăroiu government (first prime minister after the fall of the communist regime) decided the implementation of VAT in 1992, and thus repealed the "tax on the circulation of merchandise". The introduction of VAT in Romania generated on one hand a raise in consumer prices, but also stimulated exportations and investments. While not listing all of the transformations to which the VAT was subjected over the years, we underline that the main and most significant changes that occurred to VAT in Romania were due to its accession to the European Union.

In this context, Romania obliged, among others, to respect the Community acquis in the VAT field, as well as the decisions of the European Court of Justice. The rulings of the latter must be followed by the national fiscal administration, in order to uniformly apply the VAT regulations,

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[2] Liam Ebrill, Michael Keen, Jean-Paul Bodin, Victoria Summers, *The Modern VAT*, "International Monetary Fund", 2001, x.

without disregarding the particularities of each case.

Any state, whether talking about the European Union or the world needs to impose taxes in order to function properly. Traditionally, there are two types of taxes that may be imposed: (i) direct taxes and (ii) indirect taxes.

Indirect taxes are collected by the sale of goods and/or services; in general, value added taxes are considered to be consumption taxes that are collected by taxable persons on a transaction basis, i.e. upon the supply of goods and services, which is also why, as noted already, they are, without exception, classified as indirect taxes[3]. The particularity of value added taxes is that they are strictly speaking not imposed on the addition of value to products and services by taxable persons, but on the consumption, or rather acquisition of the products and services by the end consumer[4]. This principle has also been reaffirmed by the European Court of Justice as it underlined "It is to be remembered that the basic principle of VAT is that it is a consumption tax designed to be borne only by the final consumer. VAT is precisely proportional to the price of the goods and services and it is collected by taxable persons at each stage of the production or distribution process on behalf of the tax authorities, to which they are required to pay it. In accordance with the basic principle of that system and the detailed rules for its operation, the VAT to be levied by the tax authorities must be equal to the tax actually collected from the final consumer."[5]

We may say that VAT is one of the most important taxes in the category of indirect taxation. VAT is seen as a key instrument for securing macro-economic stability and growth by placing domestic revenue mobilization on a sounder basis, so that the International Monetary Fund (IMF) has attached considerable importance to its proper design and implementation.[6]

In the European Union, VAT is regulated and implemented in the same manner in all member states. The directive sets out to establish a common system of VAT, that will be applied to all goods and services. On each transaction, VAT shall be calculated on the price of the goods or services at the rate applicable to such goods or services, and shall be chargeable after deduction of the amount of VAT borne directly by the various cost components. The common VAT system will apply to all retail and trade stages.

At this point, some clarifications are needed: even though VAT should apply to all types of economic activities, as it is a general tax on consumption, the decision was made in the 1960 by the EU legislator to exclude some consumption from the tax base, for two essential reasons – first, in order to replicate exclusions from previous cumulative taxes and second, to reflect the existence of technical obstacles to the application of VAT to some services, the so-called difficult to tax services[7].

The European Court of Justice when interpreting and ruling in case laws pertaining to the application of community VAT also takes into account the main principles that regulate VAT. The traditional EU VAT principles are the neutrality principle and the principle of VAT as a general consumption tax. Both of them have been developed by the Court as the main principles of VAT, from which by jurisprudence were deduced other principles such as: the principle of legal certainty, equivalence principle and the effectiveness principle. It is important to note and understand these principles as to further understand the interpretation and rulings of the Court in all its aspects. Thus, we propose the following definitions of these principles that were established and developed by jurisprudence.

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[3] Marie Lamensch, *European Value Added Tax in the Digital Era. A critical analysis and proposals for reform.* "IBFD Doctoral Series", December 2015, p.11.

[4] Liam Ebrill, Michael Keen, Jean-Paul Bodin, Victoria Summers, *op. cit.* (2001), 1.

[5] *MyTravel plc v Commissioners of Customs & Excise*, case C-291/03, 6 October 2005, European Court of Justice, "Reports 2005 I-08477", paragraph 30.

[6] Liam Ebrill, Michael Keen, Jean-Paul Bodin, Victoria Summers, *op. cit.* (2001), x.

[7] Rita de la Freia, *EU VAT Principles as Interpretative Aids to EU VAT Rules: The Inherent Paradox*, "M. Lang et al (eds), Recent VAT Case Law of the CJEU (Linde, 2016)", December 2016, p. 3, available online at http://dx.doi.org/10.2139/ssrn.2718107, last accessed at 10.09.2020.

2. Principles pertaining to VAT in the European Union

2.1. The neutrality principle

The first principle, that of the neutrality of the VAT is firstly mentioned by the EU Council Directive 2006/112/EC (herein after the VAT Directive). It speaks of the said principle in its preamble in considerations 5 and 7 as "a VAT system achieves the highest degree of simplicity and of neutrality when the tax is levied in as general a manner as possible and when its scope covers all stages of production and distribution, as well as the supply of services" and "the common system of VAT should, even if rates and exemptions are not fully harmonised, result in neutrality in competition, such that within the territory of each Member State similar goods and services bear the same tax burden, whatever the length of the production and distribution chain."

The court further developed the principle of neutrality in several cases, from which we cite C-255/02 decision in the case of Halifax[8]. The Court in its 78 consideration holds that "… it must be borne in mind that the deduction system under the Sixth Directive is meant to relieve the trader entirely of the burden of the VAT payable or paid in the course of all his economic activities. The common system of VAT consequently ensures complete neutrality of taxation of all economic activities, whatever their purpose or results, provided that they are themselves subject in principle to VAT". Thus, the neutrality principle is to be applied to all categories of transactions provided that those transactions do not constitute an abuse of rights by the tax payer.

The same ruling of the Court provides that a practice will be qualified as abusive if the sole purpose of the transaction is that to become a tax advantage and to elude the provisions of the legislation in force: "for it to be found that an abusive practice exists, it is necessary, first, that the transactions concerned, notwithstanding formal application of the conditions laid down by the relevant provisions of the Sixth Directive[9] and of 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."[10]

At a legislative level, the principle of neutrality is to be deduced of articles 167 and following of the VAT Directive, that impose that all transactions grant a right of deduction at the time the deductible tax becomes chargeable.

The Court affirmed the its position that any persons is entitled to deduce entirely their VAT burden throughout the years by several decisions such as Midland Bank[11] (case 98/98, paragraph 19), Abbey National[12] (case 408/98, paragraph 24), Construction Danmark[13] (case 174/08, paragraph 27) or RBS Deutschland Holdings[14] (case 277/09, paragraph 38). These companies acted in the financial banking system, having a pro-rata right of deduction, therefore a limited right to deduce their VAT, had set up subsidiaries that only undertook activities outside the financial banking domain, for which they would have the right to deduce integrally the VAT. Their national fiscal authorities declined their right to deduce the VAT of the companies. The Court ruled that according to the principle of neutrality, there is no right to limit or annul the right to deduce VAT as long as the imposable person demonstrated the use of the acquisitions of goods and services for the delivery of other goods and services that have the right to completely deduce VAT.

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[8] *Halifax plc, Leeds Permanent Development Services Ltd and County Wide Property Investments Ltd v Commissioners of Customs & Excise*, case C-255/02, 21 February 2006, European Court of Justice, "European Court Reports 2006 I-01609*"*.

[9] Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes - Common system of value added tax: uniform basis of assessment, in force until the 31.12.2006, repealed by the VAT Directive

[10] Halifax ruling, paragraph 86.

[11] Commissioners of Customs and Excise v Midland Bank plc., case C-98/98, 8 June 2000, European Court of Justice, "European Court Reports 2000 I-04177".

[12] *Abbey National plc v Commissioners of Customs & Excise*, case C-408/98, 22 February 2001, European Court of Justice, "European Court Reports 2001 I-01361".

[13] *NCC Construction Danmark A/S v Skatteministeriet*, case C-174/08, 29 October 2009, European Court of Justice, Official Journal C 312, 19.12.2009.

[14] *The Commissioners for Her Majesty's Revenue & Customs v RBS Deutschland Holdings GmbH*, case C-277/09, 22 December 2010, European Court of Justice, "European Court Reports 2010 I-13805".

The last case that we shall cite on this topic is the SMS Group Gmbh[15] (case 441/16), that opposes the Bucharest fiscal administration and a private moral person. The case is a preliminary ruling sent in by the High Court of Cassation and Justice of Romania, in which a private person, that was not a moral person incorporated in Romania, but in Germany, imported some goods from Turkey for a third party. The importation was concluded during a time in which the sales agreement was suspended for reasons beyond SMS Group's control, financial difficulties of the third party. The company filed for a VAT refund even if the transaction for which the goods were intended was never carried out and the Group never provided a concrete explanation of the subsequent movement of goods, i.e. information on the destination or date of the future sale (that was meant to be an exportation). In this context, the national authority refused to refund the said VAT. The European Court held that the right to deduce VAT is not conditioned by completing the transaction for which the goods were purchased, nor is it constrained by the proof of subsequent movement of goods (paragraphs 56 and 57 of the ruling). Thus, VAT Directive could not be interpreted as to limit the right to a reimbursement of VAT. The Court further underlined that the deduction system, as well as the refund system, seek to entirely relieve the VAT burden payable or payed by the operator, in all areas of its activity, thus perfectly guaranteeing the neutrality of the taxation, regardless of the purpose or results of the activity performed, under the one condition that the mentioned activity be in its turn subjected to VAT (paragraph 40 of the ruling).

2.2. The principle of legal certainty

This principle is to be read in conjunction with the principle of protection of legitimate expectations of the taxpayer. As this principle doesn't enjoy the same recognition as the principle of neutrality, meaning it has no mention in any on the VAT Directives, we shall underline some rulings of the European Court of Justice, in order to illustrate it. We believe that the principle has its roots in the general theory of law and its base principles, that state that a law must first be predictable in order to allow a person to know what outcome will come from a specific fact or action.

The principle of legal certainty aims towards drafting clear and precise legal rules, that shall not lead to arbitrary interpretations. By instating this principle taxpayers can understand, foresee and anticipate the fiscal burden that they shall be subjected to, and in the same time can properly manage and determine better administrative solutions for their businesses.

The first case that we shall be analysing is that of BLP Group plc[16], where a British holding company sold its shares in a German subsidiary and demanded the reimbursement of VAT for the supply of legal and financial services related to the sale. The European Court ruled that deduction is to be permitted only on supplies directly linked to taxable transactions, because if the contrary were to be permitted, the tax authorities might have to undergo investigations in order to determine the taxpayers' intentions. The last assumption would be contrary to the common VAT system and would contradict the principle of legal certainty. Thus, the Court held that VAT paid for services for an exempt transaction was not deductible, even if the ultimate purpose of the exempt transaction was a taxable transaction, except for the cases expressly listed by EU provisions.

Another case that can be used in order to illustrate this principle is the Salomie and Oltean[17] case law, on the reclassification of a transaction by the fiscal authority as an economic activity subject to VAT. In this case, two natural persons, created a partnership that had no legal personality and was not declared or identified as being subject to VAT, alongside five other natural persons. Between 2008 and 2009, they built and sold 132 apartments, without these transactions being subject to VAT. Following a fiscal inspection in 2010, the fiscal authority declared that those transactions constituted

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[15] *SMS group GmbH v Direcţia Generală Regională a Finanţelor Publice Bucureşti*, case C-441/16, 21 September 2017, European Court of Justice, not yet published, the document is available online at http://curia.europa.eu/juris/liste.jsf?num=C-441/16&language=EN, last accessed at 09.09.2020.

[16] *BLP Group plc v Customs and Excise Commissioner*, case C-4/94, 6 April 1995, European Court of Justice, "European Court Reports 1995 I-0098".

[17] *Radu Florin Salomie and Nicolae Vasile Oltean v Direcţia Generală a Finanţelor Publice Cluj*, case C-183/14, 9 July 2015, European Court of Justice, "Electronic Reports of Cases (Court Reports – general)".

a continuous economic activity and therefore should have been subjected to VAT, starting with the year 2008, as since the transactions exceeded 35.000 euros per year. In consequence, the tax authority issued tax demands for payment of VAT and default interests. The natural persons sought a preliminary ruling, questioning whether the principles of legal certainty and protection of legitimate expectations are in accordance with the imposition of further taxation of a national person, if the national tax authority had already levied the person for the tax on the income deriving from the transfer of ownership of properties forming part of his personal wealth. Can a tax authority review its position, in the same legal framework and on the basis of the same facts and reclassify the same transactions as subject to VAT, furthermore demanding retroactively calculated taxes?

The Court started by defining the principles of legal certainty and states that not only EU rules must be "certain and its application foreseeable by those who are subject to it", especially in cases that entail financial consequences, but also the legislation of Member States must be "worded unequivocally so as to give the persons concerned a clear and precise understanding of their rights and obligations and to enable national courts to ensure that those rights and obligations are observed" (see paragraphs 31 and 32 of the Court decision). The Court continues to analyse the national provisions and explains that the ground rules of an economic activity and the VAT tax exemption are sufficiently clearly explained and need no further development. The fact that the taxation in such cases is not a regular practice on the part of the fiscal administration should not give rise in the mind of a prudent and well-informed trader, that the transaction is not going to be submitted to VAT. Thus, the Court considers that the transactions can be requalified and do not prejudice the mentioned principles.

Regarding the surcharges applied by the national tax authority, the Court underlines that there is no harmonisation in EU legislation in the field of penalties pertaining to noncompliance and that Member States have the power to choose the penalties that seem appropriate. Nevertheless, the Member States' decisions must be bounded by the principle of proportionality. Thus, the Court concluded that "the principles of legal certainty and of the protection of legitimate expectations do not preclude, […] a national tax authority from deciding, following a tax audit, to subject transactions to VAT and to impose the payment of surcharges, provided that that decision is based on clear and precise rules and that that authority's practice has not been such as to give rise, in the mind of a prudent and well-informed trader, to a reasonable expectation that that tax would not be levied on such transactions, […]. The surcharges applied in such circumstances must comply with the principle of proportionality" (paragraph 53).

2.3. The principle of proportionality

The fiscal tax authorities have the right to ascertain the taxpayers' ways of complying with the legal provisions in order to prevent the possible abuses and/or infringements of in force regulations. Nevertheless, the Member States, by their national fiscal authorities, must resort to means that although allow an efficient control and prevention of fiscal fraud or tax evasion, must not prejudice the objectives and principles set out by the Community rules or legislation.

The principle of proportionality is one of the general principles of EU law that also comes into play when discussing a taxpayers' rights. Under this principle, the scope and form of the action undertaken by the European Union, its institutions and Member States must not exceed what is necessary in order to fulfil the objectives of the Treaties on which the Union is formed.

It cannot be said that the principle of proportionality fulfils the conditions for it to be recognized as jurisprudential doctrine. Nevertheless, it plays an important role in the interpretation of tax law provisions[18], especially when it comes to interpreting European VAT, and alleged frauds on this tax. The principle of proportionality is more often than not applied in conjunction with the principle of neutrality.

[18] Artur Mudrecki, *The principle of proportionality in value added tax*, "XVI International Scientific Conference "the optimization of Organization and Legal Solutions concerning Public Revenues and Expenditures in Social Interest", Vilnius", Temida 2, 2018, p. 639.

The European Court of Justice, in a historical decision[19], ruled that the prohibition to deduct VAT as charged for non-existent (arguably fraudulent) transactions is a conundrum of the neutrality principle; yet, neutrality *per se* is not a dogma of VAT implementation, and it must be interpreted consistently with the principle of proportionality in a delicate balance of the two[20], in order to make the deduction system of the VAT applicable to almost all cases and thus be in accordance with its scope.

The principle of the common system of VAT encompasses the application of a general consumption tax exactly proportional to the price of goods and services, irrespective of the number of transactions which occurred in the production and distribution process prior to the stage at which the tax is collected, thus the determination of the appropriate tax base being influenced by the principle of proportionality[21].

The principle of proportionality is often mentioned in cases concerning the right to deduct VAT, as it is reminded to Member States that in accordance with this principle, they must employ means which, while enabling them to effectively attain the prevention of possible tax evasion, avoidance and abuse and protecting their financial interests, are the least detrimental to the objectives and principles laid down by the relevant Community legislation, which include the fundamental right to deduct VAT[22].

In this optic, the European Court ruled in another case, the EN.SA., that even though VAT can't be deduced in the case of a fraudulent operation, the neutrality is to be preserved even when the operation invoiced did not actually take place, if very specific circumstances are met: namely, that no loss for the national budget occurred, that the company invoiced was not actually planning to erode its tax liability for VAT purposes and that the non-existent operation was simulated for other commercial purposes (not directly affecting the tax due). This conclusion is made possible making the principles of proportionality (and reasonableness) to prevail over a mechanical application of the tax that would otherwise prevent the right to deduct the tax charged.[23]

Thus, we may say that the principle of proportionality plays a huge role in the interpretation of Community regulations as well as in the jurisprudence of the European Court, having a fundamental impact on national legislation and preserving the right of taxpayers to deduce VAT, thus upholding the uniform application of the VAT Directives.

2.4. The principle of effectiveness

The principle of effectiveness is also called by scholars the principle of effective judicial protection and draws its basis from article 19 paragraph 1, second thesis of the Treaty of the European Union as "Member States shall provide remedies sufficient to ensure effective legal protection in the fields covered by Union law." In other words, Member States must warrant that EU provisions are not impossible or excessively difficult to enforce in practice.

This principle covers national remedies, procedure rules as well as the access granted by Member States to national and international courts. What should be noted, that as far as VAT regulations are concerned, this principle is almost always invoked in the absence of a Community

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[19] *EN.SA. Srl v Agenzia delle Entrate – Direzione Regionale Lombardia Ufficio Contenzioso, case C-712/17, 8 May 2018, European Court of Justice, "Electronic Reports of Cases (Court Reports – general)".*

[20] Marco Greggi, *Neutrality and Proportionality in VAT: Making Sense of an (Apparent) Conflict*, "Intertax", Volume 48, Issue 1, 2020, p. 122.

[21] Artur Mudrecki, *op. cit.* (2018), p. 636-637.

[22] *Alicja Sosnowska v Dyrektor Izby Skarbowej we Wrocławiu Ośrodek Zamiejscowy w Wałbrzychu,* case C-25/07, 10 July 2008, European Court of Justice, "Reports of Cases 2008 I-05129", paragraph 23. The Court expressed the same opinion in paragraphs 46 and 47 of joint cases *Garage Molenheide BVBA* (C-286/94), *Peter Schepens* (C-340/95), *Bureau Rik Decan-Business Research & Development NV (BRD)* (C-401/95) and *Sanders BVBA* (C-47/96) *v Belgische Staat*, 18 December 1997, European Court of Justice, "Reports of Cases 1997 I-07281"; paragraphs 52 and 53 of The Queen, on the application of *Teleos plc and Others v Commissioners of Customs & Excise*, case C-409/04, 27 September 2007, European Court of Justice, "Reports of cases 2007 I-07797"; paragraphs 19 and 20 of *Netto Supermarkt GmbH & Co. OHG v Finanzamt Malchin,* case C-271/06, 21 February 2008, European Court of Justice, "Reports of cases 2008 I-00771".

[23] Marco Greggi, *Neutrality and Proportionality in VAT: Making Sense of an (Apparent) Conflict*, "Intertax", Volume 48, Issue 1, 2020, abstract.

regulation, or in situations where EU law is open to interpretation. In these cases, as to a uniform application of European provisions, priority must be granted to EU regulations.

The aim of the principle of effectiveness pertaining to VAT regulations is that it should not become virtually impossible or excessively difficult for individuals to exercise rights conferred by Community law[24]. The European Court of Justice was called upon to rule on this principle on several occasions. The first we shall note will be the concretization of the principle of effectiveness in the cases of Dilexport[25] and Commission v. Italian Republic[26], where the Court held that if there is a presumption that the duties and charges unlawfully levied or collected when not due (the duties and charges collected on the basis of national provisions that are contrary to eu legal acts) have been passed on to third parties and the plaintiff is required to rebut that presumption in order to secure repayment of the charge, the provision in question must be regarded as contrary to community law[27].

The Court applied the same principle in ruling in favour of Marks and Spencer[28], when the UK government reduced the period for the repayment of wrongfully paid VAT from 6 to 3 years, to all claims made after the date of enactment of that legislation and to claims made between that date and an earlier date, being that of the entry into force of the legislation, as well as to claims for repayment made before the date of entry into force which are still pending on that date. Even though no express provision in the Directive forbid the government to do so, the Court held that the retroactive effect of which deprives individuals of any possibility of exercising a right which they previously enjoyed with regard to repayment of VAT collected in breach of provisions of the Sixth Directive with direct effect must be held to be incompatible with the principle of effectiveness (paragraph 40).

This principle has gained a lot of wight in the European jurisprudence as it grants the right to the taxpayer to pursue their rights in accordance not only to the EU regulations in force but also according to the main principles by which the European Community is governed. Thus, a "blind" or mechanical application of EU regulations is not permitted and rights are better known and applied by all concerned parties (whether it is taxpayers, fiscal administrations, national courts).

The European Court has also held that this principle is sometimes to be applied in conjunction with the principle of equivalence. The latter was defined by the Court, and implies that in the absence of relevant EU rules, it is for each Member State to lay down detailed procedural rules governing actions for safeguarding rights which individuals derive from EU law, provided that they are not less favourable than those governing similar domestic actions[29]. In two cases, the court ruled that having regard to the principles of effectiveness and equivalence, a limitation period the expiry of which has the effect of penalising a taxable person who has not been sufficiently diligent and has failed to claim deduction of input tax by making him forfeit his right to deduct cannot be regarded as incompatible with the regime established by the Sixth Directive, in so far as, first, that limitation period applies in the same way to analogous rights in tax matters founded on domestic law and to those founded on Community law (principle of equivalence) and, second, that it does not render virtually impossible or excessively difficult the exercise of the right to deduct (principle of effectiveness)[30].

All of the above-mentioned principles aim at the uniformised application of EU law, in all

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[24] Ad van Doesum, Herman van Kesteren, Gert-Jan Van Norden, *Fundamentals of EU VAT law*, Kluwer Law International B.V., 2016, p. 22.

[25] *Dilexport Srl v Amministrazione delle Finanze dello Stato*, case C-343/96, 9 February 1999, European Court of Justice, "Reports of cases 1999 I-00579", see paragraph 52.

[26] *Commission of the European Communities v Italian Republic*, case C-129/00, 9 December 2003, European Court of Justice, "Reports of cases 2003 I-14637", see paragraph 26.

[27] Gundega Mikelsone, *The binding force of the case law of the court of justice of the European Union*, "Jurisprudence", issue 20 (2), 2013, p. 480, the document is available online at https://www.mruni.eu/upload/iblock/3ef/JUR-13-20-2-06.pdf, last accessed on 12.09.2020.

[28] *Marks & Spencer plc v Commissioners of Customs & Excise*, case C-62/00, 11 July 2002, European Court of Justice, "European Court Reports 2002 I-06325".

[29] See Opinion of Advocate General Sharpston, in *Scandic Distilleries SA v Direcţia Generală de Administrare a Marilor Contribuabili*, case C-663/11, delivered on 31 January 2013, European Court of Justice, "Digital reports (Court Reports - general)".

[30] See paragraph 46 of *Ecotrade SpA v Agenzia delle Entrate - Ufficio di Genova 3*, joined cases C-95/07, C-96/07, 8 May 2008, European Court of Justice, "Reports of Cases 2008 I-03457" and paragraph 49 of *EMS-Bulgaria Transport OOD v Direktor na Direktsia 'Obzhalvane i upravlenie na izpalnenieto' Plovdiv*, case C-284/11, 12 July 2012, European Court of Justice, "Digital reports (Court Reports - general)".

Member States as well as to the preservation of persons rights. Seeing that Romania is a Member State, one might wonder about the respect of the principles stated above by the national fiscal administration, as well as the national courts. Setting aside the cases that we already cited from the European Court jurisprudence that involve Romanian parties, we draw attention to the latest ruling of the Court involving a moral person and the national fiscal administration.

3. Exercise of the right to deduct with regard to VAT

Over the years, Romania has recorded a number of defeats at the European Court of Justice over the disputes regarding the way VAT is reimbursed. One of the problems raised concerns the control conducted by fiscal authorities in which the taxable person does not have sufficient documents justifying either the right to deduct VAT or the application of tax exemptions (for instance exports, intra-Community supplies of goods). In such cases, inspectors issue tax decisions setting additional amounts of VAT as well as interest/penalties for late payments (from 2016 onwards on non-compliance) and start procedures for collecting these amounts (if enforcement is not suspended).

When such disputes reach the national courts, seeing that Directive 2006/112/EC contains a number of recommendations and not necessarily obligations concerning the regulation of the VAT refund scheme, as there is no uniform practice of national tax administration agencies, more and more courts decide to suspend cases in order to await the uniform interpretation of the European Court.

In its latest ruling, the European Court had received a request for a preliminary ruling from the Cluj county Tribunal, that opposed a moral person and the fiscal administration[31]. The request aimed to clarify the right of defence in the case of an administrative act issued by the national tax authority, without giving the taxpayer access to information or the documents on which the act was based and the compatibility of the national legislation with the principles of neutrality, proportionality and equivalence with the refusal of the tax authority of the right to deduct VAT and corporation tax, on an allegedly improper conduct of the taxpayer, retaining that he had provided no further proof of transaction other than the tax invoice.

In this case, the moral person is a company registered in 2008, in Romania, that deals with the exploitation of forestry resources and that was subject to a tax inspection on corporation tax and VAT.

The fiscal administration suggested that the transactions between the natural person and two of its suppliers were fictitious, as the suppliers had no technical or logistical means to provide the services invoiced to C.F., and they benefited of a 3% tax on turnover as they qualified as microenterprises, whereas C.F. had a 16% tax on its turnover. According to the fiscal authorities, C.F. was liable for improper conduct, as it was unable to provide further proof of the services, other than the tax invoice. The Court retained that according to the Romanian legislation in force, the taxpayer is only required to produce a tax invoice in order to exercise the right of deduction for both VAT and corporation tax.

Secondly, the tax inquiry also give rise to a criminal investigation that resorted in a decision of *nolle prosequi*. The moral person, C.F. appealed against the tax inspection report and asked to access its full administrative file, as it was not informed as to how the criminal proceedings influenced its fiscal situation. Such access was denied to the company.

This gave rise to 4 questions addressed to the European Court, whereas the first pertained to the right of defence and the following pertained to the application of EU law, where the tax authority only had doubts about the economic operations, i.e. if they were carried out effectively, do its principles preclude a taxable person from being refused the right to deduct VAT, if they are unable to produce other documents apart from the invoice.

Concerning the right to defence, the Court retained that as an integral part of the right of the defence, there is a guarantee for the person to make known his views during an administrative procedure and before the adoption of any decision that affects his interests. In this case, even though the fiscal administration is not under the obligation to grant access to an investigation file, or to

[31] *SC C.F. SRL v A.J.F.P.M. and D.G.R.F.P.C*, case C-430/19, 4 June 2020, European Court of Justice, not yet published, the document is available online at http://curia.europa.eu/juris/liste.jsf?language=en&td=ALL&num=C-430/19, last accessed at 09.09.2020.

communicate documents and information that stand reason for the decision, the referring court points out that they had no viable reason to do so, and as such asks whether the administrative decision shouldn't be declared automatically null and void. The Court underlines that the conditions of the respect of the right to of defence, nor the consequences of its infringement aren't regulated by EU provisions, and as such they must be regulated by Member States, taking into account primarily the principles of equivalence and the principle of effectiveness. Thus, in virtue of the principle of effectiveness, an infringement of the right of defence will only result in the annulment of the decision if, had the right of defence be observed, the outcome of the procedure was different.

Regarding the following questions addressed to the Court, it holds that according to the principle of neutrality, the right to deduce VAT is an integral part of the VAT scheme for all economic activities, regardless of their purpose or results, provided that they are themselves subject, in principle, to VAT. It is therefore to the national courts and administration to determine, using objective elements, that the right to deduce is invoked in a fraudulent or abusive manner. The Court further states that although a taxpayer can be obliged to make inquiries if he has suspicions of infringement, fraud or was made-know, or should have known that he was participating in a transaction related to VAT evasion, the tax authorities can't, as a general rule, require that the taxable person first verify if the contracting party is in possession of goods or services relating to the supply of the products invoiced or if the contracting party has complied with his obligations as to the declaration and payment of VAT. As the probation rules in cases of VAT refund are not regulated at EU level, it is for the Member States, through their fiscal administrations to set them, without disregarding Community regulation. Moreover, it is for the fiscal administration to determine based on objective factors, without requesting it from the invoice recipient, if the latter knew or should have known if the transaction on which the right to deduct is required was in connection with VAT fraud.

4. Assessments of the latest ruling

The right of defence is an inherent right granted to all persons under the provisions of EU law. Corroborating this principle with the one stated above, that of the principle of legal certainty we observe that a taxpayer not only has the right to know what to expect from the national fiscal authority, but also has the right to make assertions that might lead to a clarification of their fiscal situation.

According to the principles of neutrality and proportionality, it is up to the national fiscal administration as well as the national courts to determine the refusal to grant the right to deduce VAT, the general rule being that for all economical operations, this right is granted on the basis of the invoice. In order to refuse this right to the taxpayer, it must be determined, on the basis of objective elements that the right is invoked in a fraudulent or abusive manner.

As seen before, in the principle of neutrality grants taxpayers' the right to deduce VAT on any and all transactions, precluding the ones that are abusive. Thus, as mentioned before, there is no limit to the right to deduce VAT, even if there are structures especially designed for this goal, as long as they are properly set up (see Midland Bank and following). Also, the right to deduce VAT can't be subjected to explanations pertaining to the final destination of the goods (see SMS Group Gmbh), nor to demonstrating that the activity was carried out in other ways then by presenting the invoice (see C.F. SRL case).

As an analysis, the Court tends to rule in favour of companies, that within their right apply for the deduction of VAT, and tends to dismiss any and all actions of national authorities that go beyond the principle of proportionality and might add to the fiscal burden of taxpayers (see EN SA case). In this optic, Member States, through their national authorities, can't undergo operations that will go beyond their goals of protecting the national financial interest or go towards preventing tax fraud.

Furthermore, the Court clearly states in this decision that it is for the fiscal administration to obtain objective and not circumstantial proof of fiscal fraud, and thus no refusal of refunding VAT might be taken on the simple assumption or by simply stating irregularities. The implication of the taxpayer should be taken into account during the fiscal inquiry, but not pertaining to him proving the regularity of the transactions for which he is requesting the right to deduce, but taking into account

his rights to defence.

5. Conclusions

The case presented before is unique in the sense that the main questions arising are if and how the national authorities will be able to respect and implement the simplification of VAT deduction. According to the above-mentioned case-law, the only necessary document in order to request and be granted the right of deduction is the invoice, without any other supporting documents.

Given that by Law no. 241/2005 the fiscal authorities have relatively limited means in order to combat fiscal tax evasion, and given that the mentioned legislative act mostly focuses on sanctioning, rather than a preventing, one might wonder whether the approach of the European Court can be implemented. As far as we are concerned, seeing how Romania is still one of the states that collects VAT among the least within the EU, we consider that implementing a culture that will encourage taxpayers to voluntarily pay their taxes is at the very least needed. As we have figured, the so called overcontrol of the fiscal authorities rarely leads to a better collection of taxes and is usually sanctioned by international courts.

It is clear that no developed society has a full collection of taxes, but more often than not, states that report a better collection of their taxes have a preventive approach and not a sanctioning approach.

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