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Reducing the Vat Gap in Poland

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***Abstract*—The main goal of the paper is to study the effectiveness of legal changes introduced in 2016 which were aimed at reduction of the VAT gap in Poland. The study consists of a normative, legal and quantitative analysis of data provided by the Ministry of Finance and shows the financial scale of VAT gap reduction. The thesis put forward in the paper assumes that the changes in law introduced in 2016 made it possible to effectively reduce the VAT gap in Poland and to tighten the system of VAT collection. The author managed to confirm the thesis in the course of the conducted research. The paper also emphasizes that the Polish tax on goods and services is well harmonized with its EU counterpart. Also the activities aimed at combating the phenomenon of VAT fraud seem to have brought positive results. At the same time, the central invoice register which is due to be implemented in July 2019, is expected to be a significant improvement.**

Index Terms— Value Added Tax, tax audits, frauds, reducing the VAT gap

I. INTRODUCTION

The most fundamental and at the same time the most important task of fiscal administration is realisation of tax revenues, fees, non-tax and other budget receivables based on separate provisions, with the exceptions of taxes and budget receivables, in which other bodies are competent. Fiscal administration is also responsible for realisation of income from customs duties and other charges related to the importation and exportation of goods. In 2016 fiscal administration in Poland underwent reorganisation and following the changes, an entirely new institution called the National Revenue Administration (NRA) emerged. The legislator entrusted to the NRA the execution of the following tasks: determination, collection and enforcement of receivables as well as performance of audits regarding taxes and customs-fiscal issues.

II. VAT – HARMONISATION AND UNIVERSALITY

The system of intra-community transactions is the best harmonized area of the current VAT system. The harmonisation, which can be observed in all EU countries, is probably the consequence of the fact that provisions of the Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax regarding transactions between Member States, are mandatory. There was no room for applying the subsidiarity principle because should it be allowed, the harmonization of transactions would be pointless. The essence of harmonization of intra-community transactions is their mutual correlation. When there is intra-community supply on one side, there must be intra-community purchase on the other.

The principle of universality of taxation with value added tax on all goods and services results directly from article 1 of the 2006 Directive. A Member State may derogate from the principle of universality of taxation only exceptionally and only on the basis of authorizations contained in the Directive. The rules for VAT application stipulate that exclusion or exemption of certain transactions from taxation would distort calculation of VAT in a manner that would prevent the achievement of the goal of taxing only the final consumption of goods or services. Therefore, the use of exemptions was restricted only to such goods and services which are enumerated in the provisions of the 2006 Directive. The postulate of 'universality of VAT taxation' is implemented primarily by the construction of definition of supply of goods and services.

Contemporary universality of VAT guarantees that conditions for balanced competition are met. Distortions from the prescribed conditions for fair competition should be avoided in order to ensure that all taxable persons operating on the market have equal taxation rules. Hence, e.g. civil law transactions are taxed even when they are not compliant with the forms provided for by the law. For this reason, article 13

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section 2 of the 2006 Directive obliges Member States to ensure that when States, regional and local government authorities and other bodies governed by public law engage in such activities or transactions, they shall be regarded as taxable persons in respect of those activities or transactions where their treatment as non-taxable persons would lead to significant distortions of competition.

III. VAT COLLECTION MECHANISM

When it comes to collection of value added tax, it must be emphasized that it is a multiphase process which is closely connected with the principle of universality stipulating that VAT should be levied at every stage of the turnover of goods or services, up to the moment of retail delivery to the end user. At each point only the added value may be subject to taxation. The added value is calculated from the net value of goods or services, less the value taxed in the previous stages of the turnover. VAT, which is calculated on the price of goods or services at the rate appropriate for such good or service, is required for each transaction, after deduction of the amount of tax incurred directly in various cost components in the previous stage of the economic turnover. The common system of VAT shall be applied up to and including the retail trade stage. Such a method of VAT calculation is related to its next feature which is its deductibility.

Multiphase of VAT requires its calculation at all stages of goods or services turnover. It is a mechanism that guarantees that the end user is charged with this tax in accordance with the abovementioned principle of deductibility. It means that each taxable person at his stage of the turnover, while calculating the tax due charged to the next recipient, has the right to deduct from the tax due the tax that was imposed on him by his suppliers when they purchased given goods or services. The feature of deductibility distinguishes VAT from other turnover taxes. The restriction of the right to deduct input tax can only be exceptional because it determines the principle of VAT neutrality for the taxable person. VAT should not be levied on those entities participating in the turnover of goods and services who are not their end users. The burden of 'general consumption tax' should be imposed only upon end users of goods or services in the last stage of economic turnover, i.e. the retail stage. Value added tax, pursuant to article 1 clause 2 of the 2006 Directive, is referred to as a general consumption tax in accordance with the principle of neutrality which has been continued invariably following the provisions of Article 1 clause 2 of I Directive.

Implementation of the principle of VAT neutrality for the taxpayers is expressed by the right to deduct input tax i.e. the existence of such legislative solutions under which input tax calculated at the price of goods and services purchased for the purposes of the taxpayer's taxable activity, can be deducted without constituting at the same time a cost for the taxpayer in the economic sense. The moment when the right to deduct arises can be specified as the time when the deductible tax becomes chargeable. In addition, the Court of Justice of the EU emphasizes in its jurisprudence that the right to deduct input tax, which is an expression of the principle of neutrality, should be exercised immediately. As a consequence, any restrictions in this respect provided for by the legislation of a Member State would constitute infringement of the principle of neutrality and would remain in conflict with the general requirements of the common VAT system.

In the classic model of VAT collection, the taxpayer subtracted the net value of the goods at the moment of sale from the net value of the goods while purchased. The difference constituted the value added by the taxpayer from which the amount of tax due was calculated. Nowadays, the tax is calculated as follows: the taxpayer takes the entire net value of the goods sold as the tax base and calculates the amount of tax due from this value. Then, the amount of tax that the taxpayer was to pay in the price of goods purchased for the business purposes is deducted from the amount of VAT due. In the end, the taxpayer is left with the amount of tax that should be paid to the tax office.

Deduction of the amount of tax due depends on clear separation of the amount of tax in the prices of goods bought and sold. This tax is calculated by the markup on the net value of the goods. An expression of the universality of value added tax is the use of the same tax rate for the majority of goods and services. It is the so called 'basic rate' which in Poland amounts to 23%. At the same time, in countries of the so called 'old Europe' (EU-15), efforts are made to ensure that value added tax is charged at a relatively uniform rate. In reality, the most popular solution is application of a reduced or an increased rate as an alternative to the basic rate. The reduced rate generally applies to groceries, medicines, books and magazines, selected raw materials and intermediate products as well as to some social and cultural services. The increased rate of VAT applies to goods which are considered luxurious.

IV. TIGHTENING OF VAT COLLECTION SYSTEM IN POLAND

At the time when Poland joined the European Community its VAT system was characterised by complexity and illegibility and the scope of tax fraud, especially in the fuel industry, was immense. The tax on goods and services and the excise tax introduced by the Act on 8 January 1993 were not adjusted to the fiscal regulations of the European Union. Therefore, the Act has been amended many times in order to acquire the shape in the likeness of the systems functioning in the EU Member States. With the access to the European Union on 1 May 2004, Poland became obliged to fully embrace the so called *acquis Communautaire* i.e. the accumulated legislation, legal acts, and court decisions which constitute the body of European Union law. It was the fundamental cause why Poland implemented regulations on the tax on goods and services. Implementation of the 2006 Directive principle that 'taxable person' shall mean any person who, independently, carries out in any place any economic activity, whatever the purpose or results of that activity, allowed to maintain neutrality of the tax also with respect to persons who make a purchase in a country other than the country where they conduct their business activity.

On 7 July 2016, Poland passed the bill of amendment to the

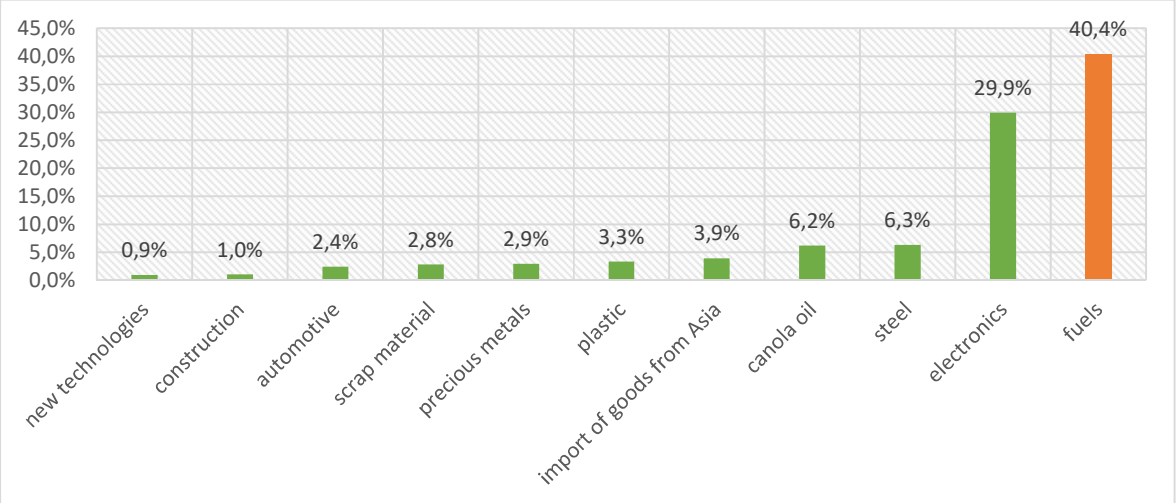
Act on tax on goods and services and selected other acts. The amendment was focused on undertaking actions counteracting or reducing the practice of VAT fraud in the fuel turnover. The amendment provided solutions that prevented circumventing the security function of the license for international fuel trade issued by the Head of the Energy Regulatory Office, regulated the system of licensing in the cross-national liquid fuel turnover and led to tightening of VAT collection in the sector of cross-national liquid fuel turnover. The amendments to the VAT Act, in turn, introduced changes with respect to declarations and payments of tax in intra-Community transactions in motor fuel trade. Under the procedure of suspension of excise collection, the taxable person is a tax warehouse or a registered recipient. The amount of collected VAT is deposited into the account of the same customs authority which is competent as regards the excise tax on transactions. The obligation to pay VAT arises essentially within 5 days after liquid fuels are brought into the territory of Poland. To determine the tax base, one may make use of the prices of motor fuels provided by the competent minister responsible for public finance. The prices are quoted based on the wholesale prices of fuels in Poland. Moreover, each entity is obliged to register for VAT purposes and to dispose of storage space in order to maintain inventory, otherwise it is obligatory to outsource the storage to an external supplier. Other changes in regulations included extension of the volume of personal data required to identify executives applying for a license, modifications to the wording of licenses and the introduction of the requirement to update data. There was also an extension to the catalogue of premises which may trigger withdrawal of a license by the head of the Energy Regulatory Office.

In practice, one may distinguish three main constituents of VAT: actual revenues, the so called *policy gap* i.e. the difference between the tax revenues at 100% collectability and hypothetical revenues with no tax exemptions and preferences in place, and finally, the VAT loophole reflecting the degree to which taxpayers meet their tax liabilities. As a result, the Ministry of Finance implemented the following new legislative tools which are supposed to reduce the scale of VAT fraud:

1) application of a uniform methodology for assessment of due diligence of buyers both in domestic and EU transactions;
2) implementation of the Standard Audit File for Tax (SAF-T) which guarantees prompt execution of audit and control activities;
3) application of the split payment mechanism;
4) amendments to the VAT Act, the Excise Duty Act, the Energy Law (EL) and the Act on stocks of crude oil, petroleum products and natural gas; implementation of the so called 'fuel package'.

The aforementioned legislative tools considerably weakened the grey zone activities increasing at the same time budget revenues by approximately 2,5 billion PLN per annum. However, it required considerable intensification of tax inspections and audits. In 2016 alone, 9,855 inspections were carried out which was 500 inspections more when compared to 2015. Additionally, tax authorities conducted more than 1,700 interrogations and drew up 2,760 requests to financial institutions to provide information constituting bank secrecy in order to examine flows on the bank accounts of business entities. As a result, auditors and inspectors discovered infringements worth about 22,2 billion PLN, which equaled the amount of almost half of the budget deficit. Once the tax system in Poland was successfully and visibly tightened, a lot of taxpayers started to fear fiscal authorities and, in consequence, the number of voluntary corrections of tax returns increased by 184%, what translated into additional 0,5 billion PLN going into the State budget. It can be estimated that more than 90% of audit findings involved VAT related issues with the joint value of fraud exceeding 20 billion PLN. At the same time, the analysis of post-audit reports shows that the area of the highest risk with the highest amount of VAT fraud was found in the fuel industry (Chart 1).

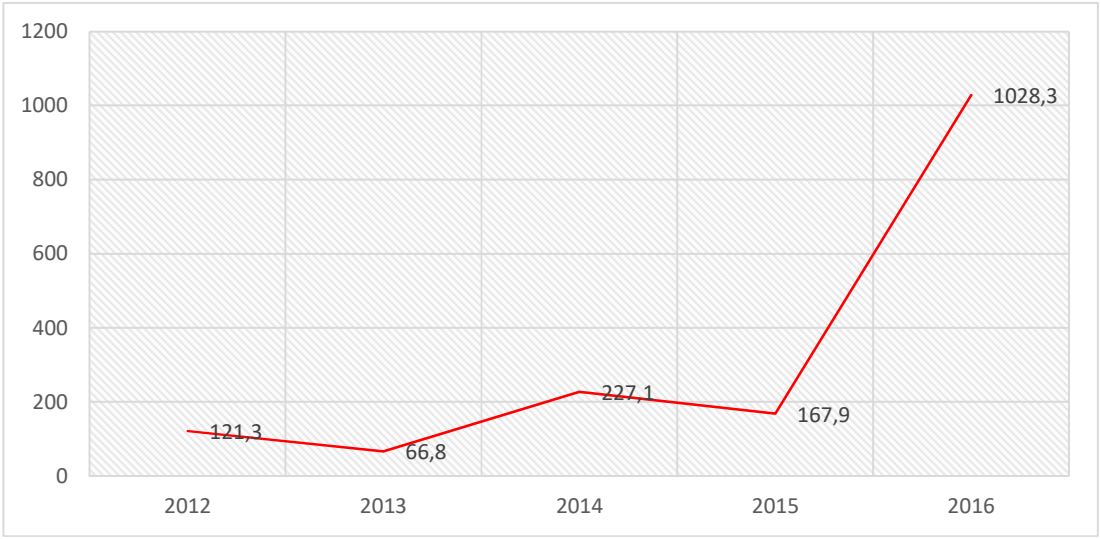
CHART 1. DISTRIBUTION OF VAT FRAUDS ACCORDING TO INDUSTRIES



Source: Own work based on data of the Ministry of Finance: https://www.mf.gov.pl/, (accessed: 29 January 2019).

On the basis of data from the Ministry of Finance, it can be stated that thanks to the amendments to law introduced in 2016, the number of prevented payments from the State budget regarding unduly claimed VAT increased considerably (by 512%) and in 2016 alone amounted to more than 1 billion PLN. In contrast, in previous years the fiscal control organs questioned and prevented the payment of only 120-230 million PLN worth of unduly claimed VAT returns (Chart 2).

CHART 2. PREVENTED RETURNS OF UNDULY CLAIMED VAT (MILLION OF PLN).



Source: Own work based on data provided by the Ministry of Finance: https://www.mf.gov.pl/, (accessed 29 January 2019).

On the basis of the analysed legal norms and post-audit reports, it can be claimed that the Ministry of Finance considerably increased the efficiency of its audit and control proceedings thanks to the amendments introduced to relevant legal acts in 2016.

V. THE NATIONAL REVENUE ADMINISTRATION (THE NRA)

Pursuant to the changes to the Polish legal system introduced in 2016, the provision of sufficient level of efficiency of the tax system when it comes to fiscal audit and control, tax collectability or fight with the grey zone in the liquid fuel sector, lies in the hands of the National Revenue Administration (NRA). The Act of 16 November 2016 on the National Revenue Administration amends or waives many provisions as well as introduces transitional, adapting and final regulations. The adapting regulations regard the following legal acts: the code of civil procedure, the code of criminal procedure, the code of petty offences, tax laws, the Act on the police, the Act on the border guard, the Act on banking law, customs law, local government acts, the Act on revenues of local government units, the Act on departments of government administration, the Act on freedom of business activity, the civil service acts, the Act on public finance, the Act on customs services, the Act on rendering services in the territory of the Republic of Poland, the *Act* on *exchange* of *information* with the *law enforcement* authorities of the *EU Member States*. In total, as a result of transformations in the organizational structure of fiscal administration, 157 acts underwent amendments. Customs authorities and tax investigation bodies were incorporated into the framework of the National Revenue Administration (NRA). The scope of the aforementioned legal changes involved most of all:

1. Replacement of regulations on tax chambers and customs chambers with regulations on revenue administration chambers;
2. Replacement of regulations on customs offices with regulations on tax offices or customs and tax offices;
3. Replacement of some regulations on fiscal inspection organs with regulations on customs and tax offices;
4. Waiving some regulations on organs of fiscal inspection both in organisational as well as procedural aspect;
5. Replacement in legal acts in force of regulations on officers of Customs Services with regulations on officers of Customs and Tax Services;
6. Replacement in legal acts in force of regulations on payments into the bank account of a tax office with regulations on payments into the bank account of the revenue administration chamber.

Following the adoption of provisions of the Act on the National Revenue Administration, the institution of the General Inspector for Treasury Control was abolished along with directors of customs chambers, directors of tax chambers, directors of treasury control offices and the heads of customs offices. The customs offices were also discontinued. At the same time it was adopted (as of 1 September 2016) that the tax

chamber continues its activities but becomes known as the chamber of revenue administration. On 1 January 2017, the chamber of revenue administration was merged with customs chamber and tax inspection office. Due to the merger, the chamber of revenue administration stepped into the entirety of rights and obligations of all merged units regardless the nature of legal relationship which gave rise to these rights and duties. Assets and liabilities of the tax chamber, the customs chamber and tax inspection office became assets and liabilities of the chamber of revenue administration.

Article 1 of the Act on National Revenue Administration stipulates the essence and subject of regulations contained therein and indicates that the fundamental aim of creation of the National Revenue Administration (the NRA) as a specialised organ of public administration, was execution of tasks related to realization of tax revenues, customs duties, fees and untaxed budget receivables, protection of vital interests of the State Treasury and the customs territory of the European Union. The NRA also provides customer service and support for taxpayers and entrepreneurs as regards correct execution of fiscal and customs duties. Moreover, within the organisational structure of the National Revenue Administration (the NRA) and the civil service corps, there is yet one more formation called the Customs and Tax Services which is a homogenous and uniformed force.

The Act on the National Revenue Administration outlines tasks, organs and organisational structure of the National Revenue Administration (the NRA), the method of execution of some tasks and special entitlements of the NRA officers as well as the rules of their disciplinary liability. The catalogue of tasks to be performed by the NRA can be found in article 2 of *the Act*. The tasks in question in majority mirror the tasks previously performed by fiscal administration, the Customs Services and organs of treasury control pursuant to the Act on fiscal offices and chambers, the Act on fiscal administration, the Act on Customs Services, the Act on treasury control, and other acts, including especially acts on fiscal and customs law. The NRA is also responsible for the implementation of customs policy imposed as the result of Poland's membership in the EU customs union, placement of goods under customs procedure and regulation of the situation of goods in import and export. The aforementioned tasks used to be performed by the Customs Services.

The National Revenue Administration (the NRA) is also obliged to engage in analytical, forecasting and research activities related to the phenomena occurring in the scope of the NRA's competences. Risk analysis (see: article 2 paragraph 1 point 10 of *the Act on National Revenue Administration*) is of key importance for the efficiency of tightening of the tax system and reducing the VAT gap. Thanks to the analytical activities mentioned above it is possible to recognize and counteract phenomena which are harmful for the fiscal and customs systems in Poland. The outcomes of research and analysis conducted by the NRA also contribute to implementation of preventive measures related to risks of taxpayers' failure to meet their fiscal and customs duties.

VI. CONCLUSIONS

The paper constitutes a confirmation of the thesis that the amendments to the Polish law introduced in 2016 effectively tightened the system of VAT collection and helped to reduce the VAT gap. The 2016 provisions amending the Polish VAT Act considerably reduced the phenomenon of VAT fraud which was particularly widespread in the fuel sector. Thanks to the activities undertaken by the National Revenue Administration it is now possible to recognize and counteract phenomena which are harmful for the fiscal and customs systems in Poland and to determine directions for further implementations aimed at increasing the efficiency of the Polish tax system. The NRA, which was established following the consolidation of customs and fiscal services with the tax inspection offices, has already improved the collectability of VAT thanks to close cooperation with the Police. Another positive aspect of the reform is the requirement for each foreign company to either have the seat in the territory of Poland or to conduct business activity through a licensed subsidiary.

On the negative side, *it can be concluded that the* only intention of the fiscal reform of 2016 was, as it seems, to increase the efficiency of VAT collection and reduce the VAT gap. Another significant limitation of the reform is the fact that the implemented solutions are only of fragmentary nature because they do not embrace the issues of public levies management or administration of taxes on local government level. The consolidation achieved as the result of the reform seems to be reduced only to simple actions such as: abolition of the existing organs, liquidation or transformation of previously functioning organisational units of fiscal administration and appointment of new organs and new organisational units. As the result of such 'consolidation' which took place on the central, national, regional and local level, a completely new organisational unit was created (the NRA) but the tasks assigned to it are practically the same as the tasks previously performed by tax offices and chambers as well as treasury control authorities, the Customs Services and the General Inspector for Treasury Control.

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