

VAT REGISTRATION GUIDE

*Pre and post registration VAT
controls*



VAT REGISTRATION GUIDE

Pre and post registration VAT controls

INTRA-EUROPEAN ORGANISATION OF TAX ADMINISTRATIONS
(IOTA)



BUDAPEST 2012

TABLE OF CONTENTS

Preface	4
1. Introduction	6
1.1. Background	6
1.2. Aim of the report	6
1.3. Task team working methods	6
1.4. Caveat	7
1.5. Reading guide	7
2. VAT Registration Application Form	8
2.1. Paper form	8
2.2. Via an electronically downloadable form	9
2.3. Via an electronic form through an online platform	9
2.4. Central processing of applications for VAT registration	10
2.5. Attendance of applicant required at the time of submission	12
3. Pre-registration controls	12
3.1. Conditions for VAT registration	13
3.2. How to balance efficiency and control level	14
3.2.1. <i>Minimum approaches</i>	16
3.2.2. <i>Premium approaches</i>	16
3.3. Check the National Register of Companies and other databases	19
3.3.1. <i>Minimum approach</i>	20
3.3.2. <i>Premium approach</i>	20
3.4. Cross-checking information against other sources	22
3.4.1. <i>Minimum approach</i>	22
3.4.2. <i>Premium approach</i>	23
3.5. Risk assessment classification	24
3.6. Profiling	26
3.6.1. <i>United Kingdom Near-Real-Time Profiling Centre</i>	26
3.7. Possibility to require financial security or bank guarantee	29
3.8. Possibility to collect further in-depth economic information	30
3.8.1. <i>Minimum approach</i>	31
3.8.2. <i>Premium approach</i>	32
3.9. Pre-registration visits/audits	32
3.9.1. <i>Minimum approach</i>	32
3.9.2. <i>Premium approach</i>	33
3.10. Communicating with applicants and professional advisers	33
3.10.1. <i>Minimum approach</i>	33
3.10.2. <i>Premium approach</i>	34

IOTA Report for Tax Administrations
Pre and post registration VAT controls

3.11.	Possibility to register a company for VAT under special conditions	35
	3.11.1. <i>Special VAT number for intra-Community transactions</i>	44
3.12.	Requirement to submit monthly VAT returns as a control measure	45
3.13.	Possibility to postpone the granting of a VAT registration.....	45
3.14.	Possibility to deny or reject the application for a VAT registration	46
	3.14.1. <i>Minimum approach</i>	46
	3.14.2. <i>Premium approach</i>	46
4.	Post-registration controls	48
4.1.	Introduction	48
4.2.	Definition of new businesses.....	49
4.3.	Control of new businesses	49
	4.3.1. <i>Minimum approach</i>	50
	4.3.2. <i>Premium approach</i>	50
4.4.	Registration threshold	50
4.5.	Checking whether the registration threshold is exceeded	51
4.6.	Questionnaires to identify risky VAT businesses	52
4.7.	Methods to identify dormant VAT registered businesses	53
	4.7.1. <i>Minimum approach</i>	53
	4.7.2. <i>Premium approach</i>	53
4.8.	Identifying missing traders, buffers, brokers, etc.	54
	4.8.1. <i>Tools for identification</i>	55
	4.8.2. <i>Joint and several liability</i>	57
	4.8.3. <i>Blacklists of suspected fraudsters or bogus companies</i>	57
	1.1.1. <i>Special attention to intra-Community transactions and third</i>	58
	4.8.4. <i>Informing customers and suppliers of missing traders</i>	59
	1.1.2. <i>Informing other Central Liaison Offices or TAs in Third</i>	60
4.9.	Deregistering businesses from the VAT register	61
	4.9.1. <i>Minimum approach</i>	61
	4.9.2. <i>Premium approach</i>	62
5.	Appendices	64
5.1.	Appendix 1 - Pre and post registration VAT Controls - Questionnaire 2010	64
5.2.	Appendix 2 - Sweden - Risk assessment and high risk sectors	64
5.3.	Appendix 3 - VAT Thresholds in the IOTA region	64
5.4.	Appendix 4 - UK - VAT Risk Assessment Questionnaire	64
5.5.	Appendix 5 - Sweden - VAT Risk Assessment Questionnaire	64

Preface

The VAT identification number is a key feature in every VAT system. In the case of intra-Community trade within the EU the VAT number is an essential element to enable the supplier to decide whether or not to charge VAT on his supply. Without a VAT identification number it is impossible for the fraudster to perpetrate VAT fraud!

VAT fraud in the IOTA region leads to severe budget losses and violates the principle of fair taxation, bringing distortions to capital movements and the conditions of competition.

One of the most important measures to assist a tax administration (hereafter 'TA') to prevent VAT fraud is to improve the VAT Registration process. There are many ways of improving the process, and this IOTA VAT Registration Guide aims to present a number of methods, ideas and procedures that have been adopted by the IOTA member TAs to improve the process, including the use of pre- and post-registration controls specifically aimed at identifying and preventing VAT fraud.

All TAs experience limitations in the resources available to them for conducting sufficient control activities in areas where a risk of tax losses occurs. Legislation can also restrict the efficiency and tools at the TAs' disposal. The aim of reducing the administrative burden that the tax rules and obligations impose on businesses often contradicts the need of TAs to obtain relevant and satisfactory information for the purposes of risk management and other control measures.

Against this background all TAs must allocate their resources in the best way possible to optimise effectiveness and efficiency. They also need to be intelligent and innovative, sharing mutually beneficial good practice and making best use of mutual exchange opportunities.

Whatever measures and activities a TA considers using, they must be based on legislation and regulations. This VAT Registration Guide seeks to highlight a range of operational methods based on legislation, and also various approaches which may improve the quality of the TAs' work in the area of VAT registration.

Of course, legislation should not prove an obstacle to effective functioning of the TA. For this reason all TAs should be proactive in reviewing the impacts of legislation, positive and negative, and promote changes in legislation where that is considered necessary. It is in this respect that legislation and good practices from other countries can serve as examples when promoting changes domestically.

IOTA Report for Tax Administrations
Pre and post registration VAT controls

Tax fraudsters are innovative too, constantly mutating and reinventing their fraud methods, requiring continuous adjustment in the methods and procedures of the TAs if they are to effectively combat tax fraud. This in itself highlights the great importance of learning from, and exchanging information between TAs on how specific problems have been dealt with.

During the preparation of the material used in this publication, input was provided by members from the IOTA Area Group "Prevention and Detection of VAT Fraud", which comprises representatives from the majority of the IOTA member tax administrations.

The IOTA Secretariat would like to thank all of them and particularly the following Task Team members: Heidar Hilmarsson (Sweden), Patrick Hackett (Norway), Laima Sinkeviciene (Lithuania) and Fabio Celozzi (Italy) who compiled this report.

The Task Team would also like to thank Mark Crawford for his significant input to the report and his valuable support in arranging a meeting with UK colleagues at HMRC.

We also thank the Dutch tax administration for allowing us to adopt parts of their handbook on how to tackle Missing Trader Intra-Community (MTIC) VAT fraud.

1. INTRODUCTION

1.1. Background

The IOTA Area Group Prevention and Detection of VAT Fraud originally established a task team in 2006 to compile a Good Practice Guide on the use of VAT Registration Controls. The guide was issued as a CD, containing background documents from 25 responding countries among the IOTA membership. The decision was taken by IOTA in 2010 to update the existing guide, and a new task team was established in 2011 for this purpose.

1.2. Aim of the report

The aim of this report is to present a variety of approaches concerning pre- and post- VAT registration controls. The format has been developed from a Good Practice Guide into something which can more correctly be termed a VAT Registration Guide. The report could also serve as a guide for developing administrations in other jurisdictions, where they intend to adopt VAT as an indirect taxation system.

The Task Team aims to present a number of methods, activities and procedures in general terms, rather than submersing the reader in too much detail. The idea is to point out directions and present measures which can be adopted without the necessity of describing how to perform a certain activity. The reason for this is that every TA must adjust the measures to the domestic conditions and limitations they face, such as national and EU legislation, organisational structure, available resource and such.

1.3. Task team working methods

This report is based on the information collected from the IOTA member tax administrations, primarily through a questionnaire and, where it was possible, telephone interviews with colleagues across the IOTA region. In some cases further queries were answered by the exchange of e-mails and in some instances countries were visited for face-to-face interviews with key personnel involved in the VAT registration process within the TAs. The Task Team members also received a lot of information from their respective tax administrations.

The submitted responses to the questionnaire were compiled and analysed, and the Task Team has attempted to incorporate the most innovative measures in this report. The Task Team has consciously chosen not to present any comparable tables or statistics, because the aim is to provide an end product that highlights methods and procedures as a readable report rather than a basic publication of comparative data that would have limited practical use to TAs considering new approaches to VAT registration controls.

1.4. Caveat

The questionnaire issued to the IOTA member tax administrations is included within the report as appendix 1.

Although most representative members of the Area Group Prevention and Detection of VAT Fraud submitted replies to the questionnaire, the individual responses differed in terms of content and quality. Some countries submitted elaborate explanations of their methods, while others chose to deliver simple yes/no responses. The Task Team has observed that some respondents interpreted the questions differently and a few countries decided not to provide a response at all.

The methods and procedures presented in this report are therefore not an exhaustive compilation of good practices within the IOTA member tax administrations, but rather a compilation of methods which the Task Team could identify from the various replies to the questionnaire and through the other contacts that the Task Team had with individual TAs. Despite this slight limitation, the results offer the reader a comprehensive practical guide on how to approach the issues of risk associated with VAT registration.

1.5. Reading guide

The report is divided into chapters which follow the different stages of the VAT registration process. The chapters are further divided into sections and sub-sections where individual methods are presented. Many of the sections and sub-sections are then dissected into what is termed a "*minimum approach*" and a "*premium approach*".

The concept of a minimum approach has been borrowed from the Common Minimum Standards issued by the EU, although it is important to note that the minimum approaches mentioned in this report are entirely based on the criteria and analysis of the Task Team and bear little or no reference to the EU CMS.

The Task Team feels that presenting a minimum approach is important in the sense of establishing a minimum baseline in terms of VAT registration controls, but it is equally important to present a premium approach, which consists of methods TAs can strive to reach and which may be more effective than simply implementing and maintaining the minimum approach.

2. VAT REGISTRATION APPLICATION FORM

In most cases the VAT registration process begins with an application from the business in question. The application form can consequently be seen as the gateway to VAT registration, which means the framing of questions and subsequent handling of applications is a matter of great importance.

This report will cover aspects related to the handling of applications. In respect of the design and the questions included in the application form we make reference to a comparative study of various application forms which IOTA presented in an earlier report produced by this Area Group and published in 2007.

The full report is available on the IOTA website:

<http://www.iota-tax.org/publications/iota-report-for-tax-administrations--vat-registration-forms.html>

2.1. Paper form

Practically all IOTA member countries offer the option to submit the VAT registration application form on paper. However, there is a gradual shift away from paper forms towards electronic forms in most countries, which is mutually desirable as it offers greater opportunities for the tax

administration to benefit from efficiency and formal controls and at the same time reduces potential costs and burdens for businesses. A number of TAs are actively removing the possibility for a business to submit paper applications, making the use of electronic and online forms the only option. The application form should be made available in several languages to reflect the increasing migration and globalisation of trade and the multicultural nature of our society.

2.2. Via an electronically downloadable form

Nearly all IOTA member countries make their forms available for downloading and printing from the TA's website or a related website. This provides easy access to the forms without the need for individuals and businesses to contact the tax office.

Some countries do not keep paper forms in stock, which effectively leaves electronic solutions as the only possibility open to the applicant. This, together with the fact that electronic submission is less burdensome, motivates applicants to submit electronically.

Regardless of whether the form is submitted electronically or on paper, it is important for the TA to record the information in a database to make it more accessible and suitable for electronic cross-checks by the TA.

2.3. Via an electronic form through an online platform

Electronic application forms can enable the TA to structure a pattern of questions to suit specific applicants. Furthermore the TA can require the document to include an electronic signature, which can arguably be deemed safer than written ones in terms of validating the originator of the document. Technically, using an electronic signature allows for pinpointing the location the application is sent from, through the IP address, but this option requires specific legislation, which most countries do not have.

Electronic registration forms can be designed to prevent submission by the applicant if the requested information is not included or where it is incomplete, thus enhancing the quality of the application and ensuring that all of the necessary information is provided.

Some TAs require a joint electronic registration with other governmental agencies, offering a "*One Stop Shop*" on the internet for their citizens. This not only improves the level of services offered to the citizens, but is also

more cost effective for the TA by sharing the cost of software solutions, infrastructure, e-certificates, etc.

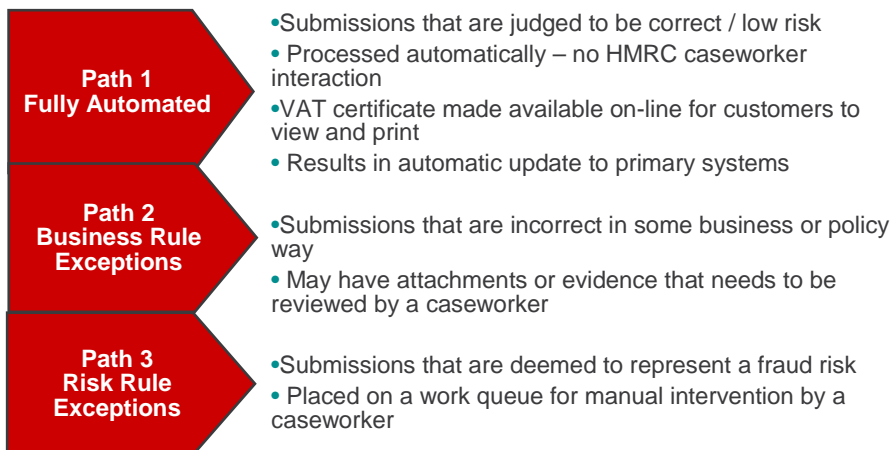
One example is the **United Kingdom's VAT Registration Transformation Project**. Their administration is developing a fully automated, user friendly electronic VAT registration system. The aim is to create a system with electronic forms with the ability to respond to and ask the applicant relevant and intelligent questions during the registration procedure.

The system will automatically verify almost all applications within 72 hours against a number of flexible pre-determined risk rules. The system will have the ability to process low-risk applications without any manual intervention by the TA.

The way that an application is treated will be determined by a "*Decision Service Outcomes and Activities*" process, which will effectively channel applications in three different paths for further processing (see figure below).



Decision Service Outcomes and Activities



| 04/01/2012 | 5

2.4. Central processing of applications for VAT registration

Whether to opt for centralised or decentralised processing of VAT application forms is a choice that is based on many factors which will differ within each IOTA member country. Some of the key factors that influence

this decision include culture and tradition, organisational structure, geographical considerations, political factors, and so on. For this reason the matter is for individual TAs to decide upon, based on their own situation, but the task team did identify advantages and disadvantages in both approaches and these are provided for reference.

Centralised Processing

Advantages:

- Concentration of resources
- No geographical limitations
- Build-up of competence and experience
- Potentially better management structure
- Equal treatment of applications
- Easier to use follow-up measures
- Reduced risks of corruption
- Less vulnerable to losses of competence

Disadvantages:

- Lack of local knowledge
- Lack of ability to make 'on-site' inspections
- More difficult coordination with local offices
- "Islands in the stream"

1.1. Decentralised processing of applications for VAT registration

The more common way of organising the processing of VAT applications is to decentralise the processing to a number of local or regional offices. Such an organisation calls for a coherent management and governance structure.

The Central or Headquarters Office must issue clear instructions, guidelines and manuals in order to ensure equal treatment of applicants on the local and regional levels.

Decentralised Processing

Advantages:

- Local knowledge
- Possibility to make visits to applicants
- Internal competition between regions/offices

- Supports essential cooperation and coordination with other functions within the region/office

Disadvantages:

- Geographical limitations
- Increased risk of corruption
- Losses of competence when skilled officers resign
- Lack of equal treatment between offices and regions

2.5. Attendance of applicant required at the time of submission

The right to request the attendance of the owner/applicant should be considered as a premium approach by a TA. Making such a request should however be permissible at any stage of the registration process (pre-, during or post-registration) to prove the authenticity of the applicant, and to further ensure the credibility of the application by interviewing the owner/applicant.

It should also be considered an important measure to have the right to require the attendance of non-resident foreign persons, since experience shows that foreign residents registering for VAT can pose a higher fraud risk.

3. PRE-REGISTRATION CONTROLS

This chapter describes the various measures that may be used during the pre-registration phase of the VAT registration process.

The key consequence of inadequate pre-registration controls is that a number of fraudsters may enter the VAT register, enabling them to inflict heavy revenue losses before the TA has a chance of stopping them.

TAs are therefore advised to put great emphasis on their pre-registration controls, in order to detect fraudsters at the earliest stage in the process and thus prevent them from entering the VAT register.

The pre-registration process can have different starting points, depending on domestic conditions and sharing of responsibilities between government agencies. The exact point at which the process comes under the authority of the TA therefore varies from country to country.

The time limits imposed on TAs for reaching a decision on whether to register a business for VAT is a further determining factor that can impact on the levels and types of pre-registration controls. To circumvent this obstacle, some TAs operate with dual time-limits in order to create space for pre-registration controls in cases of suspicious applications.

Pre-registration controls of new businesses must also be seen in the light of the definition of a new business. From a VAT registration point of view, a new business can be classified as an:

1. old business merging into a new entity which includes another VAT registered business
2. existing entity not registered for VAT, but operating in the VAT regime under an exemption scheme (thresholds, agriculture, etc.) or a different identification procedure
3. entirely new business starting in the VAT field for the first time

The level and quality of information available for pre-registration controls can be different according to the classification above. Whenever the TA detects information concerning the past activity in cases 1 and 2, this information must be used and cross-checked against the information provided in the current application form, in order to determine the fulfilment of the conditions for registration and to decide the risk score to be assigned to the current application.

In case 3, for entirely new businesses, much more effort should be put in place by registration offices, in order to collect relevant information for current and future risk analysis.

3.1. Conditions for VAT registration

The conditions for VAT registration are regulated by law in all countries. The conditions should aim to maximise the possibility of registering genuine suppliers of taxable goods and services with a minimum of effort and hindrance, whilst also enabling the TA to detect and prevent unwanted applicants from registering.

The regulatory framework varies from country to country, but the most universally common conditions require the applicant to:

- be involved in an economic activity

IOTA Report for Tax Administrations
Pre and post registration VAT controls

- supply taxable goods or services
- run a business capable of yielding a profit
- run a continuous business of a certain scale and frequency
- be independent from principal trading partners
- be a non taxable person applying for a VAT refund due to acquisitions of goods and services
- be a taxable or non taxable person due to acquisitions of services from third country (reverse charge mechanism)

Further conditions may apply on the national level.

In some countries the VAT registration is granted by an agency outside the TA, such as the National Register of Companies, which means the pre and post phases of the VAT registration are divided between two different agencies.

When the registration process is divided, the importance of electronic submission of application forms is increased, as this is shown to improve and speed up the exchange of information between the agencies. Pre-registration controls could in these cases include non-fiscal conditions and requirements provided for instance by the National Register of Companies, Social security agency, Customs agency, etc. For multi-purpose registration of this kind a common application form is recommended.

The outcome of the controls can be an automatic report indicating the fulfilment of the requirements to be exchanged between the different agencies and/or a risk score to be evaluated by the TA in order to determine whether or not to postpone the issuing of the VAT registration number.

3.2. How to balance efficiency and control level

The number of entries in the VAT register varies substantially between IOTA members. Those countries with a higher population tend to have more businesses than the less populated ones. The TA needs to strike a balance between the level of control activity and the disposable resources such as number of employees, IT support, etc.

One of the biggest obstacles to a desirable level of pre-registration controls is the imposition of time limits for reaching a decision on whether to register a business or not. Many countries have imposed short time limits, which makes it potentially difficult to perform adequate pre-registration controls.

Time limits force TAs to create ways of speeding up the processing, and there are several ways of doing this, such as:

- Automated processing of information
- Semi-automatic processing of information (for further detail see below)

The time limits indicate that TAs must be selective in which controls to carry out, and which applicants to target. In the following subsections the task team provides recommendations concerning which controls to perform as an absolute minimum, and which of the additional controls it is desirable to perform if time and resource permit.

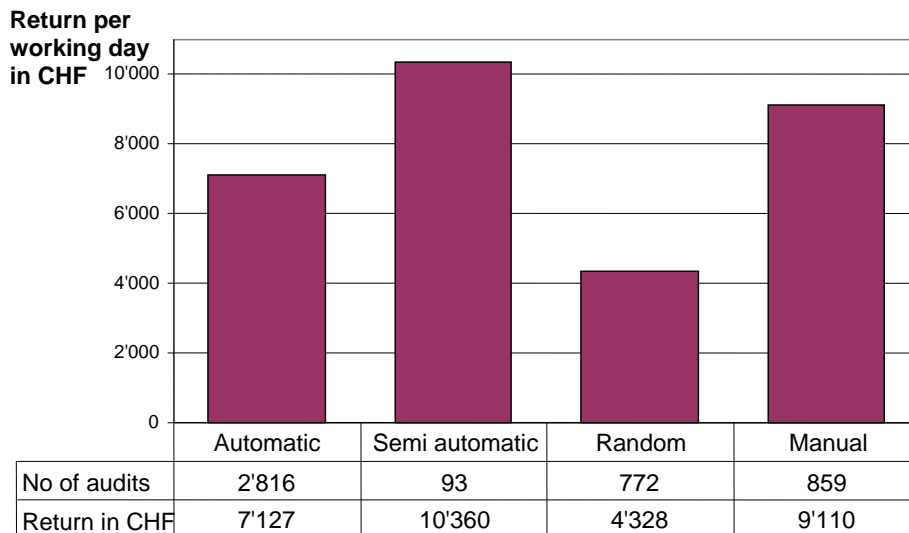
A semi-automatic process is a combination of automatic processing with cross-checks between various databases, and a manual evaluation of the results from the automated process. The main purpose of a manual evaluation and assessment is to let trained officers with skill and experience carry out the final selection.

- Goals of semi-automatic risk-based selection
 - Identifying additional cases and a higher detection result than with the fully automatic risk-based selection
 - Identifying more cases than with only manual assessment
 - Identify and test combinations of general risk rules
 - Potentially identify cases which are not identified by applying the usual risk rules
 - Test new risk indicators

The Swiss Federal Tax Administration has introduced a semi-automatic risk-based selection. The results of this selection system are presented in Graph no. 1 below.

Graph 1:

**Financial efficiency of external audit per type of selection in 2008
values as of 31.07.2008**



3.2.1. Minimum approaches

The minimum approach is to ensure the application form contains the sufficient level of data required for registration, and that the data is cross-checked against internal sources and standard risk rules applied for VAT registration.

3.2.2. Premium approaches

The task team suggests a two-step procedure for selection of applicants for in-depth inquiries and investigation, where some applications are processed in a "fast-lane" and applications from risky businesses should be processed in a "control-lane." The selection must be based on an effective and regularly updated risk management system.

This system offers a short time-limit for the "fast-lane" applications, so the businesses can quickly resume activities, while the "control-lane" provides TAs with the opportunity to perform more rigorous controls in complex cases or known high risk sectors.

Implementing various risk management systems to select applicants for further in-depth investigation is also considered a premium approach. The ratio of businesses to tax officers is obviously of importance. Countries with large numbers of businesses and a small TA will need a more comprehensive risk management system.

An example of a two-step process for VAT registration is the Danish "3-day/14 day" procedure.

Danish 3-day and 14-day procedures.

The Danish TA has an agreement with the Danish Central Business Register¹, where the registration, modification and cessation of businesses are recorded, to follow a 3-day or 14-day rule for VAT registration. The Central Business Register sends data to the TA assessing whether registrations, etc. should be approved or not.

The procedure implies that in uncomplicated cases registration must be completed within 20 working days after receiving the application, unless the application is related to cessation of the VAT registration. The goal is that new companies must be assigned a VAT registration number within 3 working days after application. The 3-day deadline also applies to cases of amendments to specific particulars of businesses that are already registered for VAT, such as changes in existing duty ratio or registration related to joint billing.

It should be noted that requests for cessation of VAT registration or changes of general trading particulars (name, address, etc.) is not included in the 3-day rule above because it typically takes longer than 3 days to handle such a procedure. The Central Business Register is working proactively towards ensuring that companies file electronic applications in order to shorten the process for alterations.

The process follows this procedure when a case is sent from the Central Business Register to TA:

- 1: Automatic registration (immediate registration)
- 2: 7-hour list
- 3: File List

1: Automatic procedure. There are a number of specific records that will be launched immediately after the registration is completed through the Central Business Register, such as the documentation for formation of

¹ The Central Business Register (CVR) is the central register containing primary data on all businesses in Denmark. The term National Register of Companies is used elsewhere in the report to describe such a register.

companies, registration of sole proprietorships with VAT, registration as employers (unless there is previous tax debts due) and changes to existing master data. A number of automatic controls ensure that relevant companies and individuals are selected for manual checks by the TA if tax debts are shown to be due (see also phase three 3 below).

2: “The 7-hour list”. There are some types of records that the TA has 7 hours to assess to determine whether there should be any further investigation. If the TA considers that it needs to check the registration further, then a manually inserted code is assigned to the application, which automatically transfers the case to the TA. The cases should, where appropriate, be transferred to either the File List (see below) or approved automatically based on automatic risk assessment.

3. The “File List”. There is certain information in the application that the TA must investigate further, related to the risk assessment determined by the TA. This can include special forms of enterprise (e.g. foreign businesses), difficult cases and businesses in sectors known to pose more risk, cases where the start date for registration requires clarification or any cases where there is a historical debt to the State. These cases are transferred via an electronic file listing to the TA and will remain with the TA until they have decided which investigative steps will be needed. The TA has 14 days (from the date of submission of the VAT application to the Central Business Register) to investigate and either require security as a condition of allowing the VAT registration, possibly denying registration or registering the applicant for VAT.

Another example of the application of a risk-based VAT registration method is The Swedish Categorisation Procedure:

Swedish Categorisation Procedure:

The Swedish Tax Agency (hereafter ‘STA’) applies a method that divides all applications into four different categories, each category being treated in a specific way.

The STA has set a goal of registering 85 % of all applications within 3 weeks of receiving the application. In order to achieve that goal all applications are divided into four different categories through a combination of automatic controls and manual checks undertaken by highly experienced officers.

A risk assessment analysis is carried out on all incoming applications.

Category 1
registration

No remark or further enquiries, immediate

Category 2

Additional information needed, then registration

Category 3	Further inquiries needed before registration, possible rejection of VAT registration application
Category 4	High risk applicant, high risk sectors, etc. Mandatory inquiries or investigation required before registration. Follow-up measures are compulsory, including monitoring of VAT declarations, income declarations, etc. Possible rejection of the VAT registration application

For some trade sectors all new companies within those sectors are regarded as high risk companies, i.e. they automatically fall within Category 4. Examples of high risk sectors are included in Appendix 2 of this report.

3.3. Check the National Register of Companies 2 and other databases

Reaching a correct decision on whether to allow VAT registration depends to a great extent on collecting, or being in a position to collect, all the information that is critical to the decision-making process. In addition to verifying the information provided by the applicant in the application form, it is essential that supplementary information is collected from a range of accessible databases.

In order to facilitate the use of supplementary information from other databases, it is recommended that the databases:

- are kept in an electronic format
- are directly accessible by relevant personnel
- support automatic exchange of information between State agencies
- include the date the information is recorded and amended
- can be adapted in response to feedback on data quality

Electronic storage and transfer of data, combined with interaction with other databases, is vital for effective VAT control. This allows for automatic access and a rapid exchange of information, which strengthens

² A National Register of Companies is a register which stores business information and makes the information available to the public. In many countries incorporating and dissolving businesses is a function of the National Register of Companies.

the fight against VAT fraud by tapping into a much larger pool of relevant information than would otherwise be available through a single database.

Information included in the application form is usually verified before registration through the National Register of Companies, which normally keeps basic information about the business. Many countries have a direct electronic connection with the National Register of Companies.

However, there are also a number of other databases which should preferably be consulted before a decision on registration is made, some of which are listed in the subsections below.

3.3.1. Minimum approach

The task team considers the minimum requirement to be a cross-check against information held on internal databases available to the TA.

Examples are databases which offer information about:

- registered taxable persons
- income tax returns
- VAT returns
- VAT Information Exchange System (VIES)
- social contributions

3.3.2. Premium approach

Beyond the minimum approach described above, a number of databases which are usually outside the immediate control of a TA could be considered.

IOTA Report for Tax Administrations
Pre and post registration VAT controls

Examples of such external databases are:

- National Register of Companies
- Enforcement agency information (Police, Customs, Trading Standards, licensing authorities, etc.)
- Municipal and local government registers
- Property register
- Land register
- Forestry register
- Fishing register
- Customs database
- Employment agency data
- EU subsidies data.
- Social insurance register
- Driver and vehicle licensing registers
- Traffic licence register for haulage businesses and professional truck drivers

The TA should work towards removing any of the legal and technical restrictions on access to such databases, as they may increase the awareness of the TA of aspects which may be of importance to the decision whether or not to register the applicant for VAT.

Collaboration between the TA and other government agencies should be established in order to improve and speed up the exchange of information. This may require the TA and agencies to consider legal issues of access as well as technical problems such as the format in which the information will be kept and exchanged.

Most TAs have a central coordinated register of legal entities. The Task Team uses the term National Register of Companies in this report, but as the structure and authority of such registers varies from country to country it is difficult to find an accurate description. Such central registers can consist of basic data from various affiliated registers (e.g. the VAT register, Employment agency, Statistical agency, etc.). The basic data from the central register provides the basic data in the VAT register, such as business name, business address, board members, business partners, statistical information such as NACE codes, and so on. This information is normally updated automatically. Some of the changes in the databases prompt a notification to VAT officers that further inquiries might be necessary.

The VAT register provides further information from internal TA databases that can be considered before granting VAT registration to the applicant. Examples are information from the Population Register to confirm the status of the applicant (who he is, where he was born, where is he now

living, etc), and from other registers that record the tax history of the applicant, his previous business involvements and so on. This information can rarely be used to deny registration on its own, but it may provide an insight into whether the applicant should be more closely monitored in the period after registration.

In the case of applications from non-residents it should be considered as a premium approach to seek information from other TAs through the existing exchange of information agreements.

3.4. Cross-checking information against other sources

3.4.1. *Minimum approach*

It should be considered as a minimum approach to run cross-checks against internal databases. But, in addition to the common internal registers described in section 3.1.1 above, cross-checks should be made against various external sources of information such as:

- Internet Search Engines for the registered and trading names of the business
- Internet Search Engines for the name of applicants
- Business websites (e.g. is the company in the same business as stated in VAT registration form, do they operate from the address they declared on the application, are there other telephone and email contacts, etc?)
- Other National Business registers, if available

Most TAs have access to a variety of databases and the information they provide needs to be processed and structured to ensure that it is relevant to the aim of enhancing pre-registration controls. In most countries the level of available information is enormous. Many countries have plenty of sources of information, but the information is spread so widely, and not structured or organised in a way that makes it immediately suitable for VAT pre-registration controls. Therefore, the biggest challenge for the TA is to extract the right information from its numerous databases, store and maintain the data in the most useful format and make the best use of it for VAT registration control purposes.

It is quite obvious that Internet access should be considered as a very important feature for all controls in general and for VAT Registration Controls in particular.

A TA needs to create and establish computer-based business rules to run systematic checks against the information given in the incoming applications (this aspect is considered in more detail in section 3.6.1 below). The selection process can be performed on a national, regional or local level depending on the organisational structure of the TA. Based on the result of the selection, the appropriate actions can be taken by officers, again on a national, regional or local level.

Many TAs have developed their own tools to perform cross-checks by creating business rules.

Equally, several TAs use more advanced selections and data mining tools such as SAS MA, including SAS Enterprise Guide, SAS Enterprise Miner, together with their different data warehouses to analyse available data in more detail. As another example, in the United Kingdom, HMRC uses 'Detica NetReveal' software for performing some of their risk assessment automatically.

3.4.2. Premium approach

Additional sources of information can include:

- European Business Register (Amadeus, Zephyr)
- Other International business registers
- National telephone directory
- Google Earth checks on address or premises
- Google Street View
- National Map Services or Street Services

Cross-checks should be made against external databases, as listed in section 3.3.2 above. The more sources of information that can be considered and analysed, the more assurances the officer has of the business' intentions. Many TAs can tap into a vast pool of information, but it is quite common to find that the information is historical and therefore outdated, limiting its use for risk assessment purposes. Consequently there should always be a validation of the date of the information which is used, and a systematic approach should be taken to keep the data fresh and updated with the latest information available. Databases should be made compatible, and where this is not currently the case it should be a priority for the TA.

TAs should continue to expand the number of data sources they use that allow for automatic exchange of relevant information.

Manual checks, such as internet searches, checking social media and placing calls to other agencies, should also be considered as premium approach.

With regard to foreign businesses applying for VAT registration, it should be customary to request information from the TA of the country of origin.

3.5. Risk assessment classification

A TA has a lot of collective areas of competence at their disposal. This competence is dispersed across the organisation. Each TA must ensure that officers working with VAT registration controls are highly skilled and for this reason the TA should introduce educational programmes, a culture of continuous learning, benchmarking with other TAs and encourage input from officers from other areas of the organisation through, for example, job shadowing and exchange programmes. The TA should also issue guidelines, instructions, operating manuals, even templates for questionnaires on such material, in order to support and increase the ability of the officers to identify and fight VAT fraud.

It is accepted that a TA will rarely have enough resources to perform sufficient controls, which means a selection must be done, based on a risk assessment. Classifying businesses according to risk is an area where the task team concludes it is not necessary to consider minimum and premium approaches. Instead the focus should be aimed at examining the information available in the best possible way.

The task team has compiled a list of examples of **risk indicators** which could serve as a basis for an initial VAT registration risk classification:

- Known to operate in a high risk business sector
- No inventory
- No stock
- No trading permit (compulsory for some trades)
- No permanent trading address
- Use of PO Box address or known accommodation address
- Blacklisted address
- Very young/old person
- Previous trade ban or other trading sanction
- Previous convictions for tax fraud
- Previous involvement in Phoenix or insolvent companies

IOTA Report for Tax Administrations
Pre and post registration VAT controls

- Previous involvement in bankruptcy
- Foreign representatives
- Foreign addresses
- Board of Directors incomplete
- Changes to Board of Directors
- Suspicious representative
- No auditor linked to limited company
- Registration form contains different addresses
- Earlier Tax debts or incomplete tax payments
- Previous involvement in Missing Trader intra-Community (MTIC) VAT fraud
- Previous tax investigation
- Previous criminal investigation
- Suspicion of Straw men³
- Indication of triangular transactions or 'third country' trade
- VAT return not filed by earlier entities in which individuals were involved
- No employees
- Vague information about the line of business
- Difficulties in making contact with the applicant
- Place of business is the same as home address
- Place of business not appropriate for stated type of business
- One or more partners in the board reside in a tax haven
- Changes of ownership
- Changes of seat for legal persons
- Off the shelf companies
- Adviser known to TA as suspect or unreliable
- No email address
- No bank account details
- No telephone number
- No web site
- Anonymous information available
- Invoices (trading partners) - business exceeding threshold
- Same address, telephone number, bank account as many other applicants for VAT registration
- Earlier VAT fraud perpetrated by relatives or known associated persons

(NB - the above list is not exhaustive)

Not all of the risk indicators listed above will be suitable for electronic cross-checks or data-mining. However, all information should be entered into the computer system in such a way that the indicators add value to the risk process. For example, if a piece of information is classified, and

³ - a person whose importance or function is only nominal, as to cover another's activities; front.
- a fabricated or conveniently weak or innocuous person, object, matter, etc.

therefore cannot be recorded openly in the system, an option would be to have a tick-box which acknowledges that such information exists with an indication of how and where the information can be accessed.

In such circumstances a need arises for semi-automatic processing of available information. By semi-automatic processing we mean that a selection can be made electronically based on various predetermined risk indicators, and then assessed by experienced officers for a final decision on whether and how to control the business. Sometimes the electronic selection criteria can result in a high volume of cases being selected for further potential control, and in such cases the manual intervention by the officer may require him to adjust the risk scores to ensure a manageable number of cases for further investigation by the available resources within the TA.

3.6. Profiling

TAs should aim to set up specialised teams to profile applicants for VAT registration in real time. The purpose of this would be to alert the TA to any suspicious traits the applicant business may have. Ideally the profiling should be done as close to the registration decision as possible - preferably in advance of the decision.

The profiling should be based on the types of risk indicators listed in section 3.5 and cross-checked against the database information listed under premium approach in section 3.3.2. The TA should assign a score to each risk indicator, thus differentiating between the applicants based on a total score of risk. Certain intervals in the score should be made, in order to allocate the applicants to various segments with their own predetermined targeted response.

It is imperative that the team continually monitors and adjusts the risk scores in line with the identified fraudulent trends. The team will set the scores based on known indicators, which makes it important that detection of new trends among fraudsters is fed back from the post-registration control units to update existing known risk indicators and ensure the inclusion of new risk indicators.

3.6.1. *United Kingdom Near-Real-Time Profiling Centre*

HMRC has established a team called the Near Real Time Profiling Centre, which aims to profile applicant businesses as close as possible to real time. The profiling seeks to alert HMRC to any suspicious characteristics, according to a number of pre-set risk rules, which are explained in more detail below.

During the Task Team visit to HMRC, UK colleagues pointed out some of the shortcomings that the existing methods and procedures have:

Today's detection systems are struggling:

- **Rules encode what you know you are looking for**
 - BUT, they cannot discover new methods of operation or multiple people operating "below the radar"
- **Data mining helps to fine tune rules and discover what you don't know**
 - BUT, it only acts on one applicant at a time
- **Data matching techniques help provide "single views"**
 - BUT, they assume you have honest individuals providing reasonably consistent names, dates of birth, Social Security Numbers (PIN/TIN) and addresses - fraudsters usually don't
- **Manually prepared link analysis diagrams are invaluable in complex cases**
 - BUT, they are time consuming and only applied to a very small number of situations
- **Reducing thresholds on systems only results in too many false positives**

The risk rules will only include known indicators, which mean they must always be on the lookout for new trends and methods being used by fraudsters to enhance the risk rules and ensure that they continue to reflect the developing tactics of the fraudsters. Close cooperation between post-registration controls and the profiling centre must be ensured, so that new tactics are accounted for in the profiling activity.

HMRC has set up a networked data system for compliance risks, where 23 source systems with a total of 81 document types provide around 800 million records to base the risk profiles on. Examples are Frameworks (citizen name, address, employment history, etc.), Self-assessment, Corporation tax, Employee tax coding, VAT returns, Agent details, Stamp duty (property), Banks, Offshore information (EU), Dun & Bradstreet business performance and credit rating information, Companies House (directors, shareholders etc.), Domicile, Charities, etc.

The Connect system has access to 5 indirect data systems as networked data for repayment risk.

This data capture process allows the profiling centre to build social networks of indicators linking different businesses together (for example, through a common mobile phone or bank account number). This allows the profiling centre to set a risk score, which in turn leads to a targeted response. This accelerates the assessment and decision making process across the full range of non-compliance from the negligent to the fraudulent.

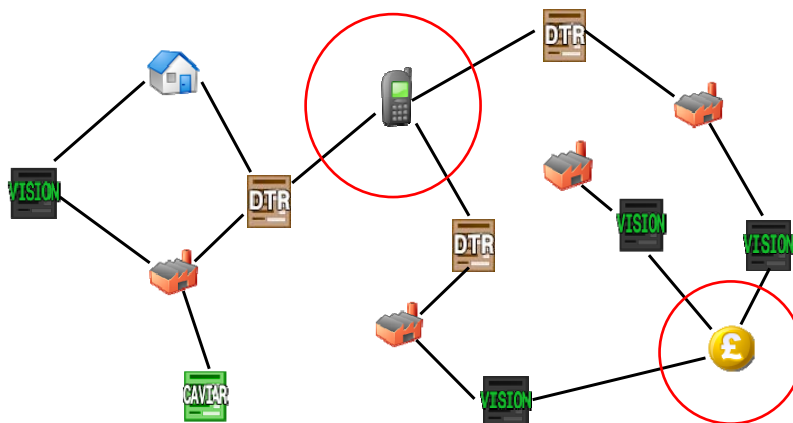
Risks can be assessed either at the point that a transaction happens (e.g. receipt of inbound application/sending of outbound payment), at an entity level - post event (business) or at the network level (identified suspect associations, root cause of error and fraud, etc.).

30 risk rules are run every night against 100% of VAT registered businesses in refreshed networks. All 'hits' are collated into one table, containing every business entity (whether they are VAT registered or not). Each risk rule has a risk level associated with it (Very High, High, Medium and Low) and each risk level has a weighting (50, 25, 5, 2). The scores for each business is added up, and the individual businesses will be put in a segment based on the overall score (Low, Medium, High-medium, High).

Network Risking

- **Example VAT Risk Rule:**

“More than two registered traders (DTR or VISION documents) share exactly the same mobile number.”



DTR = Departmental Trader Register; VISION = VAT Information System Inter Office Network; CAVIAR = Capturing and Verifying Information from Applications for Registration

If such a rule is triggered the case is flagged for handling and sent to a caseworker, who will carry out formal checks on information from the

form. The caseworker will then take appropriate action based on the checks.

Another method used for the systematic collection of information is to create a macro to compile information from various internal and external databases by activating a software macro and presenting all of the gathered information in one document, preferably in an electronic report format. This automation reduces the risk that a caseworker neglects or fails to gather certain information.

3.7. Possibility to require financial security or bank guarantee

TAs should consider the possibility to include legislative measures that give the TA the possibility to request a financial security as a condition of permitting VAT registration in cases where there is good reason to believe that there is a risk that taxes will not be paid. Examples of reasons for requiring a security will include a situation where a natural or legal person applying for VAT registration has owned, run or held a senior position in a previous business that was involved in bankruptcy, insolvency or other irregularities which led to tax revenue losses, and they now hold a similar position in an applicant business.

Financial security should only be requested of businesses where the TA envisages a risk of tax revenue losses. The opportunity to request security should be extended to apply in cases where risk management detects a number of those risk indicators listed in section 3.5.

The instrument of financial security should be seen in combination with other measures available to the TA, such as shortening the period for submission of VAT returns, for example by requiring the business to submit monthly rather than quarterly VAT returns and payments. Furthermore, the right to ask for security should apply not only at the point of registration, but throughout the life of a registered business. This creates an opportunity to sanction misconduct, or failure to provide security, by allowing for immediate deregistration.

The size of the security should be settled by each TA based on domestic circumstances, such as turnover and length of VAT periods, but experience suggests that this should typically be sufficient to cover non-payment of at least two VAT periods. Determining the size of security for businesses with no previous records should be done by looking at their declared estimated turnover in the VAT registration application form.

A variety of parameters can be chosen to trigger a request for security from businesses that are already registered for VAT. An outstanding debt

corresponding to a certain percentage of turnover is one example, a fixed amount of debt is another, and a failure to pay the amounts due from successive VAT periods is a third.

When the selected parameters are met, the TA should issue a letter requesting payment and notifying the business that a failure to pay within the given time-limit will result in a legal requirement for the business to provide financial security.

Failure to observe the security requirement should lead to deregistration for VAT purposes. Any attempt at reactivating the business after deregistration should only be accepted if the debts are paid in full and the original security request is met.

The financial security could, and perhaps should, be facilitated to embrace all taxes if the domestic conditions are conducive to this.

In cases of enforced deregistration, the TA should if possible inform the trading partners of the deregistered business, to limit the ability of the business to continue operating in the black market.

It should always be considered whether it is in the best interest of the TA to keep businesses registered and monitored, or to deregister them and run a subsequent potential risk of the business reappearing with a 'straw man', under a new name, and thereby trading under the radar.

An important consideration in this aspect is whether the applicant or registered business is a net payer of VAT to the TA or in fact makes claims to repayments of VAT from the TA. On the assumption of a liability to pay, a financial security or rejection can be an effective deterrent to fraudsters. If the expectation is a refund claim from the business, it might be wiser to register the business and keep them under closer scrutiny.

3.8. Possibility to collect further in-depth economic information

Being in a position to request in-depth economic information increases the ability of the TA to get an insight into the viability of the business applying for VAT registration. Requesting such information can bring to light the serious intentions of the business, by revealing whether the applicant has a proper business plan, budgets, financing and so on.

It is regarded as good practice to contact the applicant by telephone instead of simply issuing questionnaires, particularly where additional information is needed during the pre-registration procedures. The

experience of most TAs is that contact by telephone adds important quality to the overall registration process.

First, a telephone call offers real contact with the applicant. Secondly, a dialogue with the applicant can eliminate misunderstandings related to the application form, and quickly reveal the intent of the applicant, including the possibility to detect a risk of possible VAT misconduct or fraudulent behaviour.

This contact will also provide input to later measures open to the TA, including further information gathering activities, the need for and prospect of a visit, or risk appraisal resulting directly from that first contact.

If the result of the telephone contact indicates an increased risk according to known risk indicators, officers should continue the investigation.

The VAT registration process should be constantly monitored, revised and updated based on case experience in order to improve the process going forward. For example if the applicants keep repeating the same mistakes because they are misinterpreting information and questions in the application form, the TA should look to review the questions being asked and use this information to further develop and improve the data collection process.

3.8.1. Minimum approach

All TAs should have an option of requesting and assessing in-depth economic information such as:

- Budgets
- Bookkeeping and other records of the business
- Details about the business
- Rental or lease agreements
- Stock and inventory
- Financial information, how the activity will be financed
- Bank information
- Insurance
- Authorisation/licences
- Membership in trade bodies and associations
- Customers
- Suppliers
- Marketing
- Advertising

- Intra-Community trade

3.8.2. Premium approach

The investigation of suspected carousel fraud/MTIC (Missing Trader Intra-Community) VAT fraud increases the need for additional in-depth economic information. Due to the risk of heavy VAT losses involving these forms of VAT fraud, a TA should be empowered to request targeted information which put the applicants under an obligation to disclose the real intentions behind their applications.

To help reveal potential fraudsters, the TA should be in a position to request more specific information about:

- loans and investments
- anti fraud measures
- terms of sale
- third party payments
- accounting information
- assets
- staff
- transports and storage
- stock control

3.9. Pre-registration visits/audits

Visiting or performing an audit of an applicant business before granting VAT registration can often offer the most reliable information on which to base a decision on whether to register the business or not.

3.9.1. Minimum approach

A TA should be entitled to carry out pre-registration visits to businesses applying for VAT registration..

A TA which has different control units responsible for the same tax should coordinate their activities through a national system in order to prevent replication or overlap of visits, co-ordinate their controls activities and ensure the issuing of relevant questionnaires.

3.9.2. Premium approach

Most TAs will not have the resources to make pre-registration visits to all applicants, which means a selective visiting programme must be used. The selection of businesses for visits should always be based on a risk assessment. Where suspected MTIC businesses are identified they should be visited quickly and preferably through unannounced visits.

Businesses are geographically spread across the country, which could prevent or even exclude the possibility of the registration personnel from being able to make the visit themselves. A system should be put in place where registration personnel can request personnel in other regions or offices to carry out a visit to an applicant's business. Guidelines and questionnaires should be produced to improve the quality of the visit and inspection, since the visiting officer may not always have the required competence in respect of risk-based registration procedures.

It should be considered a premium approach to have the legal basis for the TA to carry out unannounced visits.

There is a need for TAs to be more proactive with regards to visits, with greater levels of fieldwork. It is clear that all the relevant information can't be collected or assessed fully if this process is solely based on submitted questionnaires or application forms, even when this includes risk-based desk work. Although visits are considered time consuming and require a lot of resources, visits to the business premises are highly recommended particularly where the risk rules have suggested at an earlier stage that there is cause for concern.

Some TAs are moving more of their resources into visiting businesses. The strategy is to improve the service provided by the TA to businesses, educating and preventing them from making unintentional errors, and also making the TA more visible, which in itself helps to deter those who would actively seek to suppress payments of tax due or to commit tax fraud.

3.10. Communicating with applicants and professional advisers

3.10.1. Minimum approach

Preventive work before VAT registration is an important factor which can prevent or reduce mistakes by the applicant, lessen the workload of the TA, and potentially remove some of the barriers between professional advisers and the TA.

Every TA should provide relevant, high quality information on their websites. TAs should constantly aim to improve their websites and develop new features such as e-services, interactive guides, e-learning features, mailboxes, etc. Such information can also be useful for internal purposes. Call centres with generous opening hours enhance the service available to taxpayers, thus improving the quality of the information given and the interaction between taxpayers and the TA.

In this context it is also recommended that a TA arranges informative meetings for:

- new taxpayers
- accountants
- auditors
- consultants and advisers

Examples of areas such information meetings could cover include:

- Practical questions concerning the VAT registration procedure
- VAT rules
- VAT schemes
- Intra-Community trade: rules and regulations, VIES reporting.

3.10.2. Premium approach

Some TAs have developed web-based approaches, online taxpayer forums, online guides, 'smartphone' applications and other channels to exploit modern technology.

It should be considered as a premium approach for TAs to provide registration information in English on their websites along with registration guides, downloadable as .PDF files and so on.

The task team also considers it a premium approach to continuously accommodate information meetings for businesses and professional advisers. The meetings should be properly marketed through the TA website and other relevant tax professional channels. Targeted information can be directed to a selection of businesses based on the business sector they are in, such as separate meetings for businesses involved in intra-Community trade, e-commerce, etc.

It should also be considered a premium approach to make targeted visits to the premises of selected businesses to present information on specific VAT issues relevant to the business or business sector generally.

The information can cover:

- Tax rules
- Practical VAT registration matters
- Intra-Community trade: rules and regulations
- VIES reporting

Consideration should be given to specially trained information officers conducting these information meetings.

3.11. Possibility to register a company for VAT under special conditions

In most countries taxable persons can be registered as groups of persons under one legal VAT entity (hereafter - VAT group), being a body of two or more legal persons established on the basis of an agreement founding the VAT group in order to carry out mutual transactions within the State where they are registered, subject to certain requirements, which can include:

- members of the VAT group may be only VAT taxable persons;
- the maximum number of members in the VAT group is not limited;
- the VAT taxable person at the same time may not be a member of another VAT group;
- VAT group may be founded if the total value of taxable supplies of goods and services of at least one VAT group member during a period of 12 months preceding the month of submission of the application for registration of the VAT group exceeds the level required for registration.
- members of the VAT group may be:
 - companies belonging to one group of companies
 - a branch of a foreign operator (legal persons), provided that this foreign economic operator belongs to the same group of companies to which other members of the VAT group belong;
- the members of the VAT group have concluded an agreement founding the VAT group which indicates the main or representative member company;
- members of the VAT group can be reached at their legal address.

Members of the VAT group use the common VAT group VAT registration number in all transactions with persons not belonging to this VAT group.

In **Latvia**, it is possible to register a fiscal representative, being a taxable person that (according to a written agreement between the representative and the business seeking registration) is responsible for VAT payments to the State budget and represents a taxable person from a third country or a non-registered person from another EU Member State in the following cases:

- releasing goods for free circulation if these goods are to be delivered to a taxable person in another EU Member State;
- releasing goods for free circulation for further domestic consumption;
- domestic acquisition of goods if these goods are acquired for exportation purposes and are placed in a Customs warehouse or excise warehouse for future export;
- intra-community supply of goods if these goods are acquired for exportation purposes and are placed in a customs warehouse or excise warehouse and subsequently exported

The taxable person is registered in the Latvian Register of Value Added Tax Taxable Persons as a fiscal representative and the person is given a separate (new) VAT registration number if the taxable person meets the following conditions:

- at the moment of the submission of the application is already registered in the VAT register for at least two years and is continuously performing an economic activity;
- at the moment of the submission of the application has no tax debts and fulfils their debt obligations;
- the natural person or legal person has no conviction for fraud, falsification of documents, tax evasion or other criminal offences which might have an impact on the calculation of tax amounts;
- submit timely tax and informative returns, requested documents and information that is needed for tax calculation;
- is reachable at the registered legal address or declared place of residence;
- has provided bank or insurance company guarantees;
- is the client of the Electronic declaration system of the State Revenue Service of Latvia.

List of common schemes

A variety of different conditions are laid down in EU member States' legislation in relation to the registration for VAT under special schemes and arrangements. In this part of the guide we provide you with an overview of our findings in relation to the requirements and individual TA approaches to VAT registration under special conditions currently imposed by those countries. Special arrangements apply in respect of:

- VAT Groups
- E-Commerce
- Agricultural
- Flat rate
- Distance selling
- Charities - non profit organisations

VAT Groups

The rules regarding VAT groups vary considerably from one EU member State to another. A VAT group is treated in the same way as a single entity or company registered for VAT on its own. Since cross-border VAT groups do not exist, only locally established companies can be members of a VAT group. VAT grouping systems in the EU are local systems. This means that foreign (non-resident) companies, requiring a local VAT registration for locally performed transactions, should register and perform VAT reporting individually, even if the multinational corporation to which they belong have several local subsidiaries, potentially all being part of a local VAT group.

VAT grouping is a facilitation measure by which two or more bodies corporate can be treated as a single taxable person for VAT purposes. This means that goods or services supplied to one member of the VAT group by third parties are considered as supplied to the VAT group. The goods or services provided by the individual members of a VAT group to third parties are considered as provided by the VAT group. As a result, the VAT status of the VAT group, and its right to deduct input VAT, is determined solely on the basis of the transactions of its members with third parties.

There are differences in the requirements to be registered as a VAT group in the IOTA Member TAs that include the possibility in their legislation, but most commonly "bodies corporate" can form a VAT group if each has an establishment in the same state/ territory. Another typical requirement is that the Group members are under common control and they all meet the eligibility criteria. The registration of such a group is made in the name of the 'representative member' by submitting the relevant application forms

to register as a VAT group. The representative member is responsible for completing and submitting a single VAT return and making VAT payments or receiving VAT refunds on behalf of the wider group. However, all the members of the group remain jointly and severally liable for any VAT debts that the VAT group as a whole may incur.

In some IOTA member countries there are the legal powers to prevent a company joining a VAT group and to remove an existing member from a VAT group where this is considered necessary for the protection of the revenue. Such protection powers are used when the TA considers that a revenue loss follows as a direct consequence of the business operating within a VAT group. To illustrate this, in the **United Kingdom** a "revenue loss" is potentially inherent because no VAT is charged on supplies between VAT group members, the logic being that if both members are fully taxable the amount charged will be paid and recovered in equal measure, resulting in a nil amount. However, this may not be the case where the receiving member is not able to recover the VAT in full and inclusion of that business in the VAT group may actually be a deliberate measure to effectively override the lack of ability to recover that VAT if the single business was trading outside the VAT group.

E-Commerce

This presents a major challenge for TAs, given the often multi-jurisdictional nature of the transactions and the potential anonymity of the parties involved. Supplying goods over the internet to customers in a variety of EU member States can therefore impose a significant burden on businesses in terms of monitoring levels of supplies made in each State and complying with the differing requirements.

Another potential area of difficulty with internet sales is identifying and verifying the customer's status. When a business is active in e-commerce trading, special VAT rules may be applicable in many countries. Under these rules, due to the introductions of an EU Directive aimed specifically at this market, a digital service supplier established outside the EU supplying digital services to a non-taxable person established or residing within the EU is in most cases obliged to charge VAT to that customer at the VAT rate applicable in the country where the customer receiving those services.

For the purpose of the EU Directive, digital services include the electronic transmission of software, games and information in a broad sense, as well as the subscription to radio and television channels, pay-per-view and other services supplied online via (international) databases and networks.

Agricultural - Compensatory VAT scheme for farmers

There is a special VAT scheme known as the "agricultural flat rate scheme" for farmers. The application of a specific VAT rate scheme for farmers is only possible if their total amount of income during a year for goods and services supplied in the course of their economic activities does not exceed a specified threshold. Such farmers are not registered for VAT in the ordinary way and consequently they cannot reclaim input tax on the purchases they make. There are also further specific limitations, such as the size of a farm. In case the total amount of income exceeds the pre-defined threshold, the farmer has to register for VAT in the normal way and cannot apply the compensatory VAT rate. Therefore it is important that cross-checking of data is carried out so that a farmer who should be normally registered for VAT does not continue to apply a compensatory VAT rate under the scheme when he is not legally entitled to do so.

Farmers to whom the compensatory VAT rate scheme is applied have the right to receive from their purchasers/customers a compensation for agricultural products when those agricultural products are supplied to taxable persons who are not farmers eligible to the VAT compensatory rate scheme, or where the agricultural products are supplied as an intra-Community supply to a legal person identified for VAT purposes who is not a taxable person. That means, that farmers charge and keep "a flat rate" addition based on a given percentage (4% - UK, 6% -LT) when they sell qualifying goods or services to VAT registered customers. This addition is not VAT, but rather it acts as compensation for the fact that input tax is not recovered on purchases. The flat rate addition is part of the business takings and should be included in subsequent sales figures.

Flat rate scheme

The flat rate scheme for small business was introduced in EU legislation to reduce the administrative burden imposed when operating VAT. When a flat rate scheme is being used a company pays a fixed percentage of its VAT inclusive turnover.

Using standard VAT accounting, the VAT paid to the TA or claimed back is the difference between the VAT charged to customers and the VAT paid on the purchases.

Under a flat rate scheme the actual percentage depends on the type of business; that is to say there is a range of flat rate percentages that corresponds to different business sectors. The flat rate scheme is not that beneficial for companies that make a lot of zero-rated or exempt sales or

buy a lot of standard-rated goods as there is no possibility to reclaim VAT on purchases. However, it should be noted that in each EU member State there may be different flat rates with different requirements, advantages and disadvantages. For instance, if the taxable turnover of a company is less than a certain amount, there is a possibility to simplify their VAT accounting by calculating VAT payments as a percentage of the total VAT-inclusive turnover. Although there is no opportunity to reclaim VAT on purchases, this is taken into account in calculating the flat rate percentage that the businesses must use.

The Flat Rate Scheme can reduce the time needed for a business to meet its accounting requirements and calculate the VAT liability due to the TA. Even though there is a requirement to show a VAT amount on each sales invoice issued to customers, there is no need to individually record how much VAT is charged on every sale in the business accounts. Moreover, some TAs include an incentive to encourage the uptake of flat rate accounting. For example, in the **United Kingdom**, if a company is newly VAT registered it can reduce its flat rate by 1 per cent until the day before the first anniversary of their VAT registration.

Distance selling

As a general rule, sales of goods to consumers in the EU internal market are taxed in the country where the seller is situated. Distance selling from one EU member State to another is an exception to this rule.

Distance selling takes place when a supplier from one EU member State supplies goods and is responsible for their delivery to a private individual or a non-VAT-registered person in another member State (typically, these will be internet sales and mail order selling). Contrary to the principal rule, selling of this kind is taxed where the goods are when the dispatch or transport ends. If the volume of such sales exceeds the predetermined threshold for distance selling set by the member State of destination⁴ the distance selling rule should be applied. The thresholds applicable in the IOTA region are shown in Appendix 3. Businesses engaged in distance selling must register and account for VAT in the member State of destination once the threshold of that State is exceeded.

The supply of goods is effected locally if the goods are dispatched or transported by or on behalf of the supplier from a member State to a purchaser locally, and the supply does not qualify as an intra-Community acquisition. Even when the transportation or dispatch of goods starts

⁴ http://ec.europa.eu/taxation_customs/taxation/vat/how_vat_works/distance_selling/index_en.htm or http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/traders/vat_community/vat_in_ec_annexi.pdf

outside the European Community and the goods are delivered into a State via the Member State of importation, the goods are considered to be delivered into the State from another member State. According to the distance selling rules, VAT is charged locally on sales of goods if the distance selling by a supplier locally exceeds the threshold of that State in a calendar year.

The distance selling regulations are applied only when the purchaser is a person whose purchases do not qualify as intra-Community acquisitions. In practice, the distance selling regulations apply when the purchasers are private individuals or other unregistered entities. If the purchaser is a VAT registered person, he is liable to pay VAT on intra-Community acquisitions effected in that member State.

Also, it should be noted that in most countries there is no limitation to registering as a VAT payer on a voluntary basis. This means that a business engaged in distance selling may opt to be taxed in the country of destination instead of the country of departure by submitting an application to the authorities of the country of departure. Some form of control action is required for companies that are registered as VAT payers for distance selling because these companies can otherwise avoid declaring the real value of supplied goods as the ability to control persons in other member States, who are not VAT payers, is low.

Acquisitions by non-taxable legal person or exempt persons (under the 2nd subparagraph of Art. 3 the VAT Directive 2006/112/EC)⁵

If a business is not registered for VAT locally and they acquire goods in that State directly from a VAT registered supplier in another member State, they should be required to register for VAT if the total value of these goods exceeds the threshold set by that Member State in a calendar year.

A business may also register voluntarily if they can satisfy the TA that they make, or have a firm intention to make, relevant acquisitions within that territory.

Charities - non profit organisations

Charities and non-profit organisations are not necessarily the same thing. There are special VAT exemptions and reliefs available for certain types of non-profit organisations. They are also subject to certain conditions and restrictions. In some countries in order to be recognised as a Charity you have to register at a predefined institution. In the case where the taxable

⁵ http://ec.europa.eu/taxation_customs/taxation/vat/how_vat_works/distance_selling/index_en.htm or http://ec.europa.eu/taxation_customs/resources/documents/taxation/vat/traders/vat_community/vat_in_ec_annexi.pdf

turnover of a Charity exceeds a yearly threshold it may have to register for VAT, though voluntary registration may also be an option. In case the activities are exempt from VAT, no VAT registration is available, but it should be noted that in each member State the situation concerning VAT registration of Charities and non-profit organisations is different.

VAT fiscal representative - registration of Foreign Companies for VAT purposes

In most countries the tax authorities must be informed before the start of economic activity or within 30 days after exceeding the threshold for VAT registration. The same guidelines apply to both established and non-established taxable persons. With regard to the method of communication with the TA, the same rules are applicable for established and non-established persons.

Non-established EU persons must in principle appoint a VAT representative that is jointly liable for VAT related debts. This means that taxable persons who are not established locally, and carry out economic transactions subject to VAT for which they are liable and which is deemed to be incurred on the territory of that State must appoint a fiscal representative. This particular practice is also applicable for non EU countries. For instance, in Norway, Switzerland and many other jurisdictions a foreign company may register for VAT without the requirement to form a local company; however they must appoint a local VAT Representative. The representative and company are jointly liable for the reporting and payment of VAT to the tax authority. In addition, the agent is responsible for all communications between the company and the tax authorities. A security (bank guarantee or deposit) at a level determined by the tax authorities could also be required as a condition of registration.

In most cases the representative must calculate the VAT on the goods or services supplied or acquired by the foreign business, submit VAT returns on behalf of the foreign business and pay any VAT due. The fiscal representative is jointly and severally liable, with the foreign taxable person, for the performance of tax obligations in respect of VAT. Any foreign business failing to designate a fiscal representative could be refused registration for VAT. If the foreign business has not been registered as a VAT payer locally and supplies goods and/or services on the territory of this country, the purchaser (except private persons) of those goods or services is obliged to calculate the VAT due and pay it.

Under appropriate legal provisions there is also a possibility for a TA to require a guarantee with foreign businesses who apply for registration in any case where the TA considers that the absence of a guarantee would entail an obvious risk of losses. Determining which form the guarantee must

be submitted (e.g. cash deposit, surety, mortgage or pledging of goods, securities or claims, etc.) is at the discretion of the individual TA.

When a VAT representative is appointed, whether or not they are jointly liable, the most frequently requested information can be summarised as follows:

- information about the identity of the VAT representative (the power of attorney), for the business which has to be registered as a VAT payer locally;
- information about the establishment of the VAT representative (the name, address, business ID code and contact information of the representative);
- Information about the liability of the VAT representative.
- information/proof that the representative is competent to handle the duties of a representative in compliance with the national VAT legislation, if the representative's line of business is related to something other than accounting and bookkeeping services, etc.

As a result, it is therefore common practice to require a full bank guarantee in favour of the fiscal representative to protect the State from possible losses.

In most countries, the fiscal representative is required by the national tax legislation to ensure that:

- The foreign business is properly registered with the local tax office
- The business is fully compliant with the rules on invoicing, VAT treatment, exchange rates, etc.
- Accounting records are maintained to meet local standards, and that they are readily available for inspection by the tax authorities
- All VAT and associated filings are correctly prepared and submitted
- Enquiries and tax inspections from the VAT office are handled professionally

It should also be mentioned that some members, despite the general requirements for representatives indicated above, have several types of fiscal representation. For example, the Netherlands have fiscal representatives who can operate with a general licence and with a limited licence.

A fiscal representative with a general licence acts on behalf of a non-resident company with respect to all its supplies of goods and services for which VAT is due, intra-Community acquisitions of goods and the import of goods.

A fiscal representative with a limited licence can only act on behalf of a non-resident company for the import of goods and subsequent supplies of these goods. Thus, a fiscal representative with a limited licence cannot act on behalf of the non-resident company for its intra-Community acquisitions or services rendered.

3.11.1. Special VAT number for intra-Community transactions

Some TAs issue a specific VAT registration number to businesses that are involved in intra-Community trade. This could be considered as an administrative burden on the business and also for the TA.

However, a specific VAT registration number for intra-Community trade presents an opportunity for additional control activities on the part of the TA, as this easily distinguishes intra-Community traders from the rest of the businesses registered for VAT.

Based on the fact that practically all IOTA member countries have opted against introducing a VAT number specifically for intra-Community trade, it is the opinion of the task team that the best option is that each business has only one VAT registration number.

Even though it is valuable to be able to distinguish intra-Community traders, the advantage is outweighed by other factors, notably the administrative burden placed on taxpayer and TA alike and the fact that non-filers in the intra-Community transaction system would have a legitimate VAT registration number for international trade. Two different systems for the same tax can potentially cause control problems.

Another solution provided by some EU member States is to provide a unique VAT registration number but at the same time to make use of the VIES system infrastructure to distinguish high risk operators from lower risk ones.

Those companies registered for VAT or applying for a new VAT registration number need to submit a specific application in order to make intra-Community transactions, without which they are not visible in the VIES system available through the EU Commission website or national VIES system. Most of the time the applications to be included in the VIES system in those Member States triggers an automatic risk analysis for VAT purposes and the resulting risk score provides an indicator to either deny the authorisation, perform further analysis or, alternatively, to include the applicant in VIES as a reliable operator.

3.12. Requirement to submit monthly VAT returns as a control measure

All the major fraud schemes, notably carousel fraud and MTIC, exploit the different lengths and the stagger of taxable periods to gain a head start on the TAs. Fraudsters will seek the opportunity to submit longer VAT periods for those businesses responsible for output VAT and shorter periods for the businesses deducting input VAT. TAs must be alert to this scenario when processing VAT applications.

Shorter VAT periods enable TAs to uncover and stop potential frauds by getting to the suspect businesses earlier. Longer VAT periods increase the time span before the business receives any attention from the tax authorities, and thus gives the fraudsters more time to inflict fiscal damage.

TAs should have the option of shortening the VAT period in cases of suspected VAT fraud. The task team recommends those TAs who do not have this option to work with their legislators towards acquiring this possibility.

One TA has the ability to shorten the VAT period down to one day in the most extreme circumstances, i.e. MTIC (Carousel Fraud).

3.13. Possibility to postpone the granting of a VAT registration

TAs should have the option to postpone VAT registration in cases of doubt until the applicant has provided sufficient evidence to prove that the business is legitimate.

Examples of when it should be permissible to withhold a registration include cases where the applicant:

- cannot be contacted by the TA
- does not respond to questionnaires within given deadlines
- does not fulfil requests and requirements of the TA
- has provided insufficient or incorrect data in the VAT registration application form

3.14. Possibility to deny or reject the application for a VAT registration

In order to successfully combat VAT fraud it is highly recommended that legislators provide a legal basis for the TA to deny or reject an application for VAT registration.

Applications should be denied when preset conditions have not been met, or in cases where legitimate requests for further information, as mentioned in the section above, go unanswered by the applicant.

3.14.1. *Minimum approach*

Registration should be denied when:

- there is no evidence of economic activity or the intention to carry out economic activity
- the applicant does not provide requested information
- legal conditions for VAT registration are not met
- insufficient or incorrect data in the VAT registration application form (deny or investigate)
- the applicant cannot be contacted by the TA
- the applicant fails to prove his/her real intention to carry an economic activity when further enquiries are made by the TA
- fraudulent activity is detected

3.14.2. *Premium approach*

Denying an application should be considered when:

- fraudulent activity is suspected or detected
- the use of "straw men" is suspected
- the applicant has a history of previous tax debts

IOTA Report for Tax Administrations
Pre and post registration VAT controls

- the applicant has had previous involvement in "Phoenix" or contrived insolvent companies (businesses that regularly go bankrupt and are resurrected)
- the applicant has declared that he trades from a blacklisted address
- the applicant does not attend in person when requested to do so by the TA
- a requirement of a domestic tax representative for foreign applicants is not met

In most cases denying an application for VAT registration based on suspicion alone is not possible, even though a number of risk indicators may have been triggered. The legal rights and obligations of a taxpayer mean that TAs do not have the scope to simply deny VAT registration. In the event of an application for VAT registration when risk indicators have been triggered, the registration should be carried out with additional conditions that aim to reduce the risk of non-compliance or fraud. Shortening the VAT period, as mentioned above, is of course one condition that can be imposed. Internal conditions such as obligatory follow-up measures for a specific period of time and specifically targeting suspicious businesses should be considered as a premium approach. Follow-up measures consist of monitoring the following events:

- First occurrence of refund
- Major increase in turnover
- Major increase in output VAT
- Major increase in input VAT
- First occurrence of intra-Community trade
- Change of ownership (if automatically reported)
- Change of Directors (if automatically report)

When these incidents occur, the TA should opt to instigate further action, such as:

- Issue of relevant questionnaires
- Telephone Inquiry or desk audits
- Visits (announced/unannounced)
- Audits
- Deregistration action

4. POST-REGISTRATION CONTROLS

4.1. Introduction

Post-registration control is the area where most TAs choose to allocate the majority of their resources in the VAT registration process. One key reason for this is that due to the short time limits for completing the registration process, many TAs have insufficient time to carry out in-depth pre-registration controls.

In order to determine the post-registration process it is necessary to:

1. verify all the actions taken by the TA during the pre-registration process;
2. categorise the information available to distinguish the different data types such as identification data, tax returns, payments, risk analysis reports and audit reports;
3. decide whether the available information has to be reconsidered: new information, old information to be updated, relevance of old information;
4. determine the step by step process to be performed and the deadline for concluding post-registration action.

The ability to efficiently and effectively go through these different steps depends on the degree of automation in the registration procedure and in the overall TA process. It is important for each TA to guarantee that a common minimum standard is met. In simple terms the post-registration controls can be divided into:

- (a). post-registration controls in cases where there has not been any risk analysis prior to registration
- (b). pre-registration controls on the basis of risk analysis in the registration stage, imposed within one year after registration
- (c). ongoing post-registration controls using risk analysis, performed by TAs in order to verify that the conditions and requirements for VAT registration are met in full and that the detection risk of non-compliance or fraudulent activity is correctly assessed

4.2. Definition of new businesses

Experience has taught us that new companies carry an inherently higher risk than existing ones, due to the fact that typically a TA has no information about new companies, which in turn means a decision must be reached without anything more than the information on the application form and no real knowledge of the business's prior conduct.

The basic idea behind defining a business as 'new' and then associating certain risks with such businesses stems from the fact that it is a common experience of TAs that the risks of wrongdoing, intentional or not, is higher with a business that has no previous trading history or experience. The risks are not exclusively confined to fraud, but may also include unintended errors in the VAT returns due to basic inexperience or lack of knowledge concerning the tax and their obligations as a VAT registered business.

Risks which are inherent in new businesses should be specified and analysed, and considered when carrying out monthly or quarterly credibility checks on the VAT returns. Results from such checks could act as "*early warning alerts*" to fraud investigation officers, as well as identifying registered businesses where educational or general compliance intervention by the TA is needed.

It should be considered good practice to pay particular attention to new businesses for a specific period of time after VAT registration is granted. The length of time a business should be categorised as new varies from three months to three years, depending on domestic circumstances. After expiry of the specified period, the business will be handled in accordance with normal procedures for established VAT registered businesses.

Emphasis should be put on offering help and guidance to new businesses. The rationale is that this will build trust and confidence in the relationship between the TA and the business, setting the business straight over unintended errors and last but not least give the TA a chance to gauge the overall credibility of the business. Such a strategy can ensure that basically compliant businesses that make unforced, unintentional errors are assisted and educated to get it right, reducing the rate of error and increasing the level of compliance in the future.

4.3. Control of new businesses

Enhancing the relationship between new businesses and the TA requires an element of leniency towards these businesses. However, leniency should

not come at the expense of controls. Instead, controls should be focused towards educating the business, whilst also keeping a watchful eye out of any signs of premeditated and deliberate misbehaviour.

4.3.1. *Minimum approach*

The minimum approach which should be carried out in respect of a new business is to adopt a unique risk analysis approach to new businesses, with the aim of identifying their activities such as:

- Extensive information gathering concerning their trading activities
- Monitoring the first few VAT returns submitted by the business
- Special attention to cases of non-filing or non-payment
- Considering compulsory deregistration in appropriate situations

4.3.2. *Premium approach*

The premium approach should include the following activities:

- Visiting programmes
- Targeted visits to high risk and non-compliant businesses
- Unannounced visit
- Monitoring high risk sectors - audit programmes specifically focused on identified sector risks
- Post-registration questionnaires
- Special instructions to businesses regarded as posing a risk, requiring them to submit additional information
- Unique coding of new companies in the TA registration computer systems
- Creating selection lists for targeted audits, desk audits, visits
- See also section 4.6 below (Questionnaires to identify risky VAT businesses)

Setting a target for the number of new businesses which should be visited is a decision for each TA to take, but it should be regarded as essential good practice.

4.4. **Registration threshold**

Most countries have legislated for a monetary turnover limit which must be exceeded before VAT registration can be granted.

There are pros and cons to setting a threshold for registration, some of which are listed below:

Pros

- The number of businesses potentially registrable can be estimated in advance, and the threshold set to maintain a certain level
- Small businesses can be kept out of the VAT register
- Non-profit businesses, hobbies or non-business recreational activities, etc. can be kept out of the VAT register
- Simplifies tax and other obligations for small business activities
- Lessens the administrative burden on small businesses

Cons

- Difficult to monitor the businesses
- Businesses can conceal business activity to avoid VAT registration
- Difficult to discover when a business exceeds the VAT threshold
- Zero threshold increases the administrative workload of the TA
- The imposition of a threshold is an administrative burden for the business in terms of requiring a second registration (in cases where the first registration is usually at the National Register of Companies)
- Invoicing taxable goods or services without VAT leads to suspicions or questions from the buyer, and a reluctance to trade with the business because they do not have a VAT registration number. It is a reason that many businesses trading under the VAT threshold request to be voluntarily registered.

4.5. [Checking whether the registration threshold is exceeded](#)

A TA can make use of a number of methods to establish whether an individual or business has exceeded the threshold for VAT registration.

Examples of such methods are:

- Information from internal tax registers/data warehouses
- Cross-checking against company income tax declaration or other declarations
- Cross-checking against income declaration of owner
- Monitoring private expenditure/cost of living/ lifestyle of the owner
- Reports from National Register of Companies/ Chamber of Commerce
- Cross-checks against Customs information and database
- External audit reports
- Cross-checks against VIES
- Check with external companies, telephone providers, utilities providers (gas, water, electricity), ISP providers, etc.
- Information available from other investigations/audits/desk audits
- Suppliers' list (when available from other audits)
- Bank statements
- Internet - e-commerce
- Impulse, tip offs, anonymous information
- Announced or unannounced visits

4.6. Questionnaires to identify risky VAT businesses

The TA can use comprehensive questionnaires to add value to the investigation of suspect cases. The aim of these questionnaires is to help the officers assess the wider risks of the company they are investigating, assisting them in allocating the appropriate resource and taking the relevant follow-on action.

The questionnaires can be quite extensive in their scope, which enables the investigator to select the most applicable questions in each instance.

An excellent example is the **United Kingdom VAT Risk Assessment Questionnaire**. It contains a large number of questions which are pre-sorted under various headlines. The headlines are presented below, with the number of questions under each headline listed in brackets, and the full questionnaire is attached as Appendix 4.

1. Company formation and administration (20)
2. Banking Information (4)
3. Loans and investments (5)
4. Marketing (4)
5. Anti fraud measures (3)
6. Terms of sale (10)
7. Third party payments (5)
8. Accounting Information (6)
9. Assets (10)
10. Analysis of Accounts (NB: To be undertaken when examining the accounts) (15)
11. Suppliers and Customers - General (18)
12. Commercial Viability (Integrity of the supply chain) (12)
13. Staff (4)
14. Stock Control (2)
15. Storage - Transport (20)
16. Inspection (75)

For an alternative example of a risk assessment questionnaire please see the **Swedish** example at Appendix 5.

4.7. Methods to identify dormant VAT registered businesses

Over time a large number of VAT registered businesses can cease to file VAT returns and become dormant companies. In most cases this is due to the natural ending of business activities. However, dormant companies pose a risk as they have the scope to become a tool for others to commit VAT fraud. Registration numbers which belong to dormant companies are often hi-jacked by criminals for fraudulent purposes. For this reason alone all TAs should consequently focus on deregistering dormant companies as soon as possible, once their dormant status has been established.

4.7.1. *Minimum approach*

A TA should have the legal power to deregister a business and should use these powers in the case of a dormant business. When a business stops filing VAT returns, enquiries should be made and the business deregistered as soon as possible if no sign of economic activity is found.

4.7.2. *Premium approach*

The TA should regularly examine the VAT register for repeated nil-returns and deregister the inactive businesses that are identified. The examination should ideally be automated, generating a batch of selected VAT registrations based on the nil return / dormant trading criteria. This ensures the automatic issue of a notice of deregistration to the business, unless a credible explanation is provided as to why it should remain registered. The letter should be worded in such a way that the failure of the business to reply within a reasonable period of time would lead to immediate deregistration. Businesses deregistered in this manner should remain under consideration for other controls, such as audits and visits, depending on the risk indicators.

4.8. Identifying missing traders, buffers, brokers, etc.

Missing Trader Intra-Community (MTIC) VAT fraud is the most damaging fiscal fraud in Europe. Every TA is forced to allocate considerable valuable resources to combat this type of fraud. In many European countries MTIC fraud is causing massive revenue losses, not least because this type of fraud can be performed with any type of taxable goods or services and the fraud exploits the intra-Community VAT rules combined with the limitations of TAs to keep pace with the level and pace of the frauds.

In order to combat VAT carousel fraud it is crucial to tackle the missing trader, as this is the point where visible fiscal fraud is committed.

It is the missing trader that inevitably fails to pay over to the TA the VAT that is due. This, however, is easier said than done. Fraudsters are well-prepared for this eventuality; they have a rapidly changing network of intermediaries and missing traders at their disposal. The vast numbers of intermediate links mean that the regular methods of TAs are often insufficient to detect the path to a missing trader in time. As soon as a missing trader is detected a replacement missing trader will have stepped into the network, the TA will be too late to act and the cycle of fraud repeats itself. If a TA is to be successful, the rate at which missing traders are traced and closed down must be increased.

The organisers of carousel frauds are able to introduce new intermediate links and/or missing traders at very short notice. If the TA were able to trace and prosecute intermediaries at a similar speed, it would become more difficult for the wheels of the carousel to keep turning smoothly. This is because it does take time for the fraudsters to establish new legal entities or to find other willing traders who do not have a criminal history with the TA and who are prepared to take the risk.

Intensive and swift action on the part of the TA, in combination with other preventive and repressive measures described in the following chapters, can make it possible to deactivate the carousels temporarily; or at least seriously disrupt their ability to operate. The assumption is that if the TA adopts an active approach to consistently undermine the missing traders' activities, the carousels will gradually dry up. An approach of this kind does of course require a relatively high deployment of resources as well as direct, properly coordinated action managed at a level above the local units.

4.8.1. Tools for identification

A coordinated national approach to tackling this type of fraud should focus on tracing the missing traders as quickly as possible. This can only be accomplished if the TA can follow the links in the chain at a rapid speed from the final link via the intermediate links on to the missing trader. After a missing trader has been traced, immediate preventive and repressive action (under administrative or criminal law) should be taken against the missing trader in question. Any financial means or assets should be seized to the extent that it is legally and administratively possible.

The approach that has been developed also provides for consecutive and sometimes even simultaneous actions in the administrative (auditing) and investigation fields. It is essential that TA personnel are provided with all the necessary information promptly in order to ensure the fast and effective coordination of their activities.

In chronological order, the following steps can be distinguished in the coordinated national approach:

1. identifying the carousel and tracing the final link
2. tracing the last intermediate link
3. tracing the other intermediate links
4. tracing the missing trader
5. carrying out an audit on the missing trader, possibly resulting in an administrative settlement
6. seizing possession of the missing trader's property under warrant of execution
7. initiating a criminal investigation into the missing trader if possible

8. criminal investigation into the “organisations” established by the missing traders
9. criminal investigation of the entire carousel network, with the aim of tracing and prosecuting the organisers
10. in-depth audit of the other links in the carousel, resulting in a criminal investigation and/or administrative settlement

Another important method used to identify missing traders is to monitor incoming VAT declarations to identify sudden or massive increases in turnover, output VAT or input VAT. A TA needs to implement automatic controls to detect such suspicious patterns or risky behaviour of VAT registered businesses.

The first occurrence of intra-Community or third country trade should also be monitored and the TA should consider paying extra attention to businesses that radically change their customer base, particularly where they quickly move from making in-country supplies to making increasing numbers of supplies to other EU member States and third countries.

In order to effectively detect suspected MTIC fraud it is essential for TA to have the ability to obtain bank information on cash flow, funding, money movements, etc.

Proactive control measures, such as visiting programmes to freight forwarders and brokers in order to prevent these intermediaries from getting involved in carousel fraud should also be considered as part of any premium approach. These activities should be combined with warning systems such as the '*yellow card*' procedure (The concept of the '*yellow card*' and '*red card*' actions is discussed further in the paragraph below).

Some countries have implemented legal regulations which give the TA the power to hold businesses jointly and severally liable for unpaid VAT when they are trading with businesses known to be involved in carousel fraud, simply on the basis that they are involved in the chain of transactions that are part and parcel of the overall fraud. This measure could be referred to as a “*red card*”, to use sports terminology. In Denmark they use a different method in which they issue a notification to the trading partners which outlines the consequences of carrying on trade with a suspected fraudster. This could be referred to as a “*yellow card*”. A trader who has received a notification, or '*yellow card*', and continues trading with the suspected fraudster, can then be held jointly and severally liable for VAT losses related to the transactions with the fraudster.

4.8.2. *Joint and several liability*

Joint and several liability is an important measure that several TAs have implemented in order to prevent and disrupt organised MTIC fraud.

A joint and several liability can be defined as “one-for-all-and-all-for-one” liability. Such a liability, whether it is founded on an agreement between parties or resulting from the connection between parties, defined by law, means that the liability for any VAT default is enforceable against all of the signatories (if based on an agreement) or those otherwise encumbered by such a liability, e.g. by way of law - as a group (not necessarily on a proportional or pro-rata basis), or against any of the players in the fraud chain as an individual, all at the choice of the enforcing party.

This ability to impose a liability on the various parties and businesses involved in a chain of fraudulent transactions is a very effective measure in combating organised cells of MTIC fraudsters, but it is just one measure that the TA can use..

More information can be found in the published IOTA Report on “Securing of Assets”, which can be found on the IOTA website, via the following link > <http://www.iota-tax.org/publications/iota-report-for-tax-administrations--securing-of-assets-333.html>

4.8.3. *Blacklists of suspected fraudsters or bogus companies*

Most countries have large numbers of VAT registered businesses. Among VAT registration applicants there will be businesses where the people behind the business have had previous involvement in tax fraud, with various degrees of gravity. Most TAs are deprived of the opportunity to register and maintain information electronically about the earlier fraudulent activities of individuals, due to legal constraints on holding this data and producing or publishing blacklists, etc.

VAT fraudsters are intent on registering for VAT, which means that a rejection of an application is usually met by another application from the same individuals in a different location or with a different stated *modus operandi*. Fraudsters are well acquainted with TA procedures and act accordingly to exploit this. There is a risk that applicants, who have been denied registration in one region/office, can be granted registration in another. The use of so-called “*straw men*” for registration purposes creates added difficulties for the TA due to the fact that the real person behind the business doesn’t reveal himself in the new application.

Furthermore, businesses that are already registered in the VAT register can

pose a threat to the revenue as presumptive fraudsters. Based on various risk indicators, or certain information that becomes available to the TA after the initial phases of the VAT registration process, a need can arise to carry out follow-up measures in respect of a business already in the VAT register.

In most countries there are legal restrictions on keeping and publishing blacklists. Only a few countries are allowed to keep such lists. One of the major advantages of blacklists is that they enable TAs to alert officers at an earlier stage about higher risk businesses or risky behaviour.

Most countries have methods for highlighting businesses in their computer systems that require to be more closely monitored, and to include indicators for future control actions. This method should be considered as good practice. Any TA that is not exploiting this option should seriously consider implementing it forthwith.

The legislative body in each country has to consider which tools the TA needs in order to effectively prevent and detect serious VAT fraud. What is clear is that the right to register important information related to fraudulent persons and fraudulent activities is vital if the TA is to successfully combat VAT fraud.

1.1.1. Special attention to intra-Community transactions and third country transactions

Intra-Community transactions and third country transactions pose one of the highest risks of VAT fraud among IOTA member countries. Not all countries incur losses, but even those countries that do not suffer actual VAT losses from this type of fraud can be involved and are indirectly subject to intra-Community transactions fraud by providing havens for others involved in the fraud. It is not simply a concern for those jurisdictions who suffer the VAT loss, so all TAs must thus be aware this risk.

Due to the nature of MTIC and carousel fraud, those countries suffering losses from intra-Community VAT fraud are dependent on effective administrative cooperation with other TAs to ensure the swift exchange of information and the appropriate use of multilateral or bilateral controls. Experience has shown us that in addition to existing companies being used as part of a VAT fraud, the circular nature of the fraud means that new businesses are inevitably needed to be used as tools for extending the VAT fraud. Since frauds of this type do not respect national boundaries but rather exploit them, the need for close co-operation between our TAs is essential throughout the prevention and detection processes.

Minimum approach:

The EU has recently introduced a new Regulation concerning administrative cooperation between the 27 EU member States. The EU requirements will of course serve as minimum standards to EU member States, but our view is that, while the standards are of course optional for IOTA member countries outside the EU, they should be regarded as desirable if not essential.

See EU regulation 904/2010 > <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:268:0001:01:EN:HTML>

Premium approach:

- Improve the exchange of information with other TAs, including the appropriate use of bilateral or multilateral controls
- Enhance cooperation with other government organisations, Customs, national and international law enforcement agencies, etc.
- Participate regularly in IOTA, Eurofisc, OECD forums, etc.
- Issuing handbooks and guidelines on the settlement and payment of VAT in relation to intra-Community supplies of goods and services putting special emphasis on carousel fraud
- Organise specific training on the topic for TA inspectors and auditors, controllers and VAT registration officers
- Special awareness training for TA inspectors and auditors involved in other areas of tax
- Continual identification of risk areas
- Promote legislative changes or amendments to national legislation, where this is deemed necessary to effectively tackle VAT fraud
- Increasing the skill of TA inspectors and auditors in the effective use of swift, targeted anti-VAT fraud controls and techniques
- Coordinated and project-based inspections and control actions
- Rigorous control of any business when they file initial large claims for VAT refunds

4.8.4. Informing customers and suppliers of missing traders

When a TA detects ongoing or suspected VAT fraud it is of paramount importance that relevant information is shared with other stakeholders, including those who may be inadvertently involved in the fraud.

Some TAs have the possibility to disclose such information to both customers and suppliers of a suspected VAT fraudster.

It should be considered as a premium approach to inform stakeholders

about ongoing VAT fraud. TAs should implement procedures to facilitate the issuing of such information. The channels of information should work both ways, giving businesses the opportunity to proactively request information from the TA about their business partners.

Information such as the fiscal status should be made available along with whether the business:

- has a valid VAT registration number
- is registered as an employer
- files VAT returns
- has any unpaid taxes or other debts to the TA

Some of the information above could be considered as classified or confidential, but information will only be given about the incidence - a simple 'yes' or 'no', and not the details of their tax declarations. Such simple, 'yes or no' details should be considered as reasonable information which should be made available to enquiring businesses.

Each TA should consider the fine balance between on the one hand protecting the suspected fraudsters by not disclosing information, or on the other the impact to a bona fide business risking trading with the fraudster and incurring losses due to unpaid goods and/or services.

1.1.2. Informing other Central Liaison Offices or TAs in Third Countries

As mentioned above, the European Union has issued a new Regulation aimed at improved administrative cooperation and it has a major focus on combating fraud in the field of VAT (Regulation 904/2010). The new Regulation came into force on 7th October 2010. It reflects the need for swifter exchange of information, not only between EU countries, but also with third countries, in order to prevent and detect serious cross border VAT fraud.

Third countries are encouraged to establish cooperation with EU countries and other third countries. Bilateral or multilateral agreements on exchange of information should ideally reflect the trade patterns for those countries, i.e. countries with intensive trade in particular trades or commodities should agree on exchange of information in order to prevent VAT fraud and other frauds related to their markets in these areas.

IOTA has launched a Knowledge Database under the title "Mutual Assistance and Exchange of Information in the IOTA Region in the Field of VAT Fraud".

The purpose of the IOTA Knowledge Database is to improve the administrative and operational competence of officers in relation to exchange of information and mutual assistance in VAT fraud cases. It also promotes and facilitates practical co-operation and exchange of information between TAs in the IOTA region.

The Knowledge Database can be found, after logging in to the IOTA website, at >

<http://www.iota-tax.org/publications/knowledge-databases-455.html>

4.9. Deregistering businesses from the VAT register

Deregistering businesses from the VAT register is an important measure to ensure the correctness and accuracy of the register and avoid the obvious risks of having businesses remain on the register when they should not be. The quality of data in the VAT register should be a high priority for every TA.

In 2009 an IOTA task team presented a report on common procedures for VAT deregistration, stating the following in their summary:

"The compulsory de-registration of abusive or inactive (often referred to as 'dormant') taxpayers is generally accepted as a useful tool in maintaining a healthy VAT system.

Generally the vast majority of tax administrations have the ability to compulsorily de-register VAT registrations either on the grounds of a lack of economic activity, non-compliance or outright abuse.

In demonstrating the potential involvement of others in using an abusive VAT number to commit fraud, it is essential that information on invalid VAT numbers is made as easily accessible as possible. Additionally this also supports legitimate businesses in undertaking their due diligence responsibilities."

For further information see IOTA report on VAT De-registration >
<http://www.iota-tax.org/publications/iota-report-for-tax-administrations--vat-de-registration-368.html>

Another alternative to deregistration is the temporary suspension of VAT registration or suspension of business activity as a penalty for not complying with VAT its legal obligations.

4.9.1. Minimum approach

The minimum recommendation is to deregister a business which no longer carries out an economic activity. Indications that a business is no longer active include:

- No evidence of economic activity based on the findings of an audit or investigation by the TA
- No tax returns
- Nil or blank tax returns
- Direct information from the business, or indirect information from other sources, that economic activity by the business has ceased
- Taxpayer is missing and cannot be traced

The TA must investigate whether or not an economic activity is being performed by the business. It is essential that the TA constantly keeps the VAT register updated with valid VAT registration entries. A business not performing an economic activity should be deregistered as soon as is practically possible.

4.9.2. Premium approach

The premium approach is to deregister a business which meets any of the following criteria:

- No submission of, or blank recapitulative statements
- No payments received
- Various forms of insolvency of the taxpayer
- Bankruptcy petition filed with the court (for unpaid debts) if a legal person fails to pay VAT debts
- Deletion of the legal person from National Register of Companies/Company House Register

Conclusion

There are no short cuts or quick fixes when performing effective VAT registration controls and activities that aim to prevent fraudsters from entering the VAT register. It comes down to the need for continued proactive and systematic work by the TA.

A good example was presented by the **Slovenian** tax administration, who decided to implement a comprehensive strategy to improve their VAT registration performance. Their strategy is described in the box below and serves as a very good example of how to structure an approach to the entire VAT registration process.

IOTA Report for Tax Administrations

Pre and post registration VAT controls

Slovenia: extensive approach to improve their work in the field of VAT

After Slovenia's accession to the EU certain measures were introduced in the area of tax control in the settlement of VAT in transactions within the EU. These measures are intended to guarantee greater efficiency of control over VAT tax evasions of the carousel type. The measures may be divided into:

1. Preventive measures
2. Measures concerning the detection of potential VAT carousels or "missing traders"
3. Measures concerning the reform of suspected or detected VAT carousels.

The general guidance that we followed during the determination of measures is that preventive measures are much more efficient than corrective measures.

1. Preventive measures:

a) raising the awareness of the tax control personnel about the risks involved in the settlement of VAT in case of intra-Commission and the possibilities and methods of performing such control.

- the participation of our representatives in FISCALIS seminars on VAT carousels
- the preparation of a special handbook on the performance of control over the settlement and payment of VAT in intra-Commission goods transactions laying special emphasis on carousel VAT tax evasion
- the organisation of training on the topic for inspectors, controllers and taxpayers registration staff
- the organisation of special training for all tax inspectors on the topic of international administrative help and information exchange in the field of VAT inspection control in intra-Community transactions
- the determination of risk areas of activity in which there is greater occurrence of tax evasion (cell phones, CPU, precious products, automobiles, metal waste, construction, textile products and meat) and which are the subject of rigorous inspection control.

b) Legislative changes or amendments

- the drafted and already adopted change to the VAT Act regarding the fiscal period in the case of newly registered VAT taxpayers. The compulsory fiscal period for newly registered companies in the fiscal year is currently one month
- Introduction of the system of joint and several liability
- Introduction of the reverse charge system in the field of construction and renting labour force in construction, sale of real estate and supply of waste materials – 1 January 2010
- Possibility of use of the insurance instrument at issuing of VAT identification
- Possibility of use of the insurance instrument for VAT payment at acquisition of motor vehicles from the EU
- Possibility of definition of a specific time limit for VAT payment and time limit for submission of VAT settlement on the basis of tax authority's decision, in cases of justified suspicion that VAT will not be paid.
- Obligation of submission of the list of received and issued invoices at the first VAT settlement

(All legal changes other than the first item came into force on 1 January 2010.)

c) The performance of rigorous control during the registration of VAT taxpayers

2. Measures concerning the detection of potential VAT carousels or "missing traders"

- increasing the competences of inspectors in the field such that there was an increase in the number of swift VAT inspection controls in 2008 and 2009 as compared to the previous years – verification of the reasons for discrepancies between data from the VIES system and data on the receiving of goods filed by the taxpayer;
- the execution of coordinated and project led inspection control actions in 2008 and 2009 in the field of construction and car trading.

3. Measures concerning the reform of suspected or detected VAT carousels

- The preparation and introduction of the methodology for tax control in the case of performing an audit on the evasion of VAT of the carousel type focusing on the realisation that tax inspection must, in this case, be extended to all the participants who must be considered as a whole. At the same time, the withdrawal or revocation of the taxpayer's identification number constitutes part of the procedure, in case it is found that the taxpayer does not actually perform the commercial activity.

The rigorous control of major taxpayers upon filing the first big claims for VAT reimbursement – the approval of the first big claim is possible solely on the basis of an audit whereby the aim is to prevent the unjustified VAT reimbursement to the so-called brokers.

5. APPENDICES

- 5.1. Appendix 1 - Pre and post registration VAT Controls - Questionnaire 2010
- 5.2. Appendix 2 - Sweden - Risk assessment and high risk sectors
- 5.3. Appendix 3 - VAT Thresholds in the IOTA region
- 5.4. Appendix 4 - UK - VAT Risk Assessment Questionnaire
- 5.5. Appendix 5 - Sweden - VAT Risk Assessment Questionnaire