



**SCHOOL OF
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**The Potential Impact of Digital Reporting Requirement (in
ViDA) on VAT Carousel Fraud: A preventive tool or a dream
in colour?**

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List of Abbreviations

B2B	Business-to-business
B2C	Business-to-consumer
B2G	Business-to-government
CESOP	Central Electronic System of Payment
CFREU	Charter on the Fundamental Rights of the European Union
CJEU	Court of Justice of the European Union
Commission	European Commission
Court	Court of Justice of the European Union
CTCs	Continuous Transaction Controls
DRR	Digital Reporting Requirement
EU	The European Union
GDPR	General Data Protection Regulation
IBAN	International Bank Account Number
ICA	Intra-Community Acquisition
ICS	Intra-Community Supply
MTIC	Missing Trader Intra-Community
OECD	Organisation for Economic Co-operation and Development
PTCs	Periodic Transaction Controls
TNA	Transaction Network Analysis
VAT	Value Added Tax
VAT Directive	Council Directive 2006/112/EC on the common system of VAT
VAT ID	Value Added Tax Identification Number
VIES	VAT Information Exchange System
ViDA	Value-Added Tax in the Digital Age

1 Introduction

1.1 Background

Value Added Tax ('VAT') is a valuable resource that accounts for 12% of the budget of the European Union ('EU') and a sizeable portion of the budgets of the Member States.¹ The VAT Gap² was estimated at EUR 93 billion in 2020, and a major part of this loss is caused by missing trader intra-community ('MTIC') fraud and/or carousel fraud.³ The data reveals the EU's suffering from MTIC and carousel fraud, as well as the urgency of the situation and the need for collective effort.

Since the VAT system has not undergone a drastic change since the establishment of the EU in 1993⁴, although VAT frauds manifested themselves by changing their form over time, the EU has been trying to develop different methods to tackle this problem.⁵ Taking account that digitalization is gaining momentum, a fundamental change must be made in the VAT system to combat tax fraud and enhance administrative cooperation between the Member States.⁶ In the face of the problem, in 2020 the Commission announced its Action Plan with the aim of the more fair, comprehensible and harmonized legislative package which will include renewed tax rules that can adapt to the digital era.⁷

After this step, the Commission announced a package of proposals on December 8, 2022, which aims to "modernise and make the EU's Value-Added Tax ('VAT') system work better for businesses".

The main source of this research is the development of the Digital Reporting Requirement ('DRR') that comes within this package, which has allowed Member States to implement it until 2028.⁸

1.2 Purpose of the paper

Tax fraud has been an ongoing problem since the establishment of the European Union; therefore, the matter is comprehensive and complex to tackle in limited pages. This study's boundaries are delimited by the role of the current reporting requirements and the

¹ Proposal for a Council Directive amending Directive 2006/112/EC as regards VAT rules for the digital age, COM (2022) 701 final, 8.12.2022.

² Defined by the European Commission as "The VAT GAP is an estimate of the overall difference between the expected VAT revenue and the amount actually collected.", *VAT gap in the EU*, available at https://taxation-customs.ec.europa.eu/taxation-1/value-added-tax-vat/vat-gap_en (accessed 23 Feb. 2023).

³ Ibid, and Proposal for a Council Directive amending Directive 2006/112/EC, (n.1), p.1.

⁴ Jernej Podlipnik, *Missing Trader Intra-Community and Carousel Vat Frauds – ECJ and ECtHR Case Law*, Croatian Yearbook of European Law and Policy, Vol. 8, 457–472, (2012) p.458, available at <https://www.cyelp.com/index.php/cyelp/article/view/135>. (accessed 23 Feb. 2022).

⁵ European Parliament, Study of *Possible Solutions for Missing Trader Intra-Community Fraud*, June 2022, [https://www.europarl.europa.eu/RegData/etudes/STUD/2022/731902/IPOL_STU\(2022\)731902_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/STUD/2022/731902/IPOL_STU(2022)731902_EN.pdf) (accessed 28 Feb. 2023).

⁶ Proposal for a Council Directive amending Directive 2006/112/EC, (n.1), p.1-2.

⁷ European Commission, Communication from the Commission to the European Parliament and The Council, *An action plan for fair and simple taxation supporting the recovery strategy*, COM (2020) 321 final, 15.07.2020, available at <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2020:0312:FIN> (accessed 23 Feb. 2022).

⁸ Proposal for a Council Directive amending Directive 2006/112/EC, (n.1), p.22.

aim of DRR in the VAT rules for the Digital Age ('ViDA'), the European Commission's amending Directive 2006/112/EC Proposal on 8 December 2022, in preventing VAT carousel fraud in practice.

The purpose of the analysis is threefold. Firstly, after a brief explanation of the current digital reporting systems in the EU, the author indicates the aims of the digital reporting requirement regulated under VAT in the Digital Age (section 2). Secondly, the author explains the pattern of VAT carousel fraud, the CJEU's landmark cases and the Court's stance regarding the matter (section 3). Finally, the author evaluates amendments in the Proposal and the potential impact of the DRR obligations as a preventive tool for VAT carousel fraud in the EU (section 4). The legal issue to be addressed in this paper is to analyse the impact of DRR in preventing VAT carousel fraud and potential problems regarding the implementation of these new obligations.

2 VAT Digital Reporting Systems in the European Union

2.1 Current situation

The VAT Directive dates back to the 1970s and the 'transitional' VAT system that has adopted⁹ along with the 'single area without internal tax borders' in the EU was intended to last until the creation of the single market in 1993, however, it is still in force today.¹⁰ The system was designed to split a cross-border taxable event into two: the supplier's zero-rated, with the right to deduct, intra-Community supply of goods from the Member State of departure, and the acquirer's intra-Community acquisition of goods in a different Member State.¹¹ The declaration responsibility belongs to the purchaser in the country of destination in its periodic VAT returns, in the form of recapitulative statements which are stored in Member State's databases.¹² Recapitulative statements (*regulated under Article 262(2) VAT Directive*) are supported by the VAT Information Exchange Systems ('VIES'), which facilitates the exchange of information related to intra-Community transactions and helps tax authorities to match¹³ intra-Community supplies and acquisitions and to guarantee that VAT is properly declared in the Member State of destination.¹⁴ Additionally, a generalized reverse charge mechanism has been adopted in

⁹ Adopted by Council Directive 91/680/EEC of 16 December 1991 supplementing the common system of value added tax and amending Directive 77/388/EEC with a view to the abolition of fiscal frontiers OJ L376 (1991), available at <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A31991L0680> (accessed 01 Mar. 2023).

¹⁰ Proposal for a Council Directive amending Directive 2006/112/EC, p.2 (n.1), and Sascha Jafari, Marie Lamensch, Marta Papis-Almansa, *Proposal for a Secure Digital Reporting Standard for Intra-Community Transactions*, 33 Intl. VAT Monitor 6, (2022), p.232, Journal Articles & Opinion Pieces IBFD (Accessed 28 Feb. 2023).

¹¹ Case C-409/04, *Teleos PLC and Others v Commissioners of Customs & Excise* [2006] paras. 22-25, and Case C-641/21 *Climate Corporation Emissions Trading GmbH v Finanzamt Österreich* [2022] paras. 45-47.

¹² C-430/09, *Euro Tyre Holding BV v Staatssecretaris van Financiën* [2010] para.7.

¹³ TNA (*Transaction Network Analysis*) is designed as an online tool to compile and contrast VAT transactions to aid in the early identification of VAT fraud. Along with other Benelux countries, Belgium piloted this tool in 2014, then it was made available to 10 additional Member States. It is now used voluntarily as of May 2019, by several Member States along with their activities of EUROFISC, derived from European Parliament Study of *Possible Solutions for Missing Trader Intra-Community Fraud*, (n.5).

¹⁴ Proposal for a Council Directive amending Directive 2006/112/EC (n.1), p.4-5.

2018¹⁵ and extended until the end of 2026 for supplies of goods and services above a certain amount.¹⁶

The VAT Directive has given Member States the discretion to adopt national reporting requirements, however, a harmonized level has not yet been formed and different digital reporting requirements have been introduced by several Member States.¹⁷ These techniques are briefly discussed in this section.

There are two distinctive systems regarding the DRR: periodic transaction controls ('PTCs') and continuous transaction controls ('CTCs').¹⁸

In PTCs, the data regarding the taxable transaction is reported to the tax authorities at regular intervals, sample applications of this method are the VAT Listing and SAF-T systems. The first one requires transmission of the transactional data to the tax authorities under the national regulation; however, the latter is based on an OECD standard, i.e. the Standard Audit File for Tax.¹⁹

In CTCs, the transactional data are transmitted electronically to tax authorities *just before, or shortly after the actual exchange of such data between the parties*.²⁰ CTCs comprise real-time reporting and mandatory e-invoicing systems, which are accepted in very few of the Member States.

However, the VAT Directive which allows Member States to establish their reporting requirements also contains some obstacles. A derogation from the VAT Directive under Article 395 must be requested by a Member State to enact mandatory e-invoicing requirements; this request must receive the EU Council's unanimous approval and be approved with a proposal from the Commission.²¹ Thus, it is necessary to refer to the applicable reporting systems of Spain and Hungary for real-time reporting and Italy for the mandatory e-invoice.

The Spanish tax administration developed a national 'nearly' real-time reporting system, Spanish Immediate Information System ('SII') in 2017 as a pioneer in Europe. The tax authorities must receive electronically submitted information from certain businesses

¹⁵ Council Directive (EU) 2018/2057 of 20 December 2018 amending Directive 2006/112/EC on the common system of value added tax as regards the temporary application of a generalized reverse charge mechanism in relation to supplies of goods and services above a certain threshold, OJ L329 [2018] (accessed 23 Feb. 2023).

¹⁶ European Commission, *Optional reverse charge mechanism to stay in place until 2027*, https://taxation-customs.ec.europa.eu/news/optional-reverse-charge-mechanism-stay-place-until-2027-2022-06-13_en (accessed 23 Feb. 2023).

¹⁷ Proposal for a Council Directive amending Directive 2006/112/EC, (n.1), p.3.

¹⁸ European Commission, *VAT in the Digital Age Final Report Executive Summary* (2022), p.8, available at https://taxation-customs.ec.europa.eu/system/files/2022-12/VAT%20in%20the%20Digital%20Age_Final%20Report%20Executive%20Summary%20EN.pdf (accessed 28 Feb. 2023).

¹⁹ European Commission, *VAT in the Digital Age Final Report, Volume 1 Digital Reporting Requirements* (2022), p.15 available at https://taxation-customs.ec.europa.eu/system/files/2022-12/VAT%20in%20the%20Digital%20Age_Final%20Report%20Volume%201.pdf (accessed 28 Feb. 2023).

²⁰ Ibid, p.15.

²¹ Proposal for a Council Directive amending Directive 2006/112/EC (n.1), p.3 supra n.15.

within four calendar days; this requirement is extended to eight days for entities whose invoices are issued by authorized third parties.²² The system mandates that large businesses (those with revenues of EUR 6 million or more), VAT groups and businesses who chose to register in the monthly VAT return system to report information of the transaction to the tax administration.²³ Following Spain, Hungary launched ‘KOBAK’ in 2018 and in 2021, the real-time reporting obligation was extended to all domestic B2C and B2B intra-Community transactions.²⁴ According to the system, suppliers must submit XML-formatted invoices to the Hungarian tax authorities at the time of issuance.²⁵

Italy, as one of the countries with the highest VAT Gap (20.8% in 2020²⁶), has adopted a mandatory e-invoicing system in 2019 with the Sistema di Interscambio (‘SdI’) between B2B and B2C transactions.²⁷ All companies must inform and submit their standardised e-invoices (‘FatturaPA’) to the tax authority in real-time before it is sent to the buyer, which helps tax authorities check and approve the transaction before the invoice is received by the acquirer.²⁸

2.2 Problem definition and what is to be achieved by the Digital Reporting Requirement

The current recapitulative statements date back to 1993 and are unsuitable for the digitalized economy and the system is incapable to provide transaction-based declaration; therefore, VAT fraud is inevitable due to the lack of controllability of reciprocal transactions.²⁹

Moreover, as mentioned above, several Member States have developed different digital reporting systems, within the boundaries given to them by the Directive, which causes ‘fragmentation’³⁰ and becomes burdensome for taxpayers who are registered in more than one Member State.³¹ This situation results in an obstacle to the single market and a barrier to free trade, which is one of the core aims of the EU.

Finally, the determination of different methods by several Member States does not help the Union’s solidarity and cooperation to be formed in the EU’s fight against VAT fraud, however, the DRR aims to strengthen administrative cooperation and trust between the Member States instead of various protection mechanisms.³²

²² M. Lamensch et al., (n.10), p.235, and Madeleine Merckx and Naomie Verbaan, *Technology: A Key to Solve VAT Fraud*, 28 EC Tax Review, Issue 6, (2019), p.304 (accessed 28 Feb. 2023).

²³ M. Lamensch et al., (n.10), p.236.

²⁴ European Parliament Study of *Possible Solutions for Missing Trader Intra-Community Fraud*, (n.5), p.47.

²⁵ Ibid.

²⁶ European Commission, *VAT Gap in the EU*, (n.2).

²⁷ European Parliament Study of *Possible Solutions for Missing Trader Intra-Community Fraud*, (n.5), p.48.

²⁸ Ibid, and M. Lamensch et al., (n.10), p.236.

²⁹ Proposal for a Council Directive amending Directive 2006/112/EC (n.1), p.4 supra n.15.

³⁰ European Commission, *Staff Working Document Impact Assessment Report (2022)*, p.27, available at <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52022SC0393> (accessed 03 Mar. 2023).

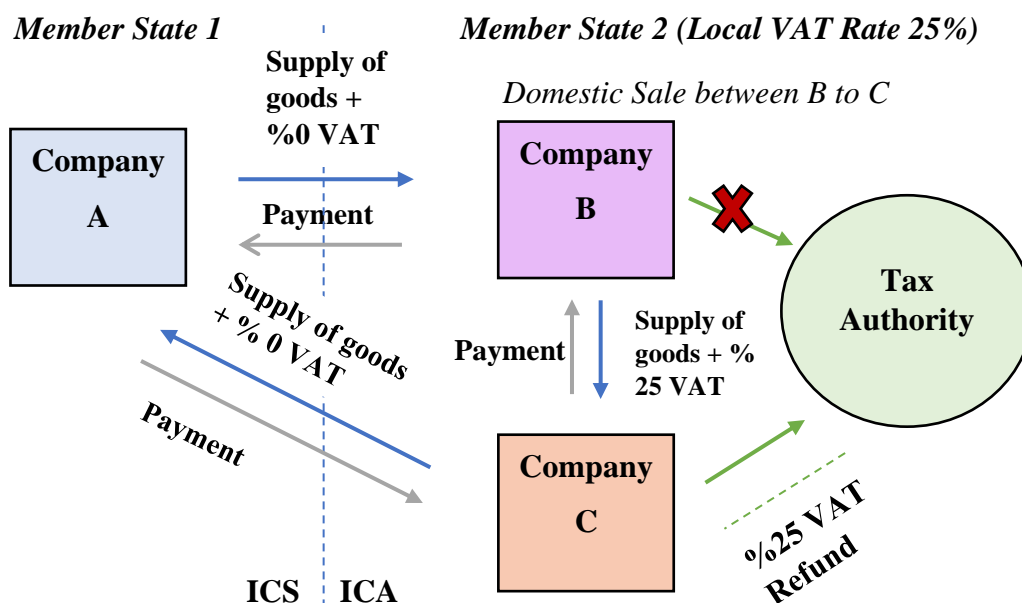
³¹ Ibid, and M. Lamensch et al., (n.10), p.231.

³² European Commission, *VAT in the Digital Age Final Report Executive Summary (2022)*, (n.18), p.10.

3 Scope of VAT Carousel fraud

MTIC is “the biggest kind of VAT fraud”³³, and at least one ‘missing trader’ is required for a carousel fraud to occur, however, not every fraud committed by a missing trader is a carousel fraud. Carousel fraud occurs when several businesses shaped a circular by selling and purchasing the same goods and services. In other words, the common ground in both MTIC and carousel fraud is at least one of the businesses involved in the scheme is a missing trader who is taking advantage of zero-rate VAT.³⁴ The business either exists on paper or uses counterfeit VAT ID numbers and disappears with money before the tax authorities realize the scheme.³⁵ The most discussed reasons for the fraud are the vulnerability of the VAT system³⁶, the presence of ‘flaws’ in the laws that create room for fraud³⁷, and the need for more than one dynamic to be together to prevent VAT fraud schemes.

3.1 Definition of the scheme



³³ European Parliament, *Missing Trader Intra-Community Fraud* (2021), available at [https://www.europarl.europa.eu/RegData/etudes/BRIE/2021/690462/IPOL_BRI\(2021\)690462_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/BRIE/2021/690462/IPOL_BRI(2021)690462_EN.pdf) (accessed 28 Feb. 2023).

³⁴ VAT Directive, Article 138(1), and Eleonor Kristoffersson and Pernilla Rendahl, “6.6. Intra-Union Acquisition of Goods,” *Textbook on EU VAT* (Iustus 2021).

³⁵ Podlipnik, J., (n.4), p.463,

³⁶ Rita De la Feria, *Tax Fraud and The Rule of Law*, Oxford University Centre for Business Taxation Working Paper 18/02, (2018), p.2, available at <https://www.sbs.ox.ac.uk/sites/default/files/2018-08/WP1802.pdf> (accessed 23 Feb. 2023).

³⁷ Podlipnik, J., (n.4), p.458.

The basic scheme can be described as follows.³⁸ Each participant in the scheme has registered as a taxable person. When goods are supplied as an intra-Community supply ('ICS'), the supply is exempt with a right to deduct. The following B2B intra-Community acquisitions ('ICA') are regarded as taxable transactions (VAT Directive Article 2/1(b)); however, "an intra-Community supply of goods is exempted in the Member State where dispatch of those goods began, without prejudice to the right to deduction or refund of input VAT paid in that Member State, whereas the intra-Community acquisition is subject to VAT in the Member State of arrival".³⁹ In Member State 1, Company A supplies goods to Company B in Member State 2, let us assume 100 cell phones. Company A makes a zero-rated intra-Community supply of goods and Company B makes an intra-Community acquisition of goods.⁴⁰ According to Article 138 (1a) of the VAT Directive, the acquirer must comply with its duty to fill recapitulative statement⁴¹ to be able to apply for the zero-rate exemption. Then, Company B makes a domestic supply to a third company called C, who can be a part of the scheme or might be an 'innocent' trader, and Company B applies the local VAT rate (25%) on the supply to Company C, however, B does not remit this VAT to the tax authorities, but C, who in turn sells the cell phones to A with 0% VAT claims his input VAT refund invoiced to him by B. When the purchaser, C, claims his/her input VAT paid to the missing trader B, the Member State suffers a loss.

The scheme may involve multiple companies and Member States to include more than one jurisdiction and to make the organization more complex and difficult to track.⁴² Initially, the fraud mainly involved expensive items that are movable across borders such as electronic items; however, the VAT fraud has evolved to include tradable services like intellectual property rights and carbon dioxide emission certificates, which are traded in industries with a high innovation potential.⁴³

3.2 The CJEU's landmark case law

It is highly troublesome for any tax authorities to catch the missing trader and accuse them of unreported VAT since they just vanish or declare bankruptcy with no assets belonging to them. Thus, Member States are trying to hold the 'buffers', legitimate and *bona fide* traders that were part of the carousel transactions, accountable for the loss of VAT.⁴⁴

³⁸ Joep Swinkels, *Carousel fraud in the European Union*, International VAT Monitor, (2008), pp.103-113, p.104, IBFD and Robert F. van Brederode & Sebastian Pfeiffer, *Combating Carousel fraud: The General Reverse Charge VAT*, 26 Intl. VAT Monitor 3 (2015), p.147, Journal Articles & Opinion Pieces IBFD (accessed 23 Feb. 2023) and Podlipnik, J., (n.4), p.463.

³⁹ Case C-641/21 *Climate Corporation Emissions Trading GmbH v Finanzamt Österreich* [2022] para. 46.

⁴⁰ VAT Directive Article 2(1) in conjunction with Art. 20 and Art. 40

⁴¹ VAT Directive, based on Article 262.

⁴² European Parliament, *Missing Trader Intra-Community Fraud*, (n.5) and Podlipnik J., (n.4), p.46, and Madeleine Merckx, Rianne Starckenburg, Naomie Verbaan, *VAT and International Trade's Crossroads: Right, Left or Straight On?* 28 EC Tax Review Is. 5, pp. 233-244, (2019), p. 236 (Accessed 23 Feb. 2023).

⁴³ F Fabrizio Borselli, *VAT Fraud, Cryptocurrencies and a Future for the VAT System*, 30 Intl. VAT Monitor 5 (2019), p.180, Journal Articles & Opinion Pieces IBFD (accessed 26 Feb. 2023).

⁴⁴ R.F.W. van Brederode & S. Pfeiffer, (n.38), p.147.

By the time the tax authorities learn about the fraudulent scheme, trader B will be missing, and the authorities will be more motivated to seek ‘compensation’ from other parties.⁴⁵ Two different strategies could be applied in this regard. First, disallow C from deducting his input VAT that B charged him⁴⁶ and second, hold all parties jointly and severally liable for participating in a fraudulent act together.⁴⁷

In *Optigen, Fulcrum, Bond House Systems Case*⁴⁸, three *bona fide* UK-based companies purchased computer chips from another UK-based company (B2B) and sold them to other receiver businesses established in another Member State.⁴⁹ When they sought to have their input VAT deductions, the UK tax authorities denied or reclaimed the paid refund and claimed that those companies have participated in carousel fraud.⁵⁰ On 12 January 2006, the CJEU held that “each transaction must be regarded on its own merits and the character of a particular transaction in the chain cannot be altered by earlier or subsequent events.”⁵¹ A fortiori, the CJEU rejected to limit one’s right to deduct input VAT since it is irrelevant.⁵² However, it would be contrary to the EU’s general principles to protect a fraudulent act, so, if a taxable person knew or should have known that his/her transactions were part of fraudulent activities, his rights arising from the EU law will no longer be protected.⁵³

In the following joined cases *Kittel and Recolta Recycling*⁵⁴, the Court has invented its well-known ‘Knowledge Test’. Computime, a Belgian company, was trading computer components from Belgium to Luxembourg and Axel Kittel was Computime’s receiver, the Belgium tax authorities suspended the Company’s transactions and rejected its right to deduct VAT paid on those supplies. At the same time, Recolta Recycling had bought 16 luxury vehicles from Mr Ailliaud, *which the latter had purchased from Auto Mail*.⁵⁵ The Belgium tax authorities claimed that Mr Ailliaud and Auto Mail has created a carousel scheme and denied Recolta’s right to deduct VAT, although Recolta was unaware of the fraudulent scheme it was involved in. In this case, the referring court has asked whether is it possible to apply the doctrine of *Optigen and others* where the supplier defrauds a taxable person who was a *bona fide* recipient and neither knew nor could have known about the deception.⁵⁶ The Court decided that “traders who take every precaution which could reasonably be required of them to ensure that their transactions are not connected with fraud, be it the fraudulent evasion of VAT or other fraud, must be able to

⁴⁵ Swinkels J., (n.38), p.104.

⁴⁶ Ibid.

⁴⁷ Podlipnik, J., (n.4), p.467.

⁴⁸ Joined Cases C-354/03, *Optigen Ltd* and C-355/03 *Fulcrum Electronics Ltd (in liquidation)* and C-484/03, *Bond House Systems Ltd* [2006] ECR I-483. ECJ Case Law IBFD.

⁴⁹ Ibid, para.8.

⁵⁰ Ibid, para 9–12.

⁵¹ Ibid, para 47.

⁵² Ibid, para 53-54.

⁵³ Joined Cases C-354/03, *Optigen Ltd* and C-355/03 *Fulcrum Electronics Ltd (in liquidation)* and C-484/03, *Bond House Systems Ltd* [2006] ECR I-483, paras. 51–52.

⁵⁴ Joined Cases C-439/04 and C-440/04 *Axel Kittel v État belge and État belge v Recolta Recycling SPRL* [2006] ECR I-06161.

⁵⁵ Ibid, para 14.

⁵⁶ Ibid, paras.27–28.

rely on the legality of those transactions without the risk of losing their right to deduct the input VAT.”⁵⁷

However, in the circumstances of “a taxable person who knew or should have known that, by his purchase, he was taking part in a transaction connected with fraudulent evasion of VAT must, ... be regarded as a participant in that fraud, irrespective of whether or not he profited by the resale of the goods.”⁵⁸

This leads to the conclusion that the rights of a taxable person, who knows and should have known the fraudulent activity will not be protected by the common system of VAT or the EU law since it is obvious that the person willingly participated in the fraudulent act.⁵⁹

Lastly, in the CJEU’s judgment in *Federation of Technological Industries*⁶⁰, the Court expressed its views on holding each party involved in carousel fraud jointly and severally liable. The Court indicated that national authorities are free to determine third-party liability, the only limit is to regulate national norms following the EU law and its principles of proportionality and legal certainty.⁶¹ Therefore, a taxable person can be made liable for paying stolen VAT if they knew about or had ‘reasonable grounds’ to suspect that they were involved in an MTIC or carousel fraud.⁶²

At this point, it may be a matter of discussion of what ‘reasonable ground’ might be, Joep Swinkels defines the circumstances as “if the price payable by him was less than the lowest price that might reasonably be expected to be payable for those goods on the market, or less than the price payable on any previous supply of those goods.”⁶³

4 Impact of the Digital Reporting Requirement on carousel fraud

4.1 What is new with the Proposal?

As has been explained above, the reasons for the increase in VAT Gap and MTIC fraud are the fact that the current system (recapitulative statement) is outdated, and one of the deficits of the VAT system is that missing traders generally disappeared until the tax authorities learn about the carousel scheme, and real-time recording of intra-Community transactions are not possible at EU level.⁶⁴

The ViDA proposal is anticipated to generate net benefits between EUR 172 billion and EUR 214 billion within 9 years (2023-2032), including EUR 51 billion in savings, and particularly EUR 41.4 billion from VAT reporting.⁶⁵ In this chapter, the modifications on

⁵⁷ Ibid, para 51.

⁵⁸ Ibid, para 56.

⁵⁹ Ibid, para 57.

⁶⁰ Case C-384/04 *Federation of Technological Industries v Commissioners of Customs and Excise*, Attorney General, [2006] ECR I-4191.

⁶¹ Ibid, para 29 and 35.

⁶² Podlipnik J., (n.4), p.469-470.

⁶³ Swinkels J., (n.38), p.106.

⁶⁴ European Commission, *Staff Working Document Impact Assessment Report*, (n.30), p.28-29, and Proposal for a Council Directive amending Directive 2006/112/EC (n.1) p.4.

⁶⁵ Proposal for a Council Directive amending Directive 2006/112/EC (n.1) p.14-15.

the VAT Directive 2006/112/EC will be briefly explained and their possible impact on carousel fraud will be discussed.

The implementation of mandatory e-invoicing requirements begins in 2028 with amended Article 218. Formerly Article 232 regulated the necessity of the recipient's consent in the acceptance of issuing an e-invoice is now deleted.⁶⁶ Accordingly, Article 218 regulates the obligation of issuing standardised EU invoice, EN16931⁶⁷, which is currently known for mandatory B2G e-invoicing.⁶⁸ A significant alteration is that suppliers wanting to issue e-invoices would no longer depend on the recipient's consent. The content of the e-invoice has been expanded with Article 226 as (i) IBAN of the supplier, (ii) the due date(s) for payment of the invoice, and (iii) in the case of a corrective invoice, the sequential number of the corrected invoice; also, Article 222 necessitates the issuance invoices on a transactional basis and sets up two days of deadline after the chargeable event takes place.⁶⁹

However, the supreme revolution is the changes in the articles between Article 262 and Article 271 under Chapter 6 of Title XI, which previously regulated recapitulative statements, stipulating the digital reporting requirement of intra-Community transactions on a transaction-by-transaction basis.⁷⁰ From 2028, all businesses, including non-residents but except for *call-off stocks* under Article 17a, will be subject to report the intra-Community supply (ICS) in digital format (Article 262). The functioning and the features of the new DRR are defined under Articles 263 and Article 264; the data will be first submitted to the national tax authorities and the transmission of the data might be transferred with a national e-invoice format (*with the requirement of adhering to EU standard*) by the taxable person or by a third party no later than 2 working days after issuing the invoice, in former Article 263 the declaration period was "each calendar month within a period not exceeding one month".⁷¹ Likewise, Article 268 obliges Member States to require data from taxable persons who, in their territory, make the intra-Community acquisition of goods in terms of Article 21 or 22, which was discretionary for Member States under the recapitulative statements.⁷² Lastly, due to the abolishment of recapitulative statements, formerly regulated aspects of the recapitulative statements are also deleted.

Finally, under the new Section 2 of Chapter 6 of Title XI, the new rules aim to harmonize the existing and future reporting systems and prevent fragmentation and administrative burdens within the Member States.⁷³ Article 271a envisages Member States to adopt reporting systems for their domestic B2B supplies and the form of reporting is similar to

⁶⁶ Ibid, (n.1), p.18.

⁶⁷ Commission Implementing Decision (EU) 2017/1870 of 16 October 2017 on the publication of the reference of the European Standard on electronic invoicing and the list of syntaxes pursuant to Directive 2014/55/EU of the European Parliament and of the Council OJ L 266 [2017].

⁶⁸ Proposal for a Council Directive amending Directive 2006/112/EC, (n.1) p.18 and p.37.

⁶⁹ Ibid, p.18,19, and p.50.

⁷⁰ Ibid, p.19.

⁷¹ Ibid, p.20 and p.51.

⁷² Ibid, p.20 and p.52.

⁷³ Ibid, p.21.

Article 263. In order to see the operability and results of the system, it is stipulated in Article 271c that the EU Commission will submit a report showing the outcomes in March 2033 and evaluate its future harmonization plans.⁷⁴

Last but not least, amendments to Regulation No. 904/2010 on administrative cooperation have been made in ViDA package⁷⁵. According to Article 24g of Regulation No. 904/2010, the Commission will maintain and manage a new central database called “Central VIES” that will store DRR transactions’ data such as taxpayer identification data, including VAT ID numbers for 5 years.⁷⁶ The current VIES, which enables the exchange of information on transborder purchases and VAT registration numbers between Member states, would be replaced by this system.⁷⁷ Thanks to this novelty, the system would be able to store data and cross-check information received on intra-Community supplies and acquisitions and detect MTIC and carousel fraud, and the integration into the Central Electronic System of Payment (‘CESOP’) is possible under Article 24k.⁷⁸

4.2 What role does it play in carousel fraud?

It is undeniable that any systematic change made to VAT reporting obligations or a move to enhance administrative cooperation, and the effort of the system to keep up with the digitalizing world, are improving steps against VAT fraud.

As explained above, with the new DRR obligations proposed within the package of the ViDA, the trader who performs a zero-rated (Article 138(1) VAT Directive) ICS transaction and the potential ‘missing trader’ who makes an ICA transaction in another Member State, shall report their transactions to the tax authorities in almost real-time. Thus, the new rules aim to help tax authorities and the Member States quickly identify a potential carousel scheme and create a level-playing field and fair competition between trading partners.⁷⁹

The preventing effect of the ‘knowledge test’, which is established by the CJEU, is debatable. The knowledge test seems to be a helpful method used by the CJEU to ‘identify’ the parties of carousel fraud, however, at the end of the day, it is up to the national court to decide on the refusal of a taxpayer’s rights stemming from the VAT Directive. This decision must be made in the light of objective factors and the evaluation of the circumstances of whether the taxpayer should or should have known that the

⁷⁴ Ibid, p.21 and p.53.

⁷⁵ Proposal for a Council Regulation amending Regulation (EU) No 904/2010 as regards the administrative cooperation arrangements needed for the digital age COM (2022) 703 final.

⁷⁶ Ibid, Article 24h (6).

⁷⁷ Proposal for a Council Directive amending Directive 2006/112/EC, (n.1), Preamble (4), p.28.

⁷⁸ European Commission, *Central Electronic System of Payment information (CESOP)*, available at https://taxation-customs.ec.europa.eu/taxation-1/central-electronic-system-payment-information-cesop_en (accessed 03 Mar. 2023).

⁷⁹ European Commission, *VAT in the Digital Age Final Report Executive Summary*, (n.18), p.10 and Marta Papis-Almansa, *VAT in the Digital Age, Real-time digital reporting based on e-invoicing for businesses, Highlights & Insights on European Taxation*, Wolters Kluwer Nederland BV, Issue 3 (2023), pp.1-6, p.5, (accessed 27 Feb. 2023).

company/he/she had been involved in a carousel scheme.⁸⁰ It is an undeniable fact that in some cases it may be obvious that the ‘absolute and ultimate’ purpose of the cross-border transaction is to realize VAT fraud and take advantage of the ICS exemption provided by the VAT Directive.⁸¹ On the other side of the coin, there are also bona fide traders and third parties who do not know and cannot possibly know that the business they are involved in, is part of a fraudulent scheme. In this case, it would be naïve to believe that the knowledge test’s effect is fair enough to prevent the MTIC or carousel fraud. However, again thanks to the ‘knowledge test’, the CJEU allows national courts to refuse a benefit derived from a right laid down by the VAT Directive in the event of fraud.⁸²

The main reason for VAT’s vulnerability to fraud is the abuse of the cross-border ICS exemption, which was initially determined as a ‘transitional process’ but has continued to this day, yet the Court emphasized protecting the rights of bona fide traders and taking certain additional measures by the Member States.⁸³ Although there is no such rule in the proposal regarding the annulment of the cross-border ICS exemption, it would be a logical suggestion to annihilate the exemption as a mechanism to solve the MTIC and carousel fraud.

Considering statistical results analysed from Member States such as Italy⁸⁴, which implements mandatory clearance e-invoicing and Spain⁸⁵, which adopts (nearly) real-time reporting, DRR will be helpful to tackle carousel fraud and decrease the VAT Gap.

Even though the ViDA proposal is still newly introduced, and nothing has been accepted; there are criticisms regarding the security of the collected data and the potential breach of the privacy of private life.⁸⁶ Moreover, the discretion given to Member States to impose a DRR on taxable persons even in domestic transactions might cause administrative

⁸⁰ Joined Cases C-131/13, C-163/13 and C-164/13 *Staatssecretaris van Financiën v. Schoenimport “Italmoda” Mariano Previti vof and Turbu.com BV, Turbu. com Mobile Phone’s BV v. Staatssecretaris van Financiën* [2014] ECLI:EU:C: 2014:2455 para.69.

⁸¹ For example, C-277/14 *PPUH Stehcemp* and C-131/13 *Italmoda*.

⁸² C-131/13 *Italmoda* Para 62: “...it is for the national authorities and courts to refuse a taxable person, in the context of an intra-Community supply, the benefit of the rights to deduction of, exemption from or refund of VAT, even in the absence of provisions of national law providing for such refusal, if it is established, in the light of objective factors, that that taxable person knew, or should have known, that, by the transaction relied on as a basis for the right concerned, it was participating in VAT evasion committed in the context of a chain of supplies.” Also see that effect on C-285/11 *Bonik* para. 37, C-32/03 *Fini H* para. 34, C-439/04 and C-440/04 *Kittel and Recolta Recycling* para. 55; and C-80/11 and C-142/11 *Mahagében and Dávid*, para. 42.

⁸³ De la Feria R., (n.36), p.27–28.

⁸⁴ Aleksandra Bal ‘*European VAT E-invoicing Debate-Will Everyone Follow the Italian Example?*’: “In the first year of the SdI operation, the Italian VAT revenue from domestic transactions increased by 3,623 million euros (\$4.311 million) (which equals to 3%) compared to 2018.” available at <https://news.bloombergtax.com/daily-tax-report-international/european-vat-e-invoicing-debate-will-everyone-follow-the-italian-example> (accessed 16 Mar. 2023).

⁸⁵ ‘*Electronic VAT Reporting in Europe: Implementation and Evolution*’: “In just one year (2017-2018), VAT collection from large enterprises grew by EUR 3.4 billion.” available at <https://blog.groupseres.com/en/electronic-vat-reporting-in-europe-implementation-and-evolution> (accessed 16 Mar. 2023).

⁸⁶ Papis-Almansa M., (n. 79) p. 5-6 and M. Lamensch et al., (n.10) p.240).

costs⁸⁷ (infrastructure of the system) since several Member States still use various reporting systems or have not adopted a reporting requirement due to the low VAT Gap in their country or the insufficient resources of the country. The issue has become controversial regarding the efficiency and the proportionality of the DRR on domestic transactions in combating MTIC fraud.⁸⁸ Once and for all, it must be admitted that although the EU has been trying to develop effective methods to detect MTIC, as CJEU stated, what will happen to fraudsters at the end of the day, and how they will be penalized is still in the discretion of the Member States.⁸⁹

In the author's view, while the EU VAT system is expected to be relatively more harmonized, the failure to adopt solidarity in reporting systems until the ViDA proposal reveals the urgency of the problem. However, given the deadline of the proposal, it does not seem very realistic to the author that the Member States that still use VAT-Listing or have not adopted any reporting system to reach this 'ideal' harmonization level within the next 5 years. Expenses and responsibilities should not be shaped only on the installation of the new system. From the author's perspective, Member States should also be responsible for 'educating' and informing all taxpayers who will use and enter data into the system. For example, let us consider a business that cannot keep up pace with the technology, and performs a job near a borderline with another Member State, which may lead to dealing with cross-border transactions, therefore the company must comply with national and EU-level reporting requirements. While considering the costs of the adaptation of this new system (DRR)⁹⁰, not only the installation and infrastructure costs but also the costs of development of the taxpayers and resources should be considered. Since the proposed time frame is short, the achievability of these drastic changes is open to discussion.

It is apparent that with DRR, the detection of carousel fraud will be much easier and more effective and tax authorities will take faster actions. However, there could be some other collective steps that should be taken within these 5 years. Although national courts are responsible for evaluating the taxpayer's 'good faith' and 'knowledge' in a carousel scheme, the author believes that this task might be reinforced with deterrent and punitive sanctions given by all national courts in the Member States as a collective action.

Additionally, until 2028, as Spain does, the DRR system might be adapted gradually by determining some intervals in line with the annual revenues of the MNCs. By doing that, the effects of the new reporting requirement system can be monitored by the authorities and the companies that will apply the system in the next stage will have the opportunity to observe how the system functions and save time in preparing their infrastructure systems.

⁸⁷ Proposal for a Council Directive amending Directive 2006/112/EC as regards VAT rules for the digital age, COM (2022)701 final, p.4 sp.20, (n.15).

⁸⁸ Papis-Almansa M., (n.79) p. 6.

⁸⁹ Ibid, p.5.

⁹⁰ See Proposal for a Council Directive amending Directive 2006/112/EC as regards VAT rules for the digital age, COM (2022)701 final, p.4 *supranote* 20, (n.15) : "... a small-scale MNC can be expected to invest about EUR 25 000 for real-time requirements and more than EUR 50 000 in case of e-invoicing."

5 Conclusion

A pressing need to reform the system of EU VAT has been in the air since 2020.⁹¹ Considering that the current version of the VAT Directive is based on about 30 years ago, it is incapable of adapting to the digital world, and it has a structure that paves the way for VAT fraud (*EUR 3 000 lost every second in the EU VAT revenues*)⁹², one must admit that the steps taken with the ViDA are vitally important.

Although several Member States have accepted some reporting requirements with their initiatives or by the request of derogation from Article 395 VAT Directive, a harmonization has not been established yet. Moreover, the steps to prevent MTIC fraud, which is the corollary of the VAT Gap and is considered the supreme loss of EU VAT revenue⁹³, are not effective due to the lack of administrative cooperation between Member States and the system is creating barriers within the internal market.⁹⁴

The DRR aims to unify the Member States, especially in terms of standard e-invoice reporting by abolishing ‘old-fashioned’ recapitulative statements by strengthening the trust between the Member States and establishing a control system called ‘Central VIES’ which will store and cross-check DRR data by transaction-by-transaction basis with the help of technology.⁹⁵

Even though there are critical views towards this Proposal, it is worth saying that the aims of the changes might be effective in preventing MTIC fraud, but its validity can be arguable in terms of applicability. Again, exposing the detected MTIC and/or carousel fraud to deterrent penalties at the EU level might be a crucial step towards the aim of collective action against VAT fraud.

⁹¹ European Commission, *An action plan for fair and simple taxation supporting the recovery strategy*, COM (2020) 321 final, (n.6).

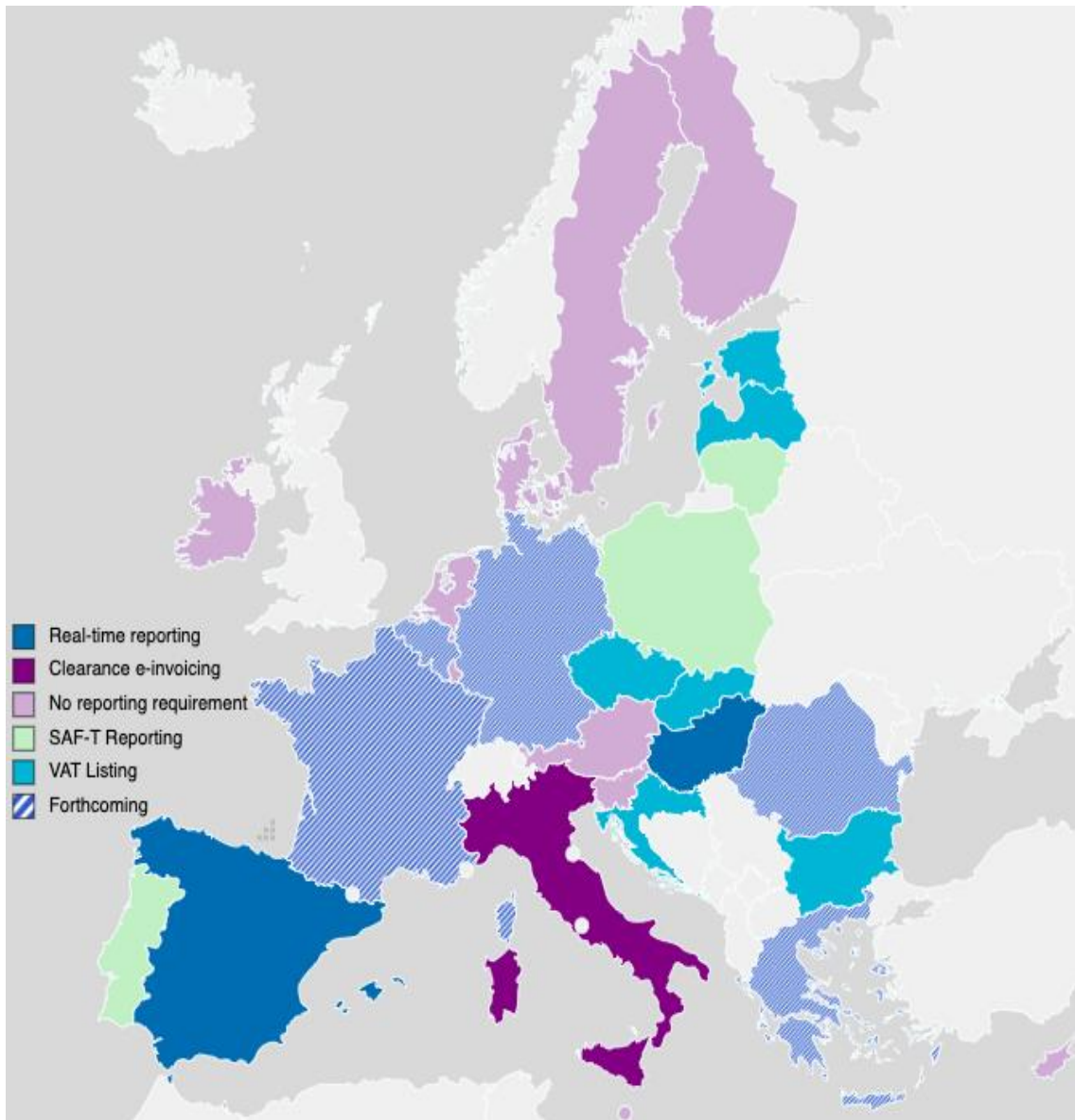
⁹² European Commission, *The VAT Gap-Facts and Figures*, available at https://taxation-customs.ec.europa.eu/taxation-1/value-added-tax-vat/vat-gap_en (accessed 04 Mar. 2023).

⁹³ Proposal for a Council Directive amending Directive 2006/112/EC, (n.1), Preamble, p.27.

⁹⁴ *Ibid*, p.28.

⁹⁵ *Ibid*, p.28-29.

ANNEX – The VAT Reporting Systems in the EU



Source: Author's elaboration based on Proposal for a Council Directive amending Directive 2006/112/EC (n.1), p.4. and EU Commission, *ViDA Final Report Executive Summary* (2022), p.8, and EU Commission, *ViDA Final Report, Volume 1 Digital Reporting Requirements* (2022), p.18 and EU Commission *Working Document Impact Assessment Report* (2022), p.16. and for Belgium, 'Belgium will make the B2B Electronic Invoice Mandatory' is available at <https://www.vatupdate.com/2023/03/08/belgium-will-make-the-b2b-electronic-invoice-mandatory/> (accessed 16 Mar. 23).

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