

THE IMPACT OF THE EUROPEAN LAW ON THE NATIONAL TAX LEGISLATION REGARDING VALUE ADDED TAX

Ramona Mihaela MOLDOVAN*
Daniela Cristina VALEA**

Abstract: *The contribution of taxes to the formation of state tax revenues varies, as a rule, depending on the level of economic development so that the contribution of the indirect taxes in developed countries is lower than that of the direct taxes and the share of the indirect taxes in the total tax revenues knows differences from country to country. Each state, enjoying tax sovereignty, establishes its national fiscal policy according to the political, economic, social and moral conditions that give local specifics, thus creating differences in the revenue structure from one state to another. Although improperly appointed as a tax, VAT represents also an indirect tax, consisting of tax levy placed on the patrimony and the movement of goods and services. Being considered at present, the only real Community tax, it benefits from a number of particular Community provisions, provisions which even the Romanian legislation and tax system had to rally to.*

Keywords: VAT, direct tax, fiscal policy, fiscal amortization, fiscal legislation

JEL Classification: K 34

Indirect taxes - important category of budget revenues

For achieving the goals regarding the economic and social development of the country, it is necessary that the national public budget to be systematically fed with an adequate income¹. Among the state revenues, a major share is being represented by the taxes, which are a levy form of a part of the income and/or the wealth of individuals and businesses to the state in order to cover public expenditure, levy that is necessarily done with a definitively title (grant) and, unlike taxes, without direct consideration of the State².

Taxes can be collected directly from individuals and legal entities who, according to the intention of the legislator, must bear at appointed terms, the tax burden based on the fiscal instruments available to the fiscal bodies regarding the people, properties, possessions or the income of each taxpayer and of the quotas set by law (these taxes are called direct taxes) or they

* Teaching assistant, "Petru Maior" University of Tîrgu-Mureş, Faculty of Economics, Law and Administrative Sciences, Romania.

** Assistant professor, PhD., "Petru Maior" University of Tîrgu-Mureş, Faculty of Economics, Law and Administrative Sciences, Romania.

¹ See Gh.D. Bistriceanu and the collective: "*Finanţele agenţilor economici*", Economic Publishing House, Bucharest, 2001, p. 316.

² See Iulian Văcărel, Gh. D. Bistriceanu and the collective, „*Finanţe Publice*”, the 4th edition, Didactic and Pedagogic Publishing House, Bucharest 2004, p. 358

could not be established directly and nominative on taxpayers, but to set upon the sale of goods or upon labor conscription (the indirect taxes).

Indirect taxes are those sources of budgetary revenues that occur mainly in the form of taxation on consumption, levying upon the sale of goods, upon the carrying out of certain services, respectively upon the execution of some works. It concerns exclusively the consumption of goods and services, causing a fiscal burden sharing, meaning that the taxes are due and payable by a person, but shall be borne by another person³.

Indirect taxes have certain characteristics⁴: 1. they are levied on the sale of goods and services by adding a tax rate to prices and fees; 2. they are collected from all persons who purchase goods and services subjected to the indirect taxation, regardless of the income, wealth or their personal condition; 3. they are determined in proportional rates regarding the sale price of goods and services on a settled sum per unit thereof; 4. they have a highly regressive characteristic, because of the discrepancy between the amount of income of different social categories; 5. they have an unfair characteristic, because they don't provide a non-taxable minimum income, do not include certain facilities for those with children or persons in their care, and at the same time they are beneficial for the persons with high income; 6. they are transferred to the public budget by the producers, traders, however, they are borne by consumers being included in the prices of goods or in the services charges, in this respect there is a discrepancy between the tax payer to the budget and the real payer; 7. their use, as in the case of direct taxation, results in a lower living standard for people, because by reducing the real income it is diminished the purchasing power of population 8. their size is unknown to the consumers, being "hidden" in prices or charges; 9. they show a greater sensitivity towards the economic situation (for example, when a certain economy has an upward trend, indirect taxes may have a high tax return and reverse in the situation of economic recession); 10. their perception is convenient and requires a relatively low cost.

VAT - an indirect income of the modern countries

Indirect taxes can be divided into: general, those that cover all goods, whether they are consumer goods or capital goods (VAT) or special, which are laid only on certain goods or services (custom taxes, excise taxes)⁵.

Over the time, indirect taxes were introduced in various forms: cumulative tax, imposed at all stages where products pass, the moment they leave the sphere of production until they reach to the consumer, their absolute extent depending on the circuit route length, depending on the number of firms that are interposed between producer and consumer, the flat tax, monophasic, applied either to production either to sales, the flat tax but only with fractional payment – the income is calculated considering the value added tax in each stage of the economic circuit⁶. Value added tax represents the difference between the value of a good obtained from the sale and the value of all goods and services purchased for the achievement of that good⁷.

For the first time, this type of tax, called value added tax was introduced in France by the fiscal reform of 1954-1955⁸, with the aim to eliminate the repeated taxation, or cascade taxation, and it was limited to the production and wholesale trade, then it was extended by the Law of January 6, 1966 to the retail trade, handicrafts and provision of services and finally by the Law of December 29, 1978 it was extended to liberal professions⁹. Later it was adopted by all member countries of the European Community (now European Union) since January the 1st, 1970¹⁰. Later, other states that were not yet members of the European Community took over this tax system. In

³ See Mircea Ștefan Minea, Lucian Teodor Chiriac, Cosmin Flavius Costăș, „*Dreptul finanțelor publice*”, Accent Publishing House, Cluj-Napoca, 2005, p. 286.

⁴ See Gh. D. Bistriceanu, „*Lexicon de finanțe, bănci, asigurări*”, Economic Publishing House, Bucharest, 2001, p. 250.

⁵ See Mircea Ștefan Minea, Cosmin Flavius Costăș, „*Drept financiar*”, vol. II, Sfera Juridică Publishing House, Cluj-Napoca, 2006, p. 39.

⁶ See Dan Drosu Șaguna, „*Drept financiar și fiscal*”, vol. II, Oscar Print Publishing House, Bucharest, 1997, p. 128.

⁷ See Dan Drosu Șaguna, „*Tratat de drept financiar și fiscal*”, C.H.Beck Publishing House, Bucharest, 2001, p. 809.

⁸ By the Law of April 10, 1954.

⁹ See Michel Bouvier, M. Christine Esclassan, Jean Pierre Lassale, „*Finances publiques*”, 4th edition, L.G.D.J., Paris, 1998, p. 595.

¹⁰ See Dan Drosu Șaguna, „*Drept financiar și fiscal*”, p. 252.

Hungary, the VAT has been introduced since 1988, in Poland in 1993, in the Czech Republic and Slovakia in 1992¹¹ and in Bulgaria in 1995¹².

VAT was defined as a general tax regarding the consumption applicable on goods and services directly proportional to the product price, regardless of the number of transactions carried out before the stage when the taxation was done¹³.

VAT is a fairly significant percentage of the total gross domestic product (GDP) of our country (about 6%) and it is predicted a rising value.

Regarding the European Union budget, VAT is the "solution to balance the overall EU budget"¹⁴. VAT revenues are achieved through allocation by the Member States of a part of the proceeds from the collection of VAT by applying a uniform rate (1% in 1970, 0.5% in 2000, 0.3% in 2007 and 0.5% in 2008) to the VAT assessment from each member state¹⁵ harmonized (the tax being calculated on a (trim)¹⁶ basis unified in all the member countries¹⁷. As shown in a performed study, VAT is the only tax that meets the most criteria of a Community tax, namely: revenue sufficiency, stability, visibility, lower operating costs, equity¹⁸.

The European Union Directives in the field of VAT

At the Community level, the VAT is regulated by several directives, documents that set only binding targets for the Member States, leaving it up to them the ways to achieve them¹⁹. The most significant was the Directive 77/388/EEC (the sixth of the Council of May 17, 1977) regarding the harmonization of legislation of the Member States in what concerns the turnover taxes – the common system of the value added tax, modified later by numerous directives.

Gradually, through successive Community regulations there was shaped a Community regime applicable to this indirect tax. There are established aspects regarding the taxable subjects (any person carrying out economic activities imposed), taxable operations (supplies, services, exchange of goods or services, importation of goods), the deductibility²⁰ and the generator factor of VAT (making taxable transaction). Following the Directive. no. 77/338 the uniform trim²¹ was established for all Member States (6 at the time). To remove a number of difficulties, the rule which should govern the application of VAT in the Community territory should be that of taxation in the state of origin and not in the state of consumption, which would mean that each trader should pay VAT at the normal rate of the country in which they operate and to deduct the paid VAT anywhere within the European Union on its common declaration of VAT. The Directive 99/49/CE has considered the application of a minimum VAT rate, that of 15%, but also reduced rates for certain goods or services (equal to or greater than 5%) (some states were allowed to keep VAT rates below 5%).

The new Directive regarding VAT is the Directive 112/2006²², which is a "recap" of the previous systematic provisions. Its value results primarily from the transcript of the provisions in a simplified manner, in titles, chapters, sections and subsections, which allow an easier understanding of the text.

¹¹ It is remarkable that there were only 8 taxes in these countries, one of which was VAT.

¹² See Dan Drosu Șaguna, „*Tratat de drept financiar și fiscal*”, CH Beck Publishing House, Bucharest, 2001, p. 644, 645.

¹³ The mechanism: along the entire manufacturing process, each trader pays VAT to its suppliers (along with the price they pay for raw materials, energy), then he collects the VAT from the purchaser of his goods (which pays VAT once with the price of the goods), reduces VAT on all raw materials and services that were rendered and the balance (difference) is paid to the budget. The final consumer bears the VAT as part of the price of purchasing the product or service. VAT is a tax affecting consumption.

¹⁴ See Mircea Ștefan Minea, „*Drept financiar internațional*”, Accent Publishing House, Cluj-Napoca, 2001, p. 70-

¹⁵ See Norel Neagu, „*Fraudarea bugetului comunitar*”, Wolters Kluwer Publishing House, Bucharest, 2008, p. 40.

¹⁶ The trim represents the way of settlement of the budget income by the taxable subject or matter.

¹⁷ See Mircea Ștefan Minea, Lucian Chiriac, Cosmin Costăș, *op.cit.*, pp. 374-375.

¹⁸ See M. Șt. Minea, Cosmin Flavius Costăș, „*Fiscalitatea în Europa la începutul mileniului III*”, Rosetti Publishing House, Bucharest, 2006, p. 339.

¹⁹ See Augustin Fuerea, „*Manualul Uniunii Europene*”, the 3rd edition revised and modified, Universul Juridic Publishing House, Bucharest, 2006, p. 143.

²⁰ The VAT payers are entitled to deduction for goods or services destined for the achievement of taxable transactions.

²¹ The method of settlement of the budget income regarding the taxable object or material – the direct method, the indirect method, the method of settlement on flat tax grounds, the administrative method).

²² Published in the Official Journal of the European Communities (JOCE) no. L 347 of December 11, 2006.

Also, once with the development of technology and an increased use of the electronic media, the new directive specifically provides the use of electronic invoicing, electronic storage of invoices, electronic elaboration of certain statements and discounts, the need to establish special procedures for operators that carry out services electronically²³. Thus, on a national level, we could mention the Register of nontransferable goods and the Register of the goods received, which may be drawn up manually or by typing, but also using the computer system, and may be stored by any means, on Romanian territory, and if they are drawn up electronically they can be kept in any place, on condition that during storage it is guaranteed the online access to the data and they are available to the reach of the responsible fiscal authorities without delay²⁴.

Community provisions relating to tax rates

Following political agreement on VAT set with the occasion of the Economic and Financial Council of June 24, 1991, EU Member States have pledged that in the period 1993-1996 to harmonize their incident regulations regarding this tax, in order to reach the application, throughout the Community, to a level equal to 15% or above it, but also the suppression of the increased rates (especially for luxury goods), issue that hasn't been set entirely²⁵. However, for instance, in France, by the application of the Community provisions, by the Law of April the 1st, 1992 the surcharge of 33.33% for luxury products²⁶ has abolished.

The Directive 112/2006 resumes these provisions and provides in the Art. 97 the following: "(1) From January the 1st, 2006 until December 31, 2010, the standard rate cannot be more than 15%. (2) The Council decides, in accordance with the article 93 of the Treaty, regarding the level of the standard rate applied after December 31, 2010. "

And in the Art. 98 and 99 there are provided the reduced rates: "The Member States may apply either one or two reduced rates. The reduced rates apply only to supplies of goods or services in the categories listed in Annex III. Reduced rates are fixed as a percentage of the base of taxation, which can not be less than 5%.

How it was implemented at a national level, it is shown in the table below²⁷.

Country	The standard rate	The reduced rate
Austria	20,0 %	12,0 or 10,0 %
Belgium	21,0 %	12,0 or 6,0 %
Bulgaria	20,0 %	-
Cyprus	15,0 %	5,0 %
Denmark	25,0 %	-
Switzerland	7,6%	3,6% and 2,4 %
Estonia	18,0 %	5,0 %
Finland	22,0 %	17,0 and 8,0 %
France	19,6 %	5,5 și 2,1 %
Germany	19,0 %	7,0 %
Greece	19,0 %	8,0 and 4,0 %
Ireland	21,0 %	13,5 or 4,4 %
Italy	20,0 %	10,0 and 4,0 %
Latvia	18,0 %	9,0 or 5,0 %
Lithuania	18,0 %	9,0 or 5,0 %
Luxembourg	15,0 %	12,0 - 9,0 - 6,0 - 3,0 %
Malta	18,0 %	5,0 %
Portugal	20,0 %	12,0 or 5,0 %
Poland	22,0 %	7,0 or 3,0 %
Czech Republic	19,0 %	9,0 %
Great Britain	15,0 %	5,0 %
Romania	19,0 %	9,0 %
Slovakia	19,0 %	-

²³ See the exposition of motives of the Directive, section 45 and 56 and Title XI, Ch. 4, Section 4.

²⁴ See Ilie Popovici, „Organizarea evidenței în scopul taxei pe valoare adăugată”, in „Impozite și taxe”, Monthly journal, Tribuna Economică Publishing House, no. 9/2007, p. 10

²⁵ See M. Șt. Minea, Cosmin Flavius Costăș, *op.cit.*, p. 80

²⁶ See Michel Bouvier, M. Christine Esclassan, Jean Pierre Lassale, *op.cit.*, p. 595

²⁷ Source: www.wikipedia.org

Slovenia	20,0 %	8,6%
Spain	16,0 %	7,0 , 4,0 and 0 %
Sweden	25,0 %	12,0 or 6,0 %
Hungary	20,0 %	5,0 %

We can see that the rate systems of the Member States comply with the Community provisions, unlike the tax rates from the states outside the Community. By the negative popular vote given to the Agreement regarding the European Economic Area in December 1992, Switzerland is the only country in Western Europe, with a major economy, which is not part of the EU. It is to be noted that in Switzerland the rate is only 7.6%, which makes Switzerland be considered a true "fiscal paradise", many entrepreneurs establishing their fiscal setting in this country. The standard rate is 7.6% and the low ones are of 3.6% for hotel services, respectively 2.4% for food and non-alcoholic drinks, books, newspapers and magazines²⁸.

In European Union member states, the reduced rates apply to different products, so that in Italy for example, the reduced rate of 10% applies to hotel benefits, restaurants, cafes, and the rate of 4% to agricultural products and to publishing houses²⁹. In Austria, the reduced rate of 10% applies to food, books, newspapers and works of art³⁰.

In our country, the standard rate in 1997 was if 18% and reduced one of 9% (for animal meat and poultry, fish, milk, oils, fats, medicines³¹). We can see, comparing the current situation, a small increase in the standard rate from 18% to 19%, and a change in the categories of goods that benefit from the reduced rate of VAT: the access to castles, museums, memorial houses, historical monuments, architectural and archeological monuments, zoos and botanical gardens, fairs, exhibitions and cultural events, cinemas, school manuals, books, newspapers and magazines, (except those intended exclusively or mainly to advertising), prostheses and accessories thereof, except dentures, human and veterinary medicines, etc..

Taxable operations

At present, the taxable operations can be divided into three categories³²: taxable in their nature (e.g., purchase for resale, lease of movable property), taxable by law (e.g., operations carried out by agricultural cooperatives, activities similar to those of traders, certain real estate transactions, imports) and taxable transactions in option (from the date of Romania's accession to the European Union the construction and land sales are exempt from VAT, except for the sales of new buildings³³ and structural lands, according to the Article 141 paragraph 2 letter a of the Fiscal Code. Regarding the classification of land within the structural land or any other land (agricultural, forestry, orchard, pasture, etc.), it refers to the classification given to that land when sold by cadastral sheet or by planning permission. Therefore, any taxpayer who sells land, other than those structural ones, or buildings, other than the new ones, may apply for an exemption from VAT. However, taxable persons may apply by option charging for land sales, other than those structural ones and of buildings, other than the new ones, for which taxation is compulsory by law in accordance with Art. 141 paragraph 3 of the Fiscal Code. Usually, it opts for construction and land sales taxation to avoid the adjustments calculation of VAT and possibly of the deduction peroration.

In the Chapter 4, Title VI of the Law. 571 of December 22, 2003 regarding the Fiscal Code³⁴ there are established the operations which are subjected to value added tax in our country.

But a question which arises concerning the field of application is whether they may be considered taxable operations and some of them illegal operations.

²⁸ Provisions for VAT rates are found in the Constitution of Switzerland in the Art. 130, voted by referendum on November 28, 2004, that came into force on January 1, 2007.

²⁹ See M. Șt. Minea, C. F. Costaș, *op.cit.*, p. 150.

³⁰ *Ibid*, p. 85.

³¹ See Dan Drosu Șaguna, „*Drept financiar și fiscal*”, vol. II, p. 263.

³² See Raymond Muzellec, „*Finances publiques*”, 11 editions, Ed. Sirey, Paris, 2000, p. 374.

³³ For the purposes of the law, a building is considered new in the tax effect from the date of the first occupation, which coincides with the date of receiving the minutes, until December 31 of the following year.

³⁴ Published in the Official Gazette no. 927 of December 23, 2003.

The European Court of Justice ruled that there must be achieved a distinction concerning VAT between licit and illicit transactions. But this distinction should not be generalized. On principle, all operations may enter the sphere of application concerning VAT. But certain products with special characteristics that should prevent their movement in the ordinary economic cycle, which excludes any competition between the legitimate economic sector and an unlawful sector, are excluded from the application of these rules. Thus, operations such as supply of narcotic drugs or counterfeit currency traffic, as it is the object of a sales ban in all the Member States are not subject to VAT. In the Case *Happy Family* the Court noted that the economic movement of certain narcotic drugs is strictly prohibited and that the supply of such products are not subjected to the European directives and VAT is not owed³⁵.

But there is also the situation where a performed activity represents an infraction, but nonetheless it has the nature of an economic activity and thus there is a competition in the respective sector for lawful activities (we can recall here the unauthorized export of information systems, counterfeit perfumes, organizing illegal gambling). Placed in the position of deciding in such a legal issue, the European Court of Justice had to answer also to a moral issue. On one hand, if it includes such operations in the scope of VAT, this would mean that the company is accepting such activities. On the other hand, exemption from VAT for certain activities that are condemned by the society is an advantage offered to these activities towards the legal ones.

Approached with the preliminary action in the case *Café Siberia*³⁶, the Court had to decide whether renting a table in a cafe in the Netherlands to a person, in order to sell soft drugs represents an "economic activity", so that the owner may be considered "taxable individual" to whom there should be applied the rules regarding value added tax, or being accessory to the crime of drug traffic, it is not subjected to taxation. In this case, the Court took into account the fact that at that time in the Netherlands there were in force the Instructions of the Dutch Public Minister of 1996, under which, although the supply of soft drugs was an infraction, it was not prosecuted under certain circumstances if there is an agreement on this issue within the local authorities³⁷. Therefore The Court decided that, although illegal, the activity has the character of an economic activity of renting and it doesn't prevent competition in this sector, including the competition between licit and illicit activities. Non-application of the VAT rules would therefore undermine the principle of neutrality that underlies the common system of VAT.

Of course, we cannot accept any reverse situation, namely to subject to the payment of VAT the illicit operations, if those of the same kind, but carried out on law terms are exempt from VAT. This was the decision of the European Court of Justice in a recent case, stating that if the operation of gaming machines in casinos is exempt from VAT, so must be in the case of their operation outside the casino, regardless that operation is or is not licit in the respective State³⁸.

VAT - Export incentive

An important feature of VAT is the fact that it is always borne by the beneficiary and therefore, in the case where a commodity would be produced in a country and capitalized into another country, then the tax is applied in the state that actually revaluates the respective commodity, so everything that is exported is absolved of this tax³⁹.

Regarding foreign trade, there are no VAT charges for exports, but for the imports there is a compensation tax. For the exports made, the state returns to the company the deductible VAT (payable in upstream). In the export business, because of detaxation, the goods become more competitive in price. VAT levied on imports has the role of compensating for export losses arising sequel detaxation. If goods were delivered to the internal, state revenues would increase. Moreover, by this VAT on imports there is achieved an equalization of opportunities for the national

³⁵ See the Decision of the Court of Justice in the Case C-289/86, *Happy Family v. Inspecteur der Omzetbelasting*.

³⁶ The Decision of the European Court of Justice, Case of June 29, 1999, Case C-158 / 1998, *Staatssecretaris van financiën c. Café Siberia*.

³⁷ See Daniela Ivan, „*Hotărâri recente și consacrate ale Curții de Justiție a Comunităților Europene*”, C.H.Beck, Publishing House, Bucharest, 2007, p. 341.

³⁸ See M. Șt. Minea, C. F. Costaș, *op.cit.*, p. 271 – The Decision of the European Court of Justice of February 17, 2005- *Finanzamt Gladbeck e Edith Linnerweber (C-453/02) and Finanzamt Herne – West c. Savvas Akritidis (C-462/02)*.

³⁹ See Dan Drosu Șaguna, *op.cit.*, p. 254.

companies in comparison with the foreign ones, because if there weren't VAT on import, the external goods would be more competitive by price than the national goods.

After Romania entered the European Union, in the context of the European single market and of the elimination of the border customs, import has been redefined by the Fiscal Code, in the Article 131. Thus, import means the entry of goods which are in free circulation into the Community territory, i.e. the products proceeding from a third country for which there were made the formalities in any Member State and the customs taxes were paid.

Therefore, intercommunity trade does not involve an import-export activity. The concept of import was replaced with the concept of intra-community acquisitions and the export bears the name of intra-community delivery. Currently, intercommunity trade of goods and services is exempt from VAT, this tax being applied only to the country of final consumption, which gives the possibility of fraud (the purchase of a product with no taxes from a member country in order to resell it later in the country of destination by adding VAT).

Entities that carry out intra-community acquisitions must provide to the tax authorities all the transactions and then there is a system regulating the application of VAT in each EU state. There may be a difference between VAT of acquisitions and the VAT of intra-community deliveries, as shown in the table above, the rates vary from country to country. It is therefore necessary for the Treasury to have careful control of the intra-community acquisitions and deliveries but also of the exchange of data in order to detect the possible cases of tax evasion.

The Directive 112 provides (in article 402 paragraph 1) that this arrangement is temporary and will be replaced by the final arrangement based, on principle, on the taxation in the Member State of origin for the goods or the carrying out services. Thus, the national tax authority which collects VAT will return the funds, proceeding from the VAT collected, to the country of destination.

Conclusions

Value added tax is an indirect tax that brings, as shown above, a significant contribution to the state budget and to the European Union budget. Although called "tax", it meets the elements of a tax, and we believe that renaming it would be necessary in order to show the income category to which it belongs (as for example in Italy - imposta sul valore aggiunto).

Regarding the taxable transactions there sometimes arises problems not only legally speaking but also morally speaking: should there be subjected to taxation certain illegal acts, even if they give the impression of acceptance or to accept the idea that being infractions they cannot be taxed thus creating an advantageous position against products of the same gender, licit products. In the context where an absolute elimination of illicit activities on the European market is not feasible, we consider as being correct the solution of the European Court of Justice to submit to the payment of VAT even those services and goods that are illegal if they create a competitive market. Otherwise, we would favor and encourage more illegal acts.

At present, we can assert that the VAT is the only true communitarian tax, believed to be the solution for balancing the budget of the European Union. A part of the collected VAT on a national level is transmitted to the European Union budget, thus increasing revenues and there's also the aim to create a harmonized tax base and also a communitarian tax rate (proposal 2%). The Directive 112/2006 aims to simplify intercommunity trade (e.g. by the provisions relating to electronic bills and the possibility of data storage on electronic media) and reducing, as far as possible the tax evasion. The aim is to reach a Community system of taxation of the national kind, meaning taxation in the country of origin, and not in the country of destination. We believe this would significantly reduce tax evasion on the Community level.

