



Newsletter n. 3/2013

## Subjectively non-existent transactions Trader “awareness” and power-sharing problems

More and more frequently, in case of subjectively non-existent transactions the Italian Supreme Court, by referring to the Court of Justice, denies VAT deduction with the “creative” “*knew or should have known*” to be participating in a fraudulent transaction<sup>1</sup>.

It seems that the Supreme Court keeps on overlapping two different issues: subjectively non-existent transactions - which are issues of relative simulation - with the so called “Carousel fraud”, which are simply cases of non-payment of VAT<sup>2</sup>.

The VAT deduction right can be denied in the event of non-existent transaction between the parties indicated on the invoice.

It is, anyway, necessary, to prove – as it is now acknowledged by both the Legal Supreme Court and the Supreme Tax Court – a “trilateral simulating agreement” among interposing, fictitious interposed and real transferor.

It often occurs, anyway, that the real transferor is not even identified.

The failure to pay VAT is a “different issue”: it is generally considered to be a violation of the sole transferor, that has nothing to do with the non-existence of the transactions; indeed, we might say that the existence is a condition of the charge of failure of a conduct which is (obviously) due.

For such cases our legislator laid down art. 60-bis, VAT Decree, yet in 2004 (introduced by art. 1, paragraph 386, Law 30.12.2004, n. 311), by providing for a co-obligation of the transferee, not for the denial of VAT deduction.

And it applies only in case of purchase at lower prices than the market ones (in presence of a prior Decree of the Minister of economy and finance).

It is therefore necessary an objective circumstance, namely the purchase at lower prices than the market ones, in order to justify a joint liability of the trader.

No subjective element of other's fraud awareness is foreseen in art. 60-bis, VAT Decree. This has been the clear choice of our tax legislator since 2004 in order to counter

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<sup>1</sup> We consider “creative” the well known criterion “knew or should have known”, increasingly used to deny the VAT deduction, as the cases considered by the Court of Justice refer to real interpositions with failure to pay VAT, and not to fictitious interpositions.

<sup>2</sup> Also in the legislative Decree 10 May 2000, n. 74 the offense of “fraudulent misrepresentation through the use of invoices for non-existent transactions” (art. 2) is distinct from the offence of “failure to pay VAT” (art. 10-ter).

the so-called "Carousel frauds" (non-payment of VAT of a trader in the chain).

Other jurisdictions, close to our, such as UK<sup>3</sup>, France<sup>4</sup> and Germany<sup>5</sup>, have laid down by law the subjective element of the "awareness" in the event of omitted VAT payments of an upstream supplier. Which denotes a culture which respect the legal certainty.

\* \* \*

A jurisprudence that, in absence of the rule of law, establishes the denial of VAT deduction in the event of failure to pay VAT due to awareness of the transferee, creates legal uncertainty for both economic operators, and public officials.

Legal certainty is one of the foundations of the "rule of law". As for the concept of the "abuse of rights", even in cases of denial of VAT deduction, the tax legislator continues to allow plenty of room for action to the Jurisprudence, with obvious problems of powers' division.

Moreover. The choice to fight with such a measure (denial of VAT deduction), the behavior of those who would participate (note, not on the action level, but on that of mere awareness) of a failure to pay VAT of another person, also raises problems of conformity with the proportionality principle<sup>6</sup>.

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How can the taxpayer defend himself from a jurisprudence that focuses on the "knew or should have known" to be participating in other's fraudulent behavior?<sup>7</sup>

While waiting for a change of law or for clear legislative guidelines, perhaps the taxpayer - doubtful about the fulfillment of tax liabilities by suppliers and customers, by adapting to the Community jurisprudence that places a duty to control on the public party<sup>8</sup> - will be forced to rely on the cooperation of the tax administration, by requesting a previous authorization to trade with certain subjects. The cooperation would be particularly important in order to fight in advance potential frauds.

In this way the good faith (or lack of awareness) of the taxpayer should be saved, and also the right to deduct; otherwise we would get the block of trade which is the reason that gave birth to the European Community.

*Giovanni Moschetti*

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<sup>3</sup> Art. 77A of the *Value Added Act*, introduced in 2003.

<sup>4</sup> Paragraph 4-*bis* of art. 283, CGI (*Code Général des Impôts*), introduced with the Budget Law of 2006.

<sup>5</sup> § 25d *Umsatzsteuergesetz* (VAT law), modified with effect from the 1th of January 2004.

<sup>6</sup> *Mutatis mutandis*, it comes to mind an ancient teaching that well combines legal certainty and proportionality. In the *Apology of Socrates*, the student Plato reports the teacher's words addressed to the judges that sentenced him to death (among other things) for corruption of youth: "If I corrupt young people without awareness, this is an accidental fault that the law does not punish with a criminal prosecution, just exhorting to call the liable person in private in order to warn it appropriately. It is clear that, if rightly warned, I won't incur any more in a, without awareness, mistake".

<sup>7</sup> Moreover, we remind that in Italy there isn't the witness evidence.

<sup>8</sup> See the *Mahageben kft* case decided by the Court of Justice (C-80/11), and our Newsletter n. 7/2012.

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