

INFORMATION NOTE

VAT CAROUSEL FRAUD: HOW TO RECOGNIZE RISKY SUPPLIERS?

Pursuant to Article 272-3 of the French Tax Code, French VAT incurred on purchases of goods is not deductible when it is demonstrated that the purchaser is participating in a fraud consisting in not paying the VAT due on the basis of its purchase.

Therefore, if **the Tax Administration can demonstrate through a body of evidence that the purchaser must have known about the fraud committed by the supplier**, it would have the right to reclaim the VAT which was deducted and apply the 40% penalties for deliberate breach, or even 80% for fraudulent maneuvers.

For companies wishing to limit the risk of being involved in a carousel-type fraud, the French Tax Administration has recently published a non-exhaustive list of indicators allowing them to detect “risky” suppliers.

SUMMARY

The list of indicators should alert operators to the possibility of a supplier being involved in a carousel-type VAT fraud network. These indicators relate to some of the supplier’s general characteristics, the transaction and its invoicing as well as the payment terms.

As the Administration points out, some of these indicators taken separately are not necessarily risk-bearing. **It is the combination of several criteria which should alert the operator.**

When a supplier is concerned by several of these indicators, the operator can complete its review by asking it to produce a certificate proving its good standing in tax matters. However, such a certificate has no value with respect to a company whose deadline for filing its VAT returns has not yet passed.

KEY FOCAL POINTS

The Tax Administration lists the following indicators:

- Indicators concerning the supplier’s characteristics :
 - An invalid intra-community VAT number of the supplier;
 - A company engaging in operations that are unrelated to or far removed from its habitual activity;
 - A company operating in sectors prone to carousel-type VAT fraud;
- Indicators concerning the characteristics of the transaction, the agreement and the invoicing:
 - A transaction price that is abnormally below the market price;
 - No indication of a sales contact or a contact that is difficult to identify;
 - Canvassing by a business finder or an intermediary looking to establish relationships with unknown suppliers;
 - A high down payment compared to the total amount invoiced or the absence of an invoice when the invoiced amount is high;
 - An invoicing circuit that is different from the delivery circuit.
- Indicators concerning payment terms:
 - No bank account or bank account abroad;
 - Insistence on payment in cash or very quick payment.

OUR RECOMMENDATIONS

The French Tax Administration invites operators to be extremely vigilant so that they are able to recognize suppliers involved in VAT carousel fraud.

Where there is a combination of several indicators, operators should carry out (additional) investigations.

If such investigations are not conducted, besides challenging the VAT that was deducted and possibly applying the 40% penalties for deliberate breach, or even the 80% penalty for fraudulent maneuvers, the French Tax Administration could (as the case may be):

- Challenge the exemption of the intra-community delivery made by a taxable person who knew, or who must have known, that the presumed recipient of this delivery did not have a real activity;
- Set up a procedure whereby customers who knowingly participated in a fraud network assume joint and several liabilities for payment.

In such context, we highly recommend that operators with an extensive taxonomy of suppliers set up an audit in order to carry out the recommended additional investigations and thus assess the risk of fraud.

As a second step, an anti-fraud VAT process could be implemented in order to establish, in case of a subsequent tax audit, that the operator did not know it was involved in a VAT fraud scheme.

Such internal process should be based on an operational action plan specifying the internal processes and the anti-fraud indicators applied to identify potential risks (for the past) and secure day-to-day practices (for the future).

So as not to multiply the number of different internal documentations, and since such work should be carried out to secure VAT treatments of some operations, the documentation could be incorporated into the documentation establishing the reliable audit trail for invoicing purposes.

This alert from the French Administration requires a proactive approach where companies are expected to monitor the "VAT profiles" of their suppliers.

OUR ASSISTANCE

Fidal's lawyers are at your disposal for any assistance you may need, in order to review the processes implemented in your company to limit the risk of participating in a VAT carousel fraud scheme.

Fidal's lawyers are also at your disposal for any assistance you may need in preparing or reviewing your documentation showing that all additional investigations have been duly carried out. Such documentation could indeed be communicated in the context of a tax audit.

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