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Use of the Input Tax Deduction Mechanism in the VAT System for the Purpose of "Tax Carousel" Fraud

Abstract

The article discusses the phenomenon of "tax carousels" in the tax on goods and services, which is a specific abusive practice and is used for VAT refund scam purposes. A discussion on the jurisprudential doctrine of the abuse of law and good faith as offered by the Court of Justice of the European Union is followed by an analysis of the judicial decisions (case-law) issued in this area, which proves that taxable persons involved in value-added tax fraud practice have no right to a tax deduction. Meanwhile, those taxable persons who have fallen victim to tax fraud practices may quote the good faith doctrine and exercise the right to a tax deduction. The judicial decisions of the Court of Justice of the European Union have had a significant impact on the judicial decisions issued by administrative courts in Poland. The Supreme Administrative Court (SAC) tries to define the notion of a "tax carousel" in its decisions, as the notion is quite broad.

Keywords: value-added tax, jurisprudential doctrine of the abuse of law, doctrine of good faith, the notion of a tax carousel

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Introduction

It is firstly necessary to stress that the notion of a tax carousel in the context of notions such as: tax fraud, tax abuse, the abuse of law, trading carousel or tax law avoidance has not been so far defined with regard to the tax on goods and services. Only the Act of 13 May 2016 amending the Tax Ordinance and Certain Other Acts (Journal of Laws of the Republic of Poland of 2016, item 846), effective since 15 July 2016, makes the regulation provided in Article 5, section 5 of the Act of 11 March 2004 on the Goods and Services Tax (uniform text of 2017, item 1221 as amended) allow for a certain identification of the notion of the abuse of law. According to the provision in question, the abuse of law shall be understood as conducting activities referred to in section 1 (i.e. activities subject to taxation) as part of a transaction that may be in line with the formal conditions defined in the provisions of the act, but its essential goal is to gain tax advantages, the granting of which would be against the purpose of the said provisions.

Before the said legislative changes were introduced, the notion of the abuse of law was not a normative concept, defined by the legislator in tax law provisions. It functioned in the tax law doctrine and in administrative courts' decisions as a notion describing certain patterns of action adopted and followed to obtain undue gains. When it comes to its adoption in the realm of VAT, it usually involved taking advantage of the structure of this tax to recover input tax illegally.

But there is no normative definition for tax carousels. It seems that the notion of the abuse of law is very broad, and a tax carousel is something that fits the spectrum of acts classifiable as the abuse of law. It is especially impossible to claim that a tax fraud is not an abuse of law (a tax abuse), but – quite importantly – an abuse of law will not always take on the form of a tax fraud or a trading carousel.[2] The above claim was proven by the SAC in its judgment of 25 February 2015 (ref. no. I FSK 93/14), where it was argued that in view of VAT, the abuse of law within the meaning of Article 58 § 2 of the Act of 23 April 1964 – Civil Code (Journal of Laws of the Republic of Poland from 2017, item 459, as amended) in relation to Article 88, section 3a, item 4, letter c of the VAT Act, shall be understood as an activity

[2] See also: SAC judgments of 27 June 2017, ref. no. I FSK 208/17, ref no. I FSK 371/17, ref. no. I FSK 434/17, and the Provincial Administrative Court in Warsaw's judgment of 26 February 2017, ref. no. III SA/Wa 791/15.

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against the economic-social purpose of the right to tax deduction on account of the fact that even though the formal conditions to exercise that right were met, the activity was conducted to gain a tax advantage, the awarding of which would be against the purpose of the norm in question.[3] In the light of the decisions issued by administrative courts, there can therefore be no doubt about whether the so-called tax carousel fraud meets the legal definition of the abuse of law.

The quoted position is substantiated by the manner in which tax carousels are organised, and the transactions taking place therein do not cause any concern in terms of formal matters, and the goods exchanged in transgenic transactions (intra-Community supply of goods and export) are treated only as a VAT carrier, which is proven by the decisions of administrative courts as quoted further.

Apart from this, the author finds the notion of a tax carousel fitting the normative regulation provided in Article 5, section 5 of the Act of 11 March 2004 on the Goods and Services Tax.

The view that tax fraud fits the category of a tax carousel is upheld by A. Bącal and A. Brach referring to the CJEU's judgments dated 18 December 2014, ref. no. C-131/14, Italmoda case, and 8 September 2015, ref. no. C-105/14, Ivo Tarico case, classifying tax fraud as tax abuse.[4]

In the international practice, the concept of fighting the phenomenon of tax avoidance takes two forms. The first of them is activity involving jurisprudence only. Tax authorities, especially courts deciding on tax matters, have been trying – facing the legislator's silence – to define the borders of acceptable activity of taxable persons in the area of the potential abuse of law and to counteract crossing these borders using jurisprudential measures. The concepts worked out in this area by the courts have come to be called "jurisprudential doctrines addressing the abuse of law".[5]

The second way to fight the abuse of law, including making gains from tax carousels, is the introduction of normative regulations that will make it possible to prevent tax fraud or lead to unduly obtained tax advantages being reclaimed.

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3 See also: SAC judgments of: 8 May 2015, ref. no. I FSK 149/14; 5 April 2016, ref. no. I FSK 1824/14.

4 A. Bącal, A. Brach, *Nadużycie prawa w orzecznictwie polskich sądów administracyjnych*, Warszawa 2017, pp. 38–44.

5 A. Olesińska, *Klauzula ogólna przeciwko unikaniu opodatkowania*, Toruń 2013, p. 26.

Abuse of law as a jurisprudential doctrine in the decisions of the Court of Justice of the European Union on value-added tax

It should be stressed that Polish administrative courts controlling the lawfulness of administrative decisions and individual tax interpretations should adopt an interpretation in line with the provisions of EU law, i.e. one that favours this law, in their everyday practice.[6]

In a situation in which the content of a national act gives rise to questions (ambiguities), a national court is obliged to interpret the act in a way that it can be suited to the requirements of the directive. This is proven by the rich body of decisions issued by the Court of Justice of the European Union (hereinafter referred to as: the CJEU), including in the *von Colson and Kamann* case,[7] where the CJEU stated that in applying the national law and, in particular, the provisions of the national law specifically introduced in order to implement a directive, the national court was required to interpret its national law in the light of the wording and the purpose of the directive in order to achieve the result referred to in Article 189, paragraph 3 TEC. The abovementioned formula expresses an obligation to interpret the binding national law in the light of the content and the purpose of the directive with the aim to achieve a result defined by the directive, i.e. the so-called pro-European interpretation. In applying law, courts should make its national norms assume such a meaning that makes it compliant with EU law. Moreover, if courts find some national legal norms at variance with EU law, they are obliged to adopt EU norms as the basis for their decisions, rejecting national legal norms at the same time. This is a consequence of the principle of primacy of EU law over national laws.[8]

The judicial decisions of the Court of Justice of the European Union issued so far play an important part in shaping the pro-European interpretation of law. The CJEU's competence covers the interpretation of treaties, meaning the primary law of the EU. The second area of the CJEU's competence concerns the interpretation of law and covers the interpretation of acts adopted by organisational units, bodies or institutions of the European Union. This means acts of all EU institutions. Most often, the subject of interpretation will be regulations, directives, and decisions, along with non-binding opinions and recommendations since they too may be of

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6 A. Mudrecki, *Wykładnia prounijna w orzecznictwie sądów administracyjnych w podatkach obrotowych*, [in:] H. Litwińczuk (ed.), *Prawo europejskie w polskim prawie finansowym*, Warszawa 2011, p. 382.

7 Decision issued for case 14/83, Court Reports 1984, p. 1891.

8 A. Gajda, A. Mudrecki, *Glosa do wyroku Wojewódzkiego Sądu Administracyjnego we Wrocławiu z dnia 3 kwietnia 2007 r. sygn. akt I SA/Wr 152/07*, "Orzecznictwo Sądów Polskich" 2008, 6, pp. 459–460.

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significance to national bodies' interpretation and application of law. The CJEU's interpretation of law is actually a binding interpretation of EU law.[9]

Apart from this, the Court of Justice of the European Union is qualified to answer preliminary inquiries submitted by national courts. The courts whose rulings are not final may – and courts of final instance should – address the CJEU with preliminary inquiries if they find it necessary for the issuance of a judgment (Article 267 TEC). The CJEU encourages the settlement of a dispute, but it does not decide in particular cases. This is about a certain legal collaboration through which a national court and the CJEU contribute directly and mutually to the development of a specific resolution.[10] Almost every ruling of the CJEU finds that the final judgment that leads to a resolution rests with the national court that is most knowledgeable about the actual economic affairs and circumstances related to the economic activity conducted in a given state.

When the input tax deduction mechanism is applied in the VAT system with the intention to commit a fraud using a "tax carousel", there are two clashing jurisprudential doctrines worked out by the CJEU. It should be emphasised that these doctrines are not normative in their form, i.e. they are not embedded in EU law. But given the authority of the Court of Justice of the European Union and the effectiveness of EU law, they have a considerable impact on the judicial decisions of national courts, which are EU courts after all.

On the one hand, the CJEU has developed the doctrine of the abuse of law, which limits the right of taxable persons to deduct input tax in the VAT system. On the other hand, there is the doctrine of good faith, which is to protect taxable persons who have fallen victim to tax frauds.

Even before giving opinions on the abuse of law in tax related matters, the CJEU offered its opinions in the area of abuse of law in other fields of law.

The most distinctive position can be seen expressed in the CJEU's judgment of 21 February 2006, ref. no. C-255/02, Halifax plc case (published in: *ZOTSiS 2006/2A-/I-1609, ECR 2006/2A-/I-1609*). In the said judgment, CJEU argues that transactions constitute supplies of goods or services and an economic activity within the meaning of Article 2, item 1, Article 4, item 1 and 2, Article 5, item 1, and Article 6, item 1 of Sixth Directive 77/388 on the harmonisation of the laws of the Member States relating to turnover taxes, as amended by Directive 95/7, provided that they satisfy the objective criteria on which those concepts are based, even if they are carried out with the sole aim of obtaining a tax advantage, without any other economic

[9] T. Siennicki, [in:] M. Militz, D. Dominik-Ogińska, M. Bącal, T. Siennicki, *Zasady prawa unijnego w VAT*, Warszawa 2013, p. 211–213.

[10] Ibidem, p. 210.

objective. The terms 'taxable person' and 'economic activities' and the terms 'supply of goods' and 'supply of services', which define taxable transactions under the Sixth Directive, are all objective in nature and apply without regard to the purpose or results of the transactions concerned. In that regard, an obligation on the tax authorities to carry out inquiries to determine the intention of the taxable person would be contrary to the objectives of the common system of value-added tax of ensuring legal certainty and facilitating the application of value-added tax by having regard, save in exceptional cases, to the objective character of the transaction in question. While it is true that those criteria are not satisfied where tax is evaded, for example by means of untruthful tax returns or the issue of improper invoices, the fact nevertheless remains that the question whether a given transaction is carried out for the sole purpose of obtaining a tax advantage is entirely irrelevant in determining whether it constitutes a supply of goods or services and an economic activity (see items 55–57, 59–60, and item 1 of the conclusion of the judgment).

What is more, CJEU has argued that the Sixth Directive 77/388 on the harmonisation of the laws of the Member States relating to turnover taxes, as amended by Directive 95/7, must be interpreted as precluding any right of a taxable person to deduct input VAT where the transactions from which that right derives constitute an abusive practice. For it to be found that an abusive practice exists, it is necessary, first, that the transactions concerned, notwithstanding formal application of the conditions laid down by the relevant provisions of the Sixth Directive and of national legislation transposing it, result in the accrual of a tax advantage the grant of which would be contrary to the purpose of those provisions. Second, it must also be apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain a tax advantage. To allow taxable persons to deduct all input value-added tax even though, in the context of their normal commercial operations, no transactions conforming with the deduction rules of the Sixth Directive or of the national legislation transposing it would have enabled them to deduct such value-added tax, or would have allowed them to deduct only a part, would be contrary to the principle of fiscal neutrality and, therefore, contrary to the purpose of those rules. As regards the second element, whereby the transactions concerned must essentially seek to obtain a tax advantage, it must be borne in mind that it is the responsibility of the national court to determine the real substance and significance of the transactions concerned. In so doing, it may take account of the purely artificial nature of those transactions and the links of a legal, economic and/or personal nature between the operators involved in the scheme for reduction of the tax burden. Where an abusive practice has been found to exist, the transactions involved must be redefined so as to re-establish the situation that would have prevailed in the absence of the transactions constituting that abusive

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practice. In that regard, the tax authorities are entitled to demand, with retroactive effect, repayment of the amounts deducted in relation to each transaction whenever they find that the right to deduct has been exercised abusively. However, they must also subtract therefrom any tax charged on an output transaction for which the taxable person was artificially liable under a scheme for reduction of the tax burden and, if appropriate, they must reimburse any excess. Similarly, they must allow a taxable person who, in the absence of transactions constituting an abusive practice, would have benefited from the first transaction not constituting such a practice, to deduct, under the deduction rules of the Sixth Directive, the value added tax on that input transaction (see items 74–75, 80–81, 85–86, 94–98, and items 2 and 3 of the conclusion of the judgment).

According to the quoted judgment, if any transactions have been made, they should be considered subject to value-added tax regardless of their purpose. Also, any transactions that abuse the applicable law and conform to the relevant formal requirements at the same time may not serve as a basis for input tax deduction. It is the national court to eventually decide whether an instance of abuse of law has occurred or not.

In general, CJEU has developed a case law that express clearly that preventing possible tax evasion, avoidance, and abuse is an objective recognised and encouraged by Directive 2006/112.[11] In this regard, the Court of Justice has already held that Community law cannot be relied upon for abusive or fraudulent ends.[12] Therefore, the domestic administrative and judicial authorities should refuse to allow the right to deduct where it is established, on the basis of objective evidence, that that right is being relied upon for fraudulent or abusive ends.[13] A taxable person who knew or should have known that by purchasing goods or services they were taking part in a transaction connected with fraudulent evasion of VAT must, for the purposes of Directive 2006/112, be regarded as a participant in that fraud, irrespective of whether or not the person profited by the resale of the goods or services as part of the transactions.[14]

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11 See case Halifax cited above, item 71; judgments of 7 December 2010 in case C-285/09 R., item 36; of 27 October 2011 in case C-504/10 Tanoarch, item 50.

12 See, especially, the judgment of 3 March 2005 in case C-32/03 Fini H, ECR, p. I-1599, item 32; the said judgments in case Halifax and others, item 68; the judgments in joined cases Kittel and Recolta Recycling, item 54 – thesis 41 of the grounds for the judgment.

13 See e.g. the abovementioned judgments in case Fini H, items 33 and 34; in joined cases Kittel and Recolta Recycling, item 55; judgment of 29 March 2012 in case C-414/10 Véleclair, not yet published in ECR, item 32 – thesis 42 of the grounds for the judgment.

14 See Kittel and Recolta Recycling, cited above, item 56 – thesis 46 of the grounds for the judgment.

A counterpoise to the presented case-law doctrine of the abuse of law is the developed doctrine of good faith.

One of the fundamental constructive characteristics of value-added tax is the neutrality principle, whereby a taxable person cannot be levied with this tax, as it is a consumer tax that affects the final recipient, who is not subject to VAT. The taxable person has the right to deduct input tax arising from the invoice issued by a supplier of goods or services from any due value-added tax. This matter becomes more complicated when goods or services originate from unknown sources or come from a so-called tax carousel. This raises the question of whether it is possible to restrict a taxable person's entitlement to an input tax deduction – and if so, under what circumstances this entitlement may be restricted.[15]

In the judgment of the Court of 21 June 2012 in joined cases C-80/11 and C-142/11 Mahagében kft versus Nemzeti Adó- és Vámhivatal Déldunántúli Regionális Adó Főigazgatósága and Péter Dávid versus Nemzeti Adó-és Vámhivatal Észak-alföldi Regionális Adó Főigazgatósága, the CJEU held that Articles 167, 168 (a), 178 (a), 220 (1) and 226 of Directive 2006/112 must be interpreted as precluding a national practice, whereby the tax authority refuses the taxable person the right to deduct the VAT, finding that the taxable person is liable to pay the VAT due or paid in respect of services supplied to him on the ground that the issuer of the invoice relating to those services, or one of the issuer's suppliers, acted improperly, without the authority establishing that the concerned taxable person knew or should have known that the transaction relied upon as a basis for the right to deduct was connected with fraud committed by the issuer of the invoice or by another trader acting earlier in the chain of supply.[16]

Furthermore, the CJEU held that Articles 167, 168(a), 178(a) and 273 of Directive 2006/112 must be interpreted as precluding a national practice, whereby the tax authority refuses the right to deduct on the ground that the taxable person did not satisfy himself that the issuer of the invoice relating to the goods in respect of which the exercise of the right to deduct is sought had the status of a taxable person, that the taxable person was in possession of the goods in question and was in a position to supply them, and that the taxable person had satisfied his obligations with regard to declaration and payment of VAT, or on the ground that the taxable person is not in possession of, in addition to that invoice, other documents capable of demonstrating that those conditions were fulfilled, although the substantive

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15 A. Mudrecki, *The Influence of "Good Faith" on the Taxable Person's Right to Deduct the Value-added Tax in the Light of the Case Law of the Court of Justice of the European Union*, [in:] M. Radvan (ed.), *System of Financial Law, System of Tax Law: Conference Proceedings*, Brno 2015, p. 332.

16 SIP LEX no. 1165797, www.eur-lex.europa.eu

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and formal conditions laid down by Directive 2006/112 for exercising the right to deduct were fulfilled and the taxable person is not in possession of any material justifying the suspicion that irregularities or fraud has been committed within that invoice issuer's sphere of activity.

The CJEU adopted the analogous position on the right to deduct on the basis of the so-called "dummy invoices" in the judgment of 31 January 2013 LVK – 642/11 Stroj trans EOOD versus Direktorna Direkcija "Obżałwane i uprawlenije na izpyłnenieto" – Warna pri Centrałno uprawlenije na Nacionałnata agencija za prichodite, case number C-642/11. This ruling emphasized that Article 203 of Council Directive 2006/112/EC of 28 November 2006 on the common system of value-added tax should be interpreted in the following manner:

- the value-added tax entered by a person on an invoice is payable regardless of whether a taxable transaction actually exists;
- it cannot be inferred from the fact that the tax authorities did not correct, in a tax adjustment notice addressed to the issuer of that invoice, the VAT declared by the latter, when those authorities have acknowledged that the invoice corresponded to an actual taxable transaction.

Furthermore, the CJEU expressed the opinion that principles of tax neutrality, proportionality and protection of justified expectations must be interpreted in a manner that does not preclude the recipient of an invoice from being refused the deduction of input VAT because there is no taxable transaction, even though the VAT declared by the latter was not adjusted in the tax adjustment notice addressed to the issuer of the invoice. However, if, in the light of fraud or irregularities committed by the issuer of the invoice or in earlier links of the chain of transaction relied upon as the basis for the right of deduction, the transaction is considered not to have been actually carried out, it must be established, on the basis of objective factors and without requiring checks of the recipient of the invoice which are not his responsibility, that the recipient knew or should have known that that transaction was connected with VAT fraud, a matter which is for the referring court to determine.[17]

The CJEU adopted the analogous position in the judgment of 31 January 2013 LVK – 56 EOOD versus Direktor na Direkcija "Obżałwane i uprawlenije na izpyłnenieto" – Warna pri Centrałno uprawlenije na Nacionałnata agencija za prichodite, case number C-643/11. This judgment provides that EU law must be interpreted as meaning that Articles 167 and 168(a) of Directive 2006/112 and the principles of tax neutrality, legal certainty and equal treatment do not preclude the recipient of an

[17] SIP LEX no. 1258555, www.eur-lex.europa.eu

invoice from being refused the right to deduct input value-added tax because there is no actual taxable transaction, even though the value-added tax declared by the latter was not adjusted in the tax adjustment notice addressed to the issuer of that invoice. However, if in the light of fraud or irregularities committed by the issuer of the invoice or in earlier links of the chain of transaction relied upon as the basis for the right of deduction, the transaction is considered not to have been actually carried out, it must be established, on the basis of objective factors and without requiring of the recipient checks of the invoice which are not his responsibility, that the recipient knew or should have known that that transaction was connected with value-added tax fraud, a matter which is for the referring court to determine.[18]

The discussed judgments considerably change previous case law regarding the value-added tax. They protect those taxable persons who have been victims of dishonest traders. However, should the CJEU's opinions be considered the exception to the rule, or the general rule, which must be followed by national courts and tax authorities? If the latter solution is adopted, there is the real risk that the efficiency of one of the most significant taxes considerably decreases.[19]

The impact of CJEU judgments in the area of abuse of law on the judgments of Polish courts

There can be no doubt as to whether the judgments of the CJEU regarding the abuse of law on value-added tax has influenced the judgments of Poland's Supreme Administrative Court and provincial administrative courts. This has had a significant impact on the decisions issued in cases concerning the so-called tax carousel fraud practices, and has contributed to tax fraud prevention. It needs to be stressed that the case-law doctrine of abuse of law established by the CJEU, even though not grounded in normative acts, has been adopted in the judgment-related practice of administrative courts in Poland. Of course, decisions issued in particular cases depend on the facts established by the tax administration authorities.

Firstly, the administrative courts in Poland have made attempts to describe and define a tax carousel. It should be emphasised that tax carousel frauds may take on different forms, and with time, fraudulent trading organisations become more and more elaborate. In the judgment of 28 February 2017, ref. no. I SA/Gd 1593/16 (published at CBOSA – Central Database of Administrative Court Decisions), the Provincial Administrative Court in Gdańsk argued that pursuant to the

18 SIP LEX no. 1341351, www.eur-lex.europa.eu

19 A. Mudrecki, *The Influence...*, p. 341.

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tax law, a "fictitious entity" is not only an entity that does not actually exist in trading but also an entity officially registered but merely maintaining an appearance of existence with the aim to commit a tax fraud. Proof of engagement of entities in a tax fraud defined as a "tax carousel scheme" involves circumstances such as: printed documents in circulation failing to prove actual transactions; inclusion of so-called "missing traders", who do not declare the due tax on goods and services in the issued VAT invoices, into the supply chain; instant transactions made via e-mail only, no trade agreements, no payment security (e.g. blank bills of exchange); no possibility of entities participating in the supply chain to utilise goods; reversed trading chain (supplies from "small" to "big" entities, i.e. from "missing traders" to taxable persons gaining real profit); no control over stored goods, no insurance of stored goods; no typical competitive market behaviour (e.g. aiming at shortening the supply chain); no problems with entering the market experienced by newly established entities (large turnover at the start of business operations), no application of deferred payment mechanisms, no stock of goods; short time of activity of "missing traders" (sudden discontinuation of business preceded by issuance of invoices in large quantities and for big amounts).

Another judgment, dated 9 January 2018, ref. no. I FSK 835/15, saw the SAC define the notion of a tax carousel using a definition established in tax law science. Although "carousel trading" is not a normative term, it does function as a definition of a transaction mechanism applied to gain undue advantages by taking advantage of the structure of the tax on goods and services. Engagement in such type of trading means engagement in tax abuse practices. The purpose of a tax carousel is to gain undue tax advantages. Such an engagement may take two forms: of defaulting on payment of a due tax as a delinquent taxable person ("missing trader") and/or of the unlawful deduction of input tax calculated by other entities included in a transaction chain, especially by an entity carrying out intra-Community supplies. A typical tax carousel is a multi-stage and organised scheme, with at least three entities involved in it, each performing a different role (the "missing trader", the "buffer", and the "broker"). An existing tax fraud does not mean that all participants have the same knowledge about the nature of the transactions (in particular, the entity acting as the buffer is usually an actual taxable person operating a real business and paying their taxes accordingly), the goods traded are only VAT carriers, and the transactions made in a carousel scheme have no business/economic purpose from the point of view of the entire trade.[20]

[20] W. Kotowski, *Karuzele podatkowe*, [in:] I. Ożóg (ed.), *Przestępstwa karuzelowe i inne oszustwa w VAT*, Warszawa 2017, pp. 23–24.

In the judgment of 12 December 2017, ref. no. I FSK 435/16, the SAC decided that the nature of the abuse of transactions may stem from the transactions in question themselves as well as from earlier and later transactions, which makes it necessary to trace and explain the entire chain.

In another judgment, dated 3 June 2016, ref. no. I FSK 1865/15, the SAC decided that if the taxable person knew or should have known that by purchasing goods they were taking part in a transaction involving a VAT fraud, they must be regarded, for the purposes of Directive 2006/112, as a participant in that fraud since by doing so they aid the perpetrators of the fraud, thus become their accomplices. In a situation in which such a fraud (i.e. where a taxable person does not act in good faith) is a tax carousel where the transactions made have no business purpose and are made only for VAT refund scam purposes, such a taxable person, by supplying goods purchased earlier from the previous link in the chain of entities involved in the carousel scheme to the next link in that chain, contributes knowingly to a tax fraud (i.e. acts as an accomplice in such an activity). In effect, such a "sale" is not made as part of a business activity, and so it may not be considered a supply within the meaning of Article 5, section 1, item 1 or 5 of the Act the Goods and Services Tax, i.e. an activity subject to taxation pursuant to this act. The occurrence of a situation described above in circumstances of the case in question justifies the "cancellation" – on the grounds of the settlement of the tax on goods and services – of both a purchase and a sale transaction (as made outside the scope of business activity). This means that purchasing goods in a carousel scheme does not result in the right to deduct tax calculated on the basis of invoices intended to document the purchase made, and the further resale of such goods should not be recorded as an activity producing certain effects on the grounds of the tax on goods and services, including as an intra-Community supply.[21]

In its judgment of 10 October 2017, ref. no. I FSK 97/16 (LEX no. 2388481), the SAC pointed to doubts regarding a contracting party, which implied the party's unreliability. It was decided that since the taxable person knew that Lithuanian entities often disappear from the VIES system, they should have known that such entities tended to be unreliable, which should have prompted the taxable person to apply special control measures and verify the transactions made with their contracting parties, especially since the situation involved one-off transactions.

In case with ref. no. I FSK 9/16, the SAC dealt with the right to deduct VAT and investigated the taxable person's exercise of due caution. The SAC decided that tax authorities were entitled to refuse a taxable person the right to deduct VAT if there were objective reasons that proved that the taxable person knew or should have

[21] See also: the SAC judgment of 14 April 2015, I FSK 46/14, CBOSA.

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known that the transaction intended to serve as the basis for deduction involved a fraud or abuse in the scope of VAT. The right to VAT deduction may be exercised if the following conditions are met: the material condition, meaning that goods have actually been supplied or services have actually been rendered, and the formal condition, meaning having an invoice that meets the formal conditions required for VAT deduction purposes. Even if the said conditions are met, a taxable person may be deprived of the right to tax deduction when it has been determined, on the basis of objective circumstances, that a supply (service) has been carried out for the taxable person who knew or should have known that by purchasing the goods (services) involved in the deal, they were taking part in a transaction made with the intention to commit a VAT fraud. Therefore, only in such circumstances is it necessary to investigate a taxable person's due caution (so-called good faith).[22]

The Supreme Administrative Court, in its judgment dated 25 July 2017, ref. no. I FSK 1798/15, decided that Article 86, section 1, Article 88, section 3, item 4, letter a. of the Act on the Goods and Services Tax should be interpreted as implying that a taxable person's sole adoption of procedures of verification of the contracting parties was not tantamount to acting in good faith and, in effect, did not translate into the right to deduct input tax on the basis of invoices that did not reflect the actual economic events if the said verification procedures were not followed with regard to a given contracting party.

Conclusion

The judicial decisions of the Court of Justice of the European Union play an important role in the harmonisation of value-added tax. These decisions form a case law that has produced two major jurisprudential doctrines, i.e. the doctrine of the abuse of law and the doctrine of good faith. The doctrine of the abuse of law makes it possible to counteract the negative phenomenon of tax carousel schemes.

The notion of the abuse of law is very broad, and a tax carousel is something that fits within the spectrum of acts classifiable as the abuse of law. It is especially impossible to decide that a tax fraud is not an instance of the abuse of law (tax abuse), although – quite importantly – an instance of the abuse of law will not always become a tax fraud; this limits the right of taxable persons to deduct VAT input tax. The abovementioned conclusion is substantiated in the introduction to the article, is in line with the normative concept included in Article 5, section 5 of the act of

[22] See: the judgment of 5 September 2017, ref. no. I FSK 9/16, LEX no. 2361505.

11 March 2004 on the Goods and Services Tax, and stems from judgments offered by administrative courts as covered in the article.

On the other hand, there is the doctrine of good faith, which is to protect taxable persons who have fallen victim to tax frauds, i.e. have exercised due caution.

The jurisprudential doctrines established by the CJEU and covered herein have a significant impact on the practice of tax authorities, and are taken into consideration in the decisions issued by administrative courts in Poland.

Cases related to tax carousel schemes differ greatly. The mechanisms of tax carousel frauds take on different forms as well. Also, tax carousel cases are extensive and complex in terms of evidence collection and analysis. When deciding in such cases, administrative courts first investigate whether a tax carousel phenomenon has actually occurred. On the other hand, they check whether the tax authorities have determined, as part of the handled tax proceedings, if the taxable person has exercised due caution in economic trading.

The Supreme Administrative Court's decisions issued in this area are quite diversified and dependent on the circumstances of each given case. It is also necessary to bear in mind that it is the national court that makes the final decision in settling any disputable matters.

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