DRR through the transmission of electronic invoices

The Italian experience

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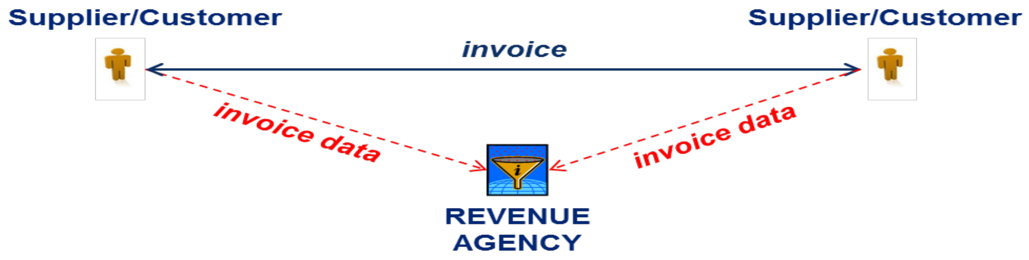
DRR obligation in Italy: a long and complex experience



Italy has a consolidated experience (**17 years**) in tax data reporting processes:

- in **2006,** a law was introduced which obliged all resident VAT operators to transmit, **on an annual basis**, a **digital report containing the aggregate tax data of invoices issued and received** (customer/supplier lists) to the Italian Revenue Agency;
- in **2010,** the law was amended and VAT operators were obliged to transmit, **on a quarterly basis**, a **digital report containing the tax data of each individual invoice issued and received** (regarding domestic and non-domestic operations).

These processes have certainly strengthened the risk analysis activities of the Revenue Agency, **improving its ability to identify cases of fraud and evasion**. However, these processes highlighted **many critical issues**.

- The preparation of the report file (even in the case of electronic generation of the invoice) was always **considered by VAT operators as an additional obligation**, **burdensome in terms of time and money.** This was because, after generating and sending (including electronically) an invoice, they would still have to generate and transmit the data report (incurring in the cost of the software that extracts the data from the invoice file, generates the report file and sends this file to the Tax Administration). The burden of the digital report was even **higher for purchase invoices, because the customer could not force the supplier to send a structured electronic invoice in a format (semantic and syntactic) that could be processed automatically**.
- Due to the frequency of the reporting (first annual and then quarterly), the Revenue Agency could **only cross-check the report data of the supplier and the customer several months after the invoice was issued**. VAT operators strongly complained about changing the transmission frequency from annual to quarterly and it **was politically impossible to increase such frequency**. Furthermore, even by increasing the frequency **there was always a time misalignment between digital reports containing active operations and those containing passive operations: the customer could only generate the report on the purchases after receiving the invoice and the Tax Administration had no way of knowing the time of receipt**.
- Due to **formal errors in the generation of the digital report** (especially for purchase operations), very often the **controls carried out by the Revenue Agency led to incorrect checks and costly disputes**. Due to both the frequency of report transmission and the formal errors made, **the Agency was unable to use the data to offer its services for the pre-filling of VAT returns**.

All these critical issues have triggered a strong **social conflict between the Tax Administration and VAT operators.**

A new strategy: DRR through e-invoicing

There were 2 options to solve the problems related to invoice data reporting: 1) eliminate the obligation and give up the controls; 2) **change the method of acquiring invoice data, making it easier for VAT operators and eliminating the risk of errors**.

In **2014, Italy introduced the obligation to transmit electronic invoices (in a structured format) to the Public Administration through a centralized system managed by the Revenue Agency.** The supplier, after generating the invoice file - complying with an XML standard (semantic and syntax) - sends this file to the Exchange System (**SdI**) managed by the Revenue Agency; SdI, after checking that the file contains the mandatory fiscal data of the invoice (under **Article 226 of the VAT Directive**), delivers the file to the Public Administration and, **at the same time, retains the fiscal data of the invoice** for the purpose of monitoring public expenditure.

At the same time, Italy was involved in the **Multi-Stakeholders Forum on e-Invoicing**, coordinated by the Commission's DG Grow, to **implement national actions aimed at spreading the use of electronic invoicing** (one of the goals of the European Digital Agenda 2020).

We therefore understood that we could *kill two birds with one stone*: **acquire invoice data through the obligation to transmit and receive electronic invoices via SdI**. After the derogation was authorised by the Council, in **2018** we introduced the law which makes it **mandatory to send and receive electronic invoices via SdI for all B2G, B2B and B2C transactions**.

With this reform, not only we have **completely solved the problems** we had with the previous invoice data reporting method, but **also a number of further positive effects** have ensued from it. Operators **only have the obligation to generate the invoice electronically**, in a standard format, **send it and receive it through the SdI**, while, **during this process, the Revenue Agency automatically acquires the fiscal data of the invoice**. Therefore, operators **no longer have the burden of extracting the data, and of generating and transmitting the data reporting file for both active and passive operations** - sending and receiving the e-invoice file through the SdI is the only obligation that stands for VAT operators. With this e-invoicing process, the **Revenue Agency can be sure that the reporting data (extracted from the invoices) are exactly the same as those shown in the invoice.** Moreover, **invoice data are acquired in real time** and thus **the Agency's ability to prevent VAT fraud has increased dramatically. The Agency was also able to develop value-added services for VAT operators such as the pre-filling of VAT returns**.

Effects of DRR through e-invoicing

- ✓ **Public expenditure tracking**
- ✓ **Gathering original invoicing data** gives certainty to suppliers, their counterparts and the Italian Revenue Agency
- ✓ **More effective and timely controls to curb fraud and counter tax evasion before VAT returns are submitted**
- ✓ **Reduction of controls after return submission**
- ✓ **Administrative burden reduction:** fiscal and accountancy obligations are easier
- ✓ **Information necessary for periodic settlements** will be provided by the Italian Revenue Agency
- ✓ **Pre-filled periodical VAT return**
- ✓ **Easier procedure for VAT refunds**
- ✓ **Enhanced collaboration and cooperation** between the Italian Revenue Agency and taxpayers
- ✓ Use of invoice data for **statistical and public policy purposes**

- ✓ **Tax Gap**
- ✓ **Tax compliance**
- ✓ **Administrative and Judicial disputes**
- ✓ **Collaboration**
- ✓ **Digitalization**
- ✓ **Simplification**
- ✓ **Growth of national economic system**

Effects on VAT and direct taxes

Esteem in Budget Law for 2019: € 1.97 Billions

Verified ex post for 2019: € 4.206 Billions

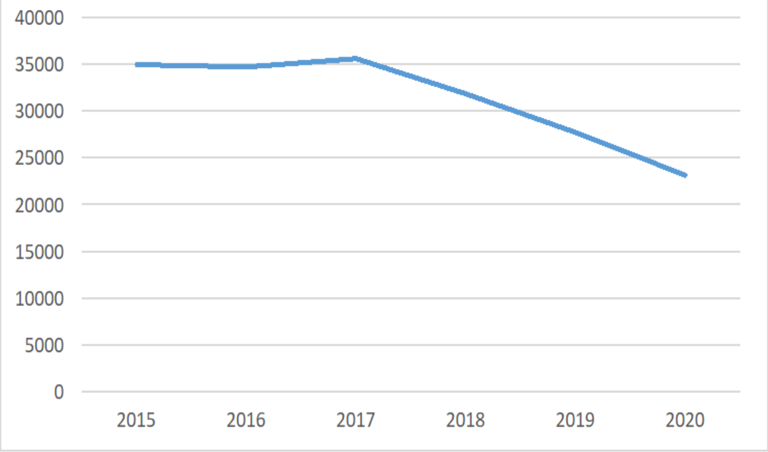
VAT FRAUD PREVENTION

In the first year of application (**2019**), the Revenue Agency identified and **blocked frauds for false VAT credits for almost € 1 billion.**

In **2022** the Revenue Agency identified and **blocked frauds for false VAT credits for almost € 9 billions.**

General ITALIAN VAT TAX GAP TREND

Data provided by Ministry of Economy and Finance



DRR through e-invoicing: Key elements of success

The **efficiency and effectiveness of the process** currently in use in Italy depend on **2 key factors**:

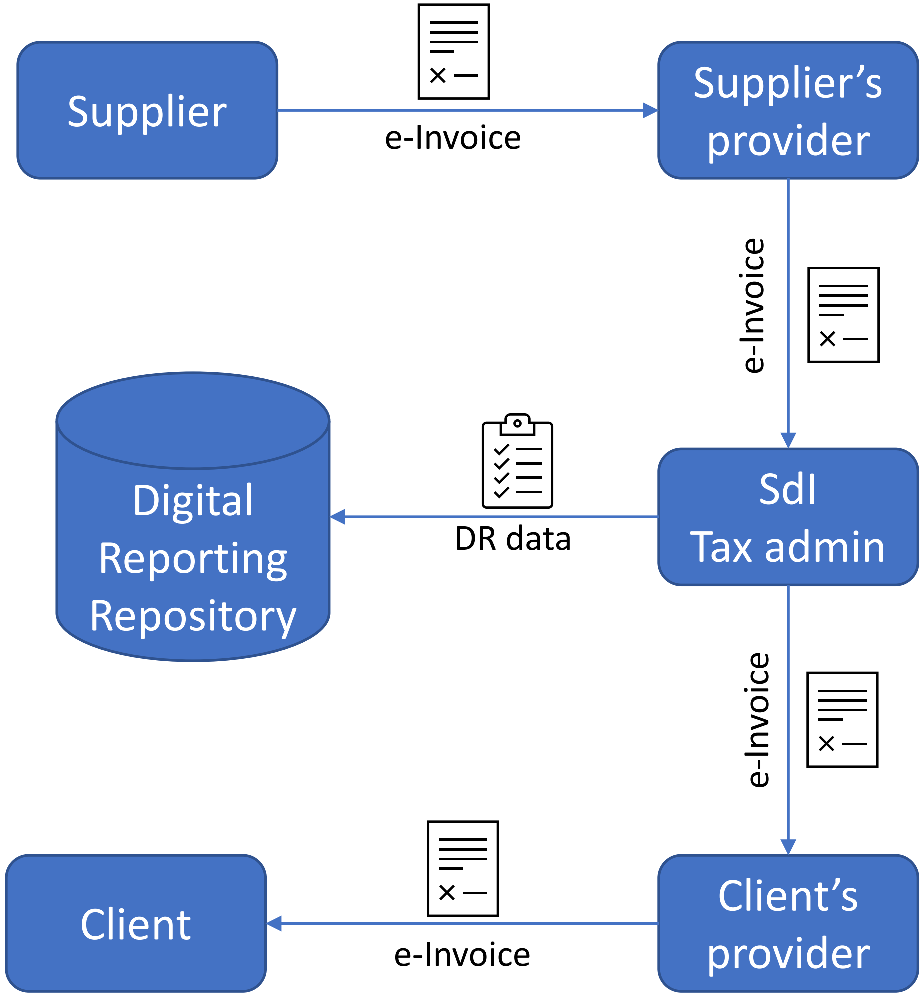
1) **Mandatory e-invoicing for VAT operations carried out among operators that are resident/established for VAT purposes**

2) **All e-invoices exchanged among resident/established operators must be sent to the SdI**, that delivers them to the recipient/customer.

As a consequence, any invoice (either in electronic or paper format) that is exchanged between the supplier and the customer by means other than the SdI, **is not a valid invoice for tax purposes and cannot be used by the customer to deduct VAT**.

Formal controls operated by SdI:

- SdI checks that the fiscal data elements indicated as mandatory by Article 226 of the VAT Directive are present in the invoice
- These controls only aim at making sure that the document is a **formally valid invoice** (compliant with the VAT Directive) and are **exactly the same controls that a reporting system should perform in order to ensure the reliability of the data being input**
- The list of controls is publicly available so that a service provider can be sure that an invoice will not be rejected.



DRR through e-invoicing:
What if the Italian e-invoicing process is made optional?

(for VAT operations carried out among operators that are resident/established for VAT purposes)

If the Italian e-invoicing process were made optional, a reporting system would need to be reintroduced in order to obtain the reporting information from the invoices that are not sent to SdI (additional cost on the public side). The system would work as follows:

- Whenever a VAT operator decides to send an e-invoice to a platform other than the SdI, this generates a **reporting obligation for the supplier and for the customer** (additional cost on the supplier/customer side).
- Whenever a customer receives an e-invoice, he should check where the e-invoice comes from: in case it does not come from SdI, the customer must send a reporting message for that invoice. An alternative to avoid this check is to send a reporting message for all the e-invoices received (additional cost on the customer side, regardless of the alternative chosen).
- Whenever a reporting message is generated and sent to the reporting system, **an error might occur**, whether intentional or unintentional (**potential quality issue for the reporting database**).
- Whenever an e-invoice is not sent to SdI, the reporting system will have to cross-check the two reporting messages (additional cost on the public side, and on the supplier/customer side in case the two messages do not match).

DRR through e-invoicing:
What if the Italian e-invoicing process is made optional?

(for VAT operations carried out among operators that are resident/established for VAT purposes) (Cont'd)

- In order to ensure compliance with the reporting requirements, **sanctions might have to be (re)introduced in case the reporting message does not match the invoice or is not sent at all**. With the current process there is no need for sanctions, because if the invoice is not sent to SdI, the customer cannot deduct the VAT (risk of new sanctions for supplier/customer).

- **There would be a loss of revenue**, in particular of VAT.

- Reporting messages are supposed to be sent within a few days, and this delay might **reduce the ability of blocking frauds** timely (potential increase in VAT TAX GAP and **consequent loss of VAT for the EU**).

- The Revenue Agency's ability to provide VAT operators with a service for making **pre-filled VAT returns available might be undermined.**

- It would be **very hard to explain to VAT operators that an EU Directive forces Italy to reintroduce a reporting system** that Italian VAT operators have always complained about, and that Italy has managed to get rid of by integrating the reporting requirements in the e-invoicing process - a decision supported by the Italian Forum on e-Invoicing, with the agreement of the vast majority of VAT operators.

DRR and e-Invoicing in the ViDA proposal

Considerations and implications

- **Digital Reporting and e-Invoicing can be considered as separate but interconnected processes**, because the data managed are partly the same. This point of view can be particularly useful when setting up a DR process in a framework where several e-Invoicing processes are already implemented and in use.
- The information managed by a DR process is a subset of the information that an e-Invoice can manage, **namely the fiscal part of the invoice (VAT Directive, Article 226).**
- In this context, the **ViDA proposal**, aimed at harmonizing the DR process, will **provide rules that define**:
  - The **set of mandatory data elements to be transmitted to the DR system** with each message
  - The **format of the message to be transmitted**
  - The **deadline for the transmission of each DR message.**
- The **ViDA proposal does not specify any rules at transmission level**, leaving this issue to Member States.
- However, **where the ViDA proposal modifies Article 218 of the VAT Directive**, by establishing rules on how the e-Invoice should (and should not) be transmitted between supplier and customer, **it is addressing directly the e-Invoicing process, not the DR process**. The reason for such a provision is harmonization.

DRR and e-Invoicing in the ViDA proposal

Considerations and implications (Cont'd)

- It can be easily verified that the e-Invoicing processes that many Member States have implemented, or are about to implement, for their domestic invoicing, are all country-specific. Of course, the **European Core Invoice is, or is going to be, the common language to be supported by all MSs.**

- It would appear that no harmonization is required for domestic e-Invoicing frameworks, nor does the ViDA proposal address this issue, except for the provision allowing for a routing of the e-Invoices that bypasses the governmental platform.

Conclusions:

- **Domestic e-Invoicing processes are all country-specific, but the European Core Invoice EN 16931 will have to be accepted everywhere in the EU.**

- Digital Reporting processes are, and will be, country-specific, but **the DR message that will be defined** following the provisions of the ViDA proposal, **as a subset of the European Core Invoice EN 16931, will have to be accepted everywhere in the EU.**

- **Harmonization is still at document level.**

- Is there actually any need to lay down provisions that make way for an e-Invoicing process that bypasses the governmental platform, even for domestic invoicing? **Why**?
  - ✓ **For the sake of privacy**? **No**, the governmental platform carries out **formal checks and acquires only the tax data set.** The **Italian and EU supervisory authorities have clarified that there are no privacy issues.**
  - ✓ **For business problems** (e.g., late payments)? **No**, instead the Italian experience has shown that **companies gain benefits from the centralized system** because the **government platform guarantees the existence, fiscal correctness and the timing of issue and receipt of the invoice.**

Case study: EDI and SdI

- The Core Invoice defined by EN 16931 was specifically designed to support fiscal data elements, **and other data elements that are commonly shown in most invoices**, including references to other documents in the purchase cycle such as order or contract, and explicitly **excluding sector-specific or Country-specific data elements - **this is also the reason for the name '**Core Invoice**'. In order to be suitable for **B2B**, EN 16931 provides **guidelines for developing extensions to support sector-specific data elements.**

- The Italian e-Invoicing format, an XML called FatturaPA, was developed under similar specifications, and for this reason the FatturaPA XML can carry a binary attachment.

- Widely used e-Invoicing standards, such as UBL and CII - to mention the syntaxes allowed by EN 16931 - provide hundreds of data elements, in order to support most business sectors, and **EDI provides a specific 'dialect' for each sector it supports.**

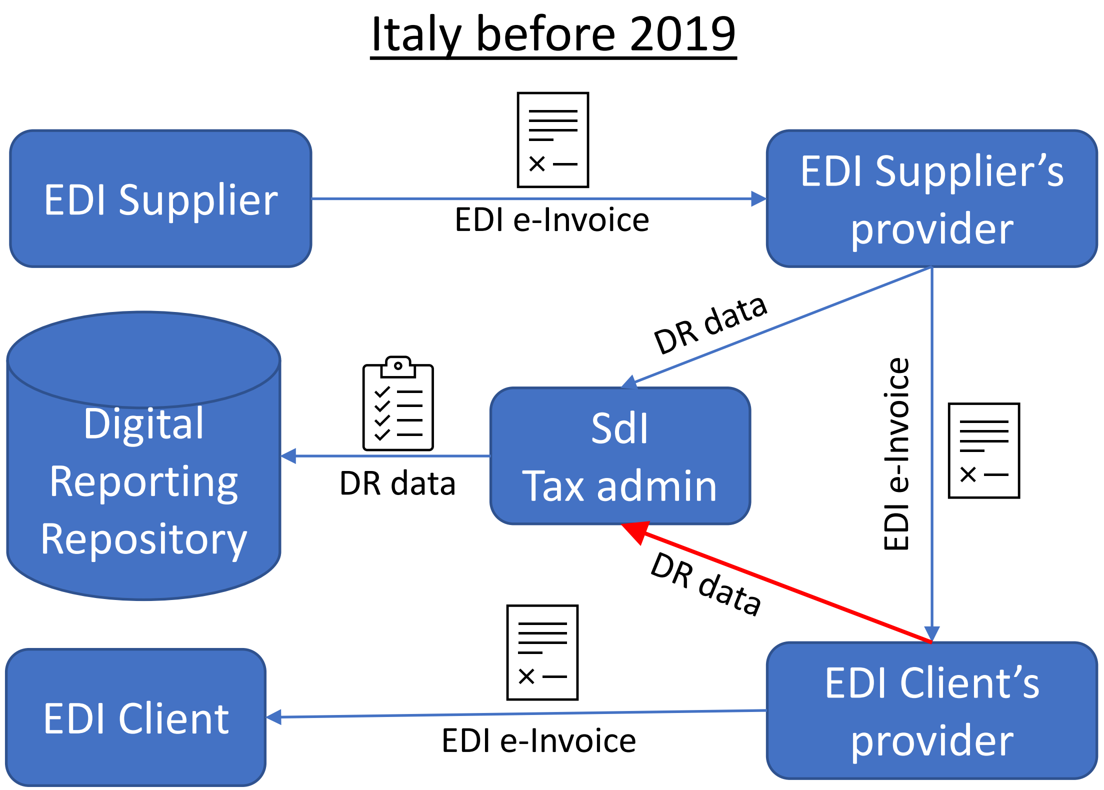
- The EDI e-Invoicing process is integrated with other processes that support the whole purchase cycle. This is one of the reasons why an **EDI e-Invoice usually contains far more information than a DR message.**

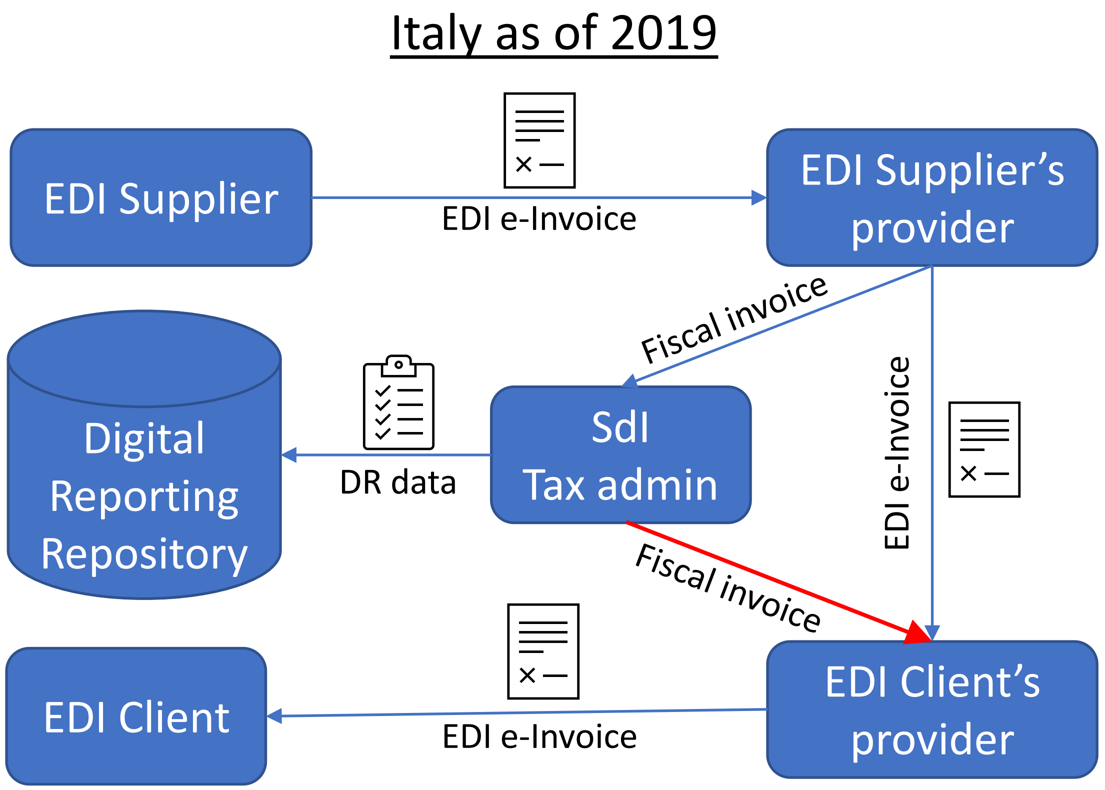
- When Italy was designing the process for the mandatory e-Invoice, the EDI companies expressed concern that e-Invoicing through SdI (the tax administration platform) could affect their well-established EDI processes.

- One of the most critical points was that **EDI is actually in real-time, while SdI generates an average delay of 2-4 hours.**

- The **topic was discussed within the Italian Forum on e-Invoicing**, and it **turned out that the e-Invoicing process through SdI would have not affected the EDI working cycle, on the condition that a reconciliation check be added to the EDI process**, as shown in the diagram below.

Case study: EDI and SdI





- The **only difference that can be found is that before 2019 the client's provider had to send the reporting message to the SdI, while since 2019 it has to verify that the fiscal invoice was correctly received from SdI.**
- Since 2019, the EDI e-Invoice does no longer constitute the fiscal invoice, but **the document and the process are the same**;
- The **DR data in the left diagram and the Fiscal invoice in the right diagram have different meanings**, because **the former is a reporting message** and **the latter is the fiscal invoice. Nevertheless, they deliver the same information, and can actually be embodied by the same document**.