

Financial Law Review

No. 16 (4)/2019
quarterly

UNIVERSITY OF GDAŃSK • MASARYK UNIVERSITY • PAVEL JOZEF ŠAFÁRIK UNIVERSITY • UNIVERSITY OF VORONEZH
<http://www.ejournals.eu/FLR>

PREVENTION OF THE LOSS OF VAT REVENUES – AN ATTEMPT AT EVALUATION OF NEW LEGAL INSTRUMENTS

JADWIGA GLUMIŃSKA-PAWLIC *

Abstract

The article discusses new regulations implemented in Poland with a view to increasing budgetary VAT revenues through sealing the system, and in particular through reducing tax fraud. The Author's main objective is an analysis of the various available instruments and their evaluation from the perspective of improvement of the effectiveness of tax collection, but also from the perspective of protection of taxpayers' rights, for the actions of the fiscal apparatus cannot be overly burdensome on entrepreneurs as they hinder their development. The article, which utilises the comparative and statistical method, features an analysis of legislation.

Key words: budget, revenues, VAT, instruments

JEL Classification: H21, H25

* Professor of Financial Law, Department of Financial Law, Faculty of Law, University of Silesia, Poland. The Author specializes in tax law and local government finance. She has authored and co-authored 6 books and more than 180 reviewed articles in prestigious journals. She is a member of the Information and Organization Centre for the Research on the Public Finances and Tax Law in the Countries of Central and Eastern Europe. Contact email: jadwiga.gluminska-pawlic@us.edu.pl; ORCID: 0000-0002-2256-4558.

1. Introduction

The functioning of each state requires that its authorities have the necessary financial resources, making it possible to cover public expenditure. Hence, the state collects revenues to carry out tasks (expenditure) regarded as essential, necessary, needed or recommended. The primary sources of budgetary revenues are taxes, which in 2017 covered 84% of state budget expenditure in Poland. Considering that VAT revenues that year accounted for 49.7% of fiscal revenues of the state budget, the importance of this tax cannot be overstated. What follows is that the loss of VAT revenues is a major problem not just in Poland, but also in other European Union member states. According to data published at <https://ec.europa.eu>, France and Germany, both of which are near the EU average, incur losses more than twice as high as those of Poland, whose losses are estimated at 25% of projected proceeds (33-55 billion PLN). The so-called "VAT gap", whose existence is a fact, constitutes a major weakening of, or even a threat to, the development of the economy of the entire European Union. Therefore, the legislative and executive authorities are looking for optimal legal solutions and effective application of those.

During the period between November 2015 and September 2018, Poland introduced 28 changes regarding the VAT. Of those, 22 led (directly or indirectly) to an increase in budgetary revenues linked to VAT, and 21 served to "seal" the system. The changes were necessary, as the years 2013-2015 abounded with VAT fraud. This was also the period when the use of fake invoices escalated, fraudsters created various structures to feign intra-Community supplies, and the effectiveness of tax authorities in fighting VAT fraud was insufficient.

The new legal instruments intended to prevent the loss of VAT revenues include the reverse charge mechanism, Standard Audit File for Tax (PL Jednolity Plik Kontrolny; JPK), IT System of the Clearing House (PL System Teleinformatyczny Izby Rozliczeniowej, STIR), VAT penalty rates, Fuel Package and Energy Package (PL Pakiet paliwowy and Pakiet energetyczny, respectively), split payment mechanism, increased sanctions for VAT fraud in the penal code, and consolidation of revenue and customs authorities.

2. Reverse charge mechanism

The reverse charge mechanism has been in use for several years to monitor the trade in selected goods (e.g. steel rods, coffee, tea, and electronics) in those segments of the market with anomalies, in particular fraudulent behaviours, including ones involving invoices that did not reflect actual transactions. Starting from 2017, Poland decided to apply this

mechanism also to some services, namely renovation and building works. This resulted in major difficulties, or even chaos, in identification of services with respect to which reverse charge was to be applied. Whereas identification of goods based on nomenclature used in statistical classifications does not raise difficulties, under market economy conditions the experiment involving services, and such sensitive ones at that, can hardly be considered successful.

While it is true that goods covered by this mechanism cannot be used for fraud based on "empty" invoices, this cannot be said of other areas, which are easily affected. This in turn means that revenues from hitherto taxable market segments decrease, as given the absence of an output tax burden with a simultaneous right to an input tax deduction (equivalent of the 0% rate), bogus supplies covered by this mechanism make it possible to create a surplus of input tax over output tax and enable a VAT return fraud without having to recourse to feign an intra-Community supply of goods. What follows is that revenues only accrue to the state budget if goods are later sold to end consumers, whereas many of the goods covered by this mechanism are not available in retail (e.g. steel or copper), and trade in these goods is largely bogus. As a result, such transactions never translate into a value added with a real tax burden, and the goods merely serve as a carrier for fraudulent deductions and "disappear" in the same way that "vanishing traders" do. Furthermore, similar goods are also sold under pretence of goods covered by the reverse charge mechanism. This applies in particular to goods whose identity cannot be ascertained, especially post-use (e.g. steel as scrap metal). What that means is that a segment of the market that is subject to normal VAT arrangements becomes excluded from taxation, and taxpayers who actually trade in goods covered by reverse charge purchase them from abroad at net prices or from suppliers exempt from VAT to avoid the need to recover input tax through a tax return from the inland revenue (prolonged time and risk of control). As a result, the greater the scope of reverse charge, the lower the demand for goods and services subject to taxation under normal arrangements on the domestic market. This mechanism also makes it possible for entities misrepresenting their identity to obtain goods or services at net prices under false pretences. Whenever this is the case, tax authorities first demand the output tax from the entity whose data was used, and only later – from the seller who, through his lack of due diligence, let this situation happen.

No reliable statistics showed an increase in budgetary revenues that would be linked to this mechanism. In fact, the opposite is the case – data point to an increase in the number of tax declarations showing a return of VAT and the amounts of those reimbursements (that is an effective revenue shortfall in the state budget), as well as an increase in the trading volumes of goods and services covered by this mechanism for which there is no real need (that is bogus trading intended to create VAT returns). Hence, the reverse charge turns out to be a

mechanism that is not only ineffective, but also makes it difficult to heal the VAT system [Radzikowski 2018: 178-179].

3. Standard Audit File for Tax (SAF-T)

The Standard Audit File for Tax (SAF-T) was introduced by Article 193a of the Tax Ordinance Act, and has been applicable to some entities since 1 July 2016. The introduction of the SAF-T enables taxpayers to submit information to tax authorities in electronic form, which makes it less time-consuming and troublesome, and which as a result helps to reduce costs and contributes to improving the effectiveness of irregularities and tax fraud. Tax authorities receive current data that they can analyse and use for control purposes. The SAF-T involves electronic exchange of two types of data: 1) automatically – monthly purchases and sales records, which is sent by 25 day of next month (JPK_VAT) and 2) upon request – ledgers (JPK_KR), bank statements (JPK_WB), inventory turnover (JPK_MAG), invoices (JPK_FA), revenue and expense ledger (JPK_PKPIR), and revenue register (JPK_EWP). The SAF-Ts support the obligation to keep electronic records and submit tax declarations (in the course of time, the SAF-T is intended to take over the role of tax declarations), and considerably reduce quarterly reports. The procedure can be compared to verification activities carried out distantly on an ongoing basis. The obligation to report using the SAF-T, introduced gradually, starting from the largest taxpayers and then smaller ones, yields results that are desirable from the point of view of the budget.

The computerisation of VAT accounting brings along a number of hopes, but also fears related to costs and inconvenience of the system. While it is beyond any doubt that the SAF-T fosters and speeds up access to information needed to reconstruct various supply chains, one should not disregard the system's limitations, for the information in question is not exchanged on an ongoing basis, and is instead submitted within deadlines similar to those applicable to tax declarations. There are also concerns that the SAF-T will only help to diagnose formal errors (e.g. wrong Taxpayer Identification Number) and not actual fraud. Furthermore, the SAF-T does not envisage any measures that could help prevent fraud; also, information is not automatically transferred between tax authorities, law enforcement authorities and other institutions (e.g. the Social Insurance Institution (ZUS) as regards payment of social insurance contributions of employees reportedly carrying out said economic transactions). All these factors mean that the SAF-T on its own is not effective in fighting VAT fraud and should instead be perceived as an auxiliary instrument to the IT System of the Clearing House (STIR).

4. IT System of the Clearing House (STIR)

The STIR System was introduced by special Act Amending Certain Acts to Combat the Use of the Financial Sector to Commit Treasury Fraud. The System provides the Head of the National Revenue Administration (NRA) with daily information on qualified entities' accounts run by banks and credit unions and on transactions at these accounts to analyse the risk of treasury fraud. Data concerning transactions by natural persons who are not qualified entities, resulting in a credit or debit on the accounts of qualified entities, are transmitted as aggregated data, which means the Head of the NRA does not receive the details of individual transactions, except for individual cases where such details may be provided upon a reasoned request. The underlying premise and objective is to make use of the IT system's capacity for the earliest possible identification of fraudulent behaviours or fraud-related risks. Until recently, tax administration has been criticised for being so late in the measures it undertakes that the fiscal and penal-fiscal consequences are borne not by those in charge of criminal groups or the initiators of fraud mechanisms, but by those taxpayers who, as a general rule, are legitimate traders whose role in criminal dealings was minor and who do not take deliberate fraudulent action.

In other words, the STIR System targets a crucial point in a fraudsters' activity: it deprives them of control over financial resources before a VAT fraud is conducted. It therefore seems that it is the most important and most effective mechanism for sealing the system. However, freezing of funds should be used with caution, as it may result in a "business death" of a random entity caused by a loss of financial liquidity and shattered reputation among its business partners. Hence, the STIR System has raised fears and concerns (also due to the risk of data leakage) despite assurances to the effect that honest entrepreneurs have nothing to fear.

5. VAT penalty rates

The Act changing the act on VAT and some other acts introduced, starting from 1 January 2017, VAT penalty rates, which at 20, 30, and 100% are intended to prevent and discourage under-declaration of output tax and over-declaration of input tax and tax returns. The 30% penalty rate may also be imposed for failing to submit a tax declaration or failing to pay the output tax. The 20% penalty rate is applicable to entities that amend their VAT tax returns or submit an overdue tax declaration and simultaneously pay the output tax. It is intended to encourage taxpayers to self-correct their declarations following a tax audit or an investigation procedure. The 100% penalty rate is applicable in case when an excessive amount of input tax declared by a taxpayer will stem from invoices: issues by a non-existent entity, stating activities that did not take place, stating amounts devoid of reality – in the part concerning those invoice items stating amounts devoid of reality, stating

activities to which provisions of Article 58 and Article 83 of the Civil Code apply (e.g. ostensible acts, designed to circumvent the law). The increased rate applies to this part of amount that covers excessive amounts of input tax resulting from those invoices. The adopted solutions prove how firmly the authorities stand against taxpayers knowingly participating in tax fraud and obtaining illegitimate financial gains at a cost to the state's budget.

The sanctions referred to above are not applied in the following cases: 1) correction of a declaration, subject to payment of the tax and accrued interest (prior to a tax audit/fiscal audit), 2) obvious errors, 3) errors as to the period for which the output or input tax were declared, as well as – in the aftermath of the Constitutional Tribunal judgment of 28 April 1998 (case file K-17/97) – towards natural persons who are subject to penal fiscal liability for committing this act. Where the sanctions are applied, increased default interest is not applicable.

These sanctions are designed to encourage taxpayers to do their tax returns correctly and ensure that irregularities are far more "costly" than any source of financing. That said, they are not used to combat tax fraud, as they concern entities that actually carry out economic activity and not so-called "vanishing" fraudsters and "strawpersons".

6. Fuel Package and Energy Package

The Act changing the act on VAT and some other acts and the Act changing the Energy Law and some other acts introduced solutions establishing a special method for accounting of VAT on intra-community acquisition of selected motor fuels, commonly referred to as the Fuel Package and Energy Package. The most important outcome of these changes was restricting the entry of fuel-carrying tanker trucks into Poland through the EU's internal borders. In 2015, the number of those trucks totalled approximately 750 per day, whereas in August 2016, it was merely 150 [PwC report "Countering shadow economy. Impact of regulations on liquid fuel industry", drawn up for the Global Compact Network Poland and Polish Oil Industry and Trade Organisation]. What follows is that the consumption of legally imported petrol and diesel fuels increased.

The effectiveness of the adopted solutions in countering shadow economy in liquid fuel trading has been confirmed by results of a statistical analysis comparing the period from the entry of the fuel package into force until November 2017 and a corresponding period before the entry of the package. The analysis has shown that the value of intra-community supplies (ICS) of diesel fuel to Poland declared by other EU member states has decreased by approx. 40% (from EUR 2.27 billion to EUR 1.36 billion). Analysis of differences in reporting between EU member states and Poland has revealed discrepancies between what

allegedly entered Poland and what actually entered it at approx. EUR 5 billion (during the period between 01.2013–07.2016). In 2017, when the fuel package was in force during all reporting periods, the reporting differences plummeted, accompanied by an increase in the intra-community acquisition, especially of diesel fuel, which means that there has been a considerable decline in the quantity of oil coming from illegitimate sources in Poland. Hence, the fuel package has proved to be a straightaway success in countering shadow economy in the fuel sector: it has led to an increase in domestic sales of legitimate goods, and a decrease in imports from the EU member states (see annual reports by the Polish Oil Industry and Trade Organisation (POPiHN) for the years 2016 and 2017). That said, the package is not free from flaws – its design fault is not adjusting the VAT and excise duty systems, which results in interpretive doubts and possible abuse of the system [Rutkowski 2018: 203-205], whereas an obvious negative consequence is the high cost of running of the package, which affects in particular dealers not affiliated with the market's major players, although this is where the majority of irregularities occurred.

As a result of the changes, the number of detected irregularities (losses in VAT revenue) has gone up significantly, which also translates into a higher number of cancelled rights to purchase excise goods as a registered recipient and a higher number of withdrawn authorisations to operate a tax warehouse.

7. Split payment mechanism

The split payment mechanism was introduced in Poland by the Act changing the act on VAT and some other acts. At that time, the solution was already in use in the Czech Republic, Romania, and Italy, and outside the EU – in Turkey. However, in other countries it is rather limited and used on a selective basis, with respect to certain activities. One example may be the Netherlands, where split payment is only used by temporary work agencies for employee secondment services. In Romania, the scope and terms of application are similar to those used in Poland. In addition to that, Romania also uses the split payment mechanism in conjunction with additional incentives in the form of income tax reliefs. The mechanism can be used by purchasers who received an invoice stating an amount of tax declared, which means it is reserved for transactions of the taxpayer – taxpayer type and can only be used where the payment is in the form of a transfer of money. As a general rule, at least initially, split payment is optional, but its application entails certain consequences for both the seller and purchaser. While the seller receives total payment for his goods or services (gross amount, including the tax), but the payment is remitted to two separate bank accounts, with the seller having restricted access to the one where the VAT is deposited.

The optional character of the application of the split payment mechanism is highly relative, as it is the purchaser's sovereign decision whether he will pay the entire amount due to the primary account or whether he will have the bank transfer the VAT to the linked VAT account that he does not need to know. All the purchaser has to do is to include a specific instruction in the transfer message. In practice, while the seller, whom the purchaser wishes to pay using the split payment, does receive the entire amount, the bank automatically transfers the VAT amount to a separate account, which in the seller's account's transaction history is shown as a separate transfer. The split payment mechanism negates any joint liability of the purchaser for the seller's obligations regarding the goods specified in annex no. 13 to the Act, commonly known as sensitive goods. With respect to defaults occurring in relation to payments of at least 95% made using this mechanism, the default interest rate referred to in Article 56b of the Tax Ordinance Act does not apply. These incentives do not apply in the case of so-called "empty invoices" or invoices issued by a nonexistent entity.

Nevertheless, the split payment mechanism is yet another deviation from the actual aim and VAT accounting technique presumably envisioned by the authors of this most important and most popular indirect tax.

8. Increased sanctions for VAT fraud in the penal code

The amendment to the penal code introduced into chapter XXXIV of the penal code special types of document fraud: Article 270a (material forgery) and Article 271a (intellectual forgery), which penalise both the act of forging (issuance) and use of a forged invoice [Radzikowski 2017 : 5-7]. The amendment provided for drastically harsher penalties, and for offences under Article 277a § 1, it went so far as to call for a penalty of deprivation of liberty for 25 years. The new provisions did not preclude the application of provisions – also harsher – laid down in Article 17 of the penal fiscal code, which added the penalty of deprivation of liberty, excluding the possibility of voluntary submission to penalty under Article 17 of the penal fiscal code. Both amendments concern only offences against documents (invoices), and do not interfere with current penalisation of fraud or decrease of public liabilities. Nevertheless, both are characterised by a high degree of severity and far-reaching uncompromisingness of the adopted solutions, which are intended to counteract VAT fraud, especially by organised crime groups, putting the state's budget at risk of multibillion losses. Offences covered by these amendments are subject to a penalty of many years' imprisonment, with the exact punishment depending on the value of empty invoices, and the deprivation of liberty may also be accompanied by a fine.

Another amendment to the penal code, effective since 27 April 2017, introduced the so-called extended confiscation, legitimising e.g. the forfeiture of an enterprise that was the

instrument of an offence, as well as forfeiture of assets handed over to third parties free of charge or below their market value, forfeiture of assets despite the failure to issue a sentence (e.g. due to the death of the perpetrator, his flight, or mental illness), and other solutions. What strikes is the severity of the regulations referred to above, which have been constructed in such a way that the perpetrator must prove that the assets he has collected comes from legitimate sources.

It is beyond any doubt that strengthening penal sanctions has a preventive effect. Nevertheless, it is difficult to sentence organisers and beneficiaries of VAT fraud; instead, the penalties are usually imposed on the "strawpersons". The new regulations will further deepen the existing tendency: draconian punishments are applicable to invoice crimes, which are easier to prove, and not to the actual state property fraud. It is both surprising and disappointing that preparatory acts (the invoice forgery itself does not yield profits) are subject to more severe penalties than the "main" offence to the detriment of the state. There is also the risk that "ordinary" taxpayers, using false invoices under conditions of the so-called *dolus eventualis* (Article 9 §1 in fine of the penal code) may be sentenced.

9. Consolidation of revenue and customs authorities

The Acts on National Revenue Administration and Provisions introducing the Act on National Revenue Administration reorganised revenue and customs authorities in order to improve their effectiveness, especially in enforcing public liabilities. On 1 March 2017, the existing customs authorities, fiscal administration, and revenue authorities, became consolidated and transformed into the National Revenue Administration, which is a specialised government administration engaged primarily in tasks related to obtaining revenues from taxes, duties, fees, and non-tax budget receivables. At this stage, it is not clear, however, whether the consolidation did guarantee a new quality in terms of coordination of measures, as it involved existing structures, and one of the deputy ministers for finance became both the Head of the National Revenue Administration, General Inspector of Fiscal Control, and an authority in charge of tax offices, customs and revenue offices, and chambers of fiscal administration as the Head of the National Revenue Administration. He was also assigned labour law tasks to be carried out for the director of the National Revenue Information, directors of chambers of fiscal administration, director of the School of Revenue Administration, and officers working in various organisational units of the office supporting the minister. Meanwhile, the tasks of the head of the organisational unit in matters related to labour law and service of officers in the chamber of fiscal administration and subordinate organisational units of the National Revenue Administration were assigned to directors of chambers of fiscal administration.

The proposed model of the National Revenue Administration is intended to facilitate an effective collection of taxes, and streamline the handling of taxpayers, including provision of assistance to taxpayers and entrepreneurs in correct carrying out of their tax and fiscal obligations. It is also designed to ensure an effective administrative enforcement of receivables and reduce the existing tax gap, as well as improve the effectiveness of measures intended to counter tax fraud and recover tax and fiscal arrears. The National Revenue Administration is supposed to provide uniform and homogeneous case-law in tax and revenue matters throughout the country, ensure fast and reliable verification of data supplied by taxpayers in tax declarations and fiscal documents, and improve the effectiveness of control of how taxpayers carry out their tax obligations [Glumińska-Pawlic 2018: 66-80]. However, available literature has emphasised views that the introduction of fiscal and revenue control which in procedural terms is significantly different from the tax audit under the Tax Ordinance Act and which, in case of entrepreneurs, also applies provisions laid down in the Business Law Act, deepens the dualism of control by the National Revenue Administration bodies. This has led to the establishments of three legal regimes governing the compliance with provisions of tax law: customs and revenue control (subject to provisions of the Act on the National Revenue Administration and the Tax Ordinance Law), tax audit of entrepreneurs (Business Law and Tax Ordinance in the absence of specific provisions in the former), and tax audit (carried out solely pursuant to provisions laid down in the Tax Ordinance Law [Strzelec 2017: 16].

It should be stressed that the efficiency of tax administration plays a major role in the effectiveness of VAT collection. In addition to the shape of the tax system, which comprises elements such as the standard VAT rate or the number of preferential tariff rates, an important role is also played by administrative costs entailed in its functioning, expressed as a percentage of income [Agha, Haughton 1996: 303-308], as well as the society's perception of the fairness of the tax system, effectiveness of the legal system and tax abuse punishability rate [Christie, Holzner 2006: 11]. Increasing expenditure on tax administration translates (in relation to net revenues) translates into higher VAT collection rates. Both the well-perceived effectiveness of the tax system and effectiveness of the legal system, as well as a high conviction rate for tax evasion contribute to reducing the VAT gap [Gajewski 2018: 63-65].

10. Conclusions

The changes introduced in Poland have led to a marked increase in tax revenues in comparison to the period before measures designed to seal the tax system were undertaken. Nevertheless, it cannot be firmly established to what extent the increase in revenues resulted from an upturn in the economy, and to what extent it was caused by

organisational measures, measures designed to close loopholes in the system, and shifting of VAT returns. While it is beyond any doubt that improving the effectiveness of collection of taxes was an important factor in increasing the budget revenues, closing the loopholes in the tax system in itself cannot be considered the only factor leading to an increase in tax revenue. However, it may be assumed that sustaining this trend will be increasingly difficult as in the first place it was only possible to inactivate specialised international groups creating highly complicated mechanisms based on chain and carousel transactions.

While it is true that thanks to the Standard Audit File for Tax the tax authorities have access to some information without having to carry out tax audits or investigation procedures, the system focuses in formal errors, and fails to distinguish between a genuine invoice and a false one in the material sense. Furthermore, the SAF-T does not diagnose unrecorded trade, i.e. the absence of invoices or receipts when they should have been issued. In addition, with the exception of the IT System of the Clearing House (STIR) the undertaken measures ignore a crucial moment in VAT fraud: the payment of public funds. This is what the authorities should focus on, however from the organisation point of view controlling the ever-growing number of declarations serving as a basis for VAT returns.

The increase in taxpayers' obligations and strengthening of powers of tax authorities, as caused by the changes in the law, entails a number of potentially negative consequences. Fiscally effective solutions usually entail considerable interference in the taxpayer's rights, which is the case with the majority of the cases analysed herein. Meanwhile, time will tell whether the National Revenue Administration bodies will prove to be modern and taxpayer-friendly, and whether they will efficiently collect levies and at the same time ensure financial security of the state. That said, it is difficult at this point to determine whether the functioning of the National Revenue Administration will indeed make it possible to avoid the undertaking of measures that are burdensome on both taxpayers and entrepreneurs as with the high level of interference, the amendments basically do not envisage any major instruments for the protection of the taxpayer.

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