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KMLZ VAT NEWSLETTER

Conditions for self-disclosure regarding exemption from punishment – Tax Compliance Management System strongly recommended

The distinction between the correction of a tax return, pursuant to sec 153 General Fiscal Code and a self-disclosure, pursuant to sec 371 AO General Fiscal Code, may be blurred in practice. Each individual mistake in a tax return might bear the potential risk of being considered as tax evasion. The tax payer or his legal representative may avoid criminal prosecution by filing a self-disclosure with the tax office. The effect of exemption from punishment by filing a self-disclosure will not apply if at least one of the tax crimes has already been detected. The constitution of an act of criminal tax evasion depends on whether the taxpayer or his representative intentionally declared incorrect information to the tax office. A company's establishment of a Tax Compliance Management System (TCMS) could be regarded by the fiscal authorities as an indication that mistakes in tax returns are not accepted, thereby excluding the assumption of intentional tax evasion.

A self-disclosure could prove to be too late

The Federal Supreme Court recently ruled, that tax evasion could be considered as already having been detected, even before the tax office has examined the relevant tax return. Once the tax crime is considered as detected, self-disclosure no longer offers exemption from punishment. This may also apply to VAT: When a VAT return requires correction, it might already be too late for a self-disclosure with the effect of exemption from punishment. The assumption of an intentionally committed tax evasion can be effectively prevented by the implementation of a Tax Compliance Management System.

1. The court judgement

In its judgement published on 28 June 2017, the Federal Supreme Court confirmed the previous tendency, i.e., to consider a tax crime, in certain circumstances, as having been detected even before the tax return has been reviewed by the tax office (decision of 09.05.2017 – 1 StR 265/16). In the present case, the recipient of commission payments (the defendant) failed to declare these revenues in his initial income tax returns. Subsequently, events unfolded which led the recipient to consider filing a self-disclosure concerning these revenues. The events in question concerned a preliminary bribery investigation which was being conducted in Greece. Bank statements, which disclosed the payments made to the defendant, were discovered by the Greek investigation team. However, at the time the defendant proceeded to file his self-disclosure and amend his incomplete income tax returns, the documents had not yet been passed on to the German tax authorities. The Federal Supreme Court found, that the tax evasion had already been detected by the Greek authorities prior to the defendant's self-disclosure.



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2. Detection of tax evasion resulting in exclusion of exemption from punishment

Pursuant to sec 371 para 2 sentence 1 no. 2 General Fiscal Code (AO), a self-disclosure does not offer exemption from punishment if at least one of the tax crimes has already been fully or partially detected, prior to the filing of the self-disclosure and the perpetrator knew this or should have expected this result after due consideration of the facts of the case. In this judgement, the Federal Supreme Court emphasizes the following aspects:

An act of tax evasion is considered as having been detected if a preliminary assessment of the known facts is regarded as being grounds for a criminal conviction. The term “detection of tax crime”, pursuant to sec 371 para 2 sentence 1 no. 2 AO, is not equivalent to the requirement of criminal suspicion. Hence, the assumption of detection of tax crime does not require the threshold of a concrete criminal suspicion pursuant to sec 170 para 1, sec. 203 Code of Criminal Procedure, nor does it require the identity of the perpetrator to already be known.

Furthermore, the tax evasion need not, necessarily, be detected by the German tax office or the German prosecution authorities. In principle, the tax evasion could be detected by anyone, provided it can be assumed that the knowledge of the detection will be passed on to the competent authorities.

3. Significance for VAT

In companies, VAT issues regularly arise in connection with large scale operations. A faulty setting within an electronic accounting transaction will result in a correction with dizzying numbers. Thresholds exist within the tax administration,

beyond which corrections are passed on “automatically” to the tax fraud units or prosecution authorities. The usual defence raised by any affected company is that its staff did not act with the intention of committing tax evasion. However, such objections often have little prospect of success. If organisational deficits exist within a company, the prosecution authorities regularly assume that these deficits are tolerated and accepted by the directors of the company, which is considered as conditional intent in terms of tax evasion (*dolus eventualis*). Regarding the present judgement, findings during a VAT audit, which were treated incorrectly, might also amount to detected tax crime.

4. Recommendations

If companies want to protect themselves and their employees from the potential risk of criminal investigation, they must actively shape and control the fulfilment of their tax tasks. A TCMS might be considered as an indication of the intention to avoid errors equating to tax evasion. The more a company takes steps to ensure the fulfilment of its tax tasks and treats these tasks as important in the day-to-day operation of the company, the less likely the company is of being exposed to an accusation of reckless understatement of tax or even intentional tax evasion. Control and supervision measures, as well as preventive action taken in order to avoid future mistakes are key elements of a TCMS. However, even if intentional behaviour could be completely excluded, the risks associated with the filing of a correction in accordance with sec 153 AO still remain. The correction of a VAT return must be filed without undue delay and must not be postponed until the next annual VAT return or the VAT return for December. A correction, which is not filed in a timely manner, constitutes tax crime.