Unjustified Set-Off as a Criminal Offence in Italian Tax Law

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Article

ABSTRACT

This article analyses the criminal offence of unjustified set-off in Italian tax law, introduced alongside the offence of non-payment of VAT by Legislative Decree No. 74/2000 (Sects. 10-ter and 10-quater) to counter increasingly common forms of tax evasion. It explains set-off as a legal mechanism (vertical vs. horizontal set-off under Sect. 17 of Legislative Decree No. 241/1997) and shows how the abuse of horizontal set-off through non-existent or non-applicable tax credits enables concealed non-payment of taxes, including in VAT carousel fraud schemes. The contribution examines the constitutive elements of the offence: the use of fictitious or ineligible credits via Form F24, failure to pay amounts exceeding €50,000 per tax period, the required mens rea (including contingent intent), the temporal moment of commission, and the position of intermediaries. It further outlines the parallel administrative offence regime, the speciality principle governing the interaction between criminal and administrative sanctions, and the mitigating effects of voluntary regularisation. The article concludes that the combined framework of return offences and payment offences (non-payment and unjustified set-off) creates a comprehensive deterrent structure aimed at improving tax compliance and protecting the financial interests of the Italian state.

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Introduction

Non-payment of an amount due by way of tax as calculated by a taxpayer in his tax return, including value added tax (VAT), is currently one of the most frequent forms of tax evasion in Italy.

Two new offences have been added[1] to the corpus of Italian direct taxes and VAT legislation with a view to curbing this practice: non-payment of VAT and unjustified set-off, as laid down by Sects. 10 ter and 10 quater, respectively, of Legislative Order No. 74 of 10 March 2000 entitled "New measures against income tax and value added tax offences."

Sect. 10 ter prescribes imprisonment for a term of six months to two years for the non-payment of VAT amounting to more than € 50,000 as calculated on the annual return.

Sect. 10 quater prescribes the same punishment for anyone who fails to pay the sums due as the result of having set off, within the meaning of sect. 17 of Legislative Order No. 241 of 9 July 1997, credits not applicable or non-existent amounting to more than € 50,000 for each taxation period.

Unjustified set-off is a more insidious offence than simple failure to pay. Non-payment of tax debts duly declared in a return, in fact, is readily detectable by Inland Revenue through the use of IT procedures that cross-check the figures on the returns lodged by taxpayers against the amounts actually effectuated. An unjustified set-off, however, is not immediately apparent but must await the determination of the non-existence or non-applicability of the credits thus employed.

Italy has introduced another measure against VAT carousel frauds perpetrated by insertion of a "missing trader" between the Community supplier and the Italian customer. When the annual VAT return is presented, the VAT debt for sales in Italy (as against the neutrality of intra-Community acquisitions) emerges. Failure to pay the tax owed according to the return would be readily detectable. Instead, the taxpayer seeks to conceal his position by setting off non-existent credits against his VAT debt.

I. Set-Off as a Legal Institution

A fuller understanding of the constituent features of this offence can best be obtained from a brief examination of the term "set-off."

Set-off is a means whereby tax liabilities can be discharged via employment, for the payment of such debts, of tax and contribution credits claimed against the State. It is classified as either vertical or horizontal.

Vertical set-off occurs when credits and debts relating to the same type of tax are involved. It is effectuated upon the presentation of the corresponding tax return. A VAT credit, for example, arising from a return filed for the fiscal year 2008, can be used, wholly or in part, to set off a VAT debt resulting from the return filed for the fiscal year 2009.

Sect. 17 of Legislative Order No. 241 of 9 July 1997 introduced horizontal set-off (the subject of the offence in question). This differs from vertical set-off in four ways:

- It applies to credits and debts arising from different taxes. An income tax credit, for example, can be set off against a VAT debt;

- Only credits arising from annual returns can be set off;

- No more than € 516,456.90 can be set off per annum;

- Set-off is not applied on the occasion of the filing of an annual return but when Form F24 is filled in. F24 is the form prescribed by Italian law for the payment of taxes and duties. It is composed of several boxes in which the taxpayer is required to indicate the relevant codes, the tax debt he has to pay, and such tax credits as he intends to use to offset the said debt, together with the balance (if any) still owing. If this balance is nil, Form F24 must nonetheless be duly filed in by the taxpayer.

Form F24 is lodged in two ways: electronically or in paper form. Holders of a VAT number are required to deliver their Form F24 via the Internet (either directly or through duly enabled intermediaries). Payment of such amounts as may be due is also effectuated electronically by withdrawal, in favour of Inland Revenue, of the sum concerned from the taxpayer's current account. The account must be at one of the banks operating in accordance with the terms of an agreement with Inland Revenue or be accessible through the home banking services of the banks themselves or the Italian GPO.

Taxpayers who do not have a VAT number can also file using the Internet. In addition, they can hand in their (paper) Form F24 at any bank or post office.

II. Unjustified Set-Off as a Criminal Offence

1. Offenders

Criminal responsibility is a personal liability (Sect. 27, Italian Constitution). The actual perpetrator (or principal in the first degree) will thus be held responsible for the offence of unjustified enrichment.

Other actors may be involved in the wrongdoing, particularly the intermediary, that is to say the person who sees to the electronic transmission of the Form F24 and is frequently the one who also handles a taxpayer's accounting and fiscal affairs. In accordance with the general principles of participation in criminal offences (Sects. 110 et seq. of the Criminal Code), an intermediary may be charged as an accessory if, for example:

- He has suggested to the taxpayer that an illicit advantage may be gained through an unjustified set-off and he has duly completed and filed the corresponding false Form F24;
- While not actually suggesting the wrongdoing, he has completed and filed Form F24 according to the taxpayer's instructions, with full knowledge of the unjustified set-off thus perpetrated.

2. Conduct Giving Rise to the Offence

The offence is one of commission perpetrated in two distinct stages: setting off in Form F24 of non-existent or non-applicable credits against other debts; filing of such a falsely completed form, whether electronically or by physical presentation.

The credit thus unjustifiably set off may be of any type. It is not confined to income taxes and VAT.

The components of the conduct that constitute the offence are as follows:

a) Exploitation of a non-existent or non-applicable credit

A non-existent credit is one invented by the taxpayer, with or without the support of a false document.

A non-applicable credit is one that actually exists but is not included among those that can be offset within the framework of Sect. 17 of Legislative Order No. 241 of 1997 or exceeds the prescribed € 516,456.90 threshold.

b) Failure to pay sums that are due

Following his resort to an unjustified set-off, the taxpayer does not pay the corresponding fiscal debts that would otherwise be due. It is not yet clear from the case law whether the rule is confined to the non-payment of direct taxes and VAT or whether it also extends to other taxes and duties. Two approaches can be taken:

- The narrower view starts from the premise that the rule itself forms one of the provisions of Legislative Order No. 74 of 2000, whose sole purpose is the ordering of offences relating to income taxes and value-added tax.
- The broader view is founded on the literal formulation of the rule insofar as it expressly punishes non-payment, not of taxes but simply of sums due within the meaning of Sect. 17 of Legislative Order No. 241 of 1997, through the unjustified setting off of non-applicable or non-existent credits.

The punishability threshold

Legislative Order No. 74 of 2000 has been drafted with the intention to confine the imposition of a criminal sanction to actions that result in a serious detriment to the economic interests of the State. The perpetrator of an unjustified set-off can therefore only be charged with a criminal offence if his action results in the non-payment of sums due amounting to more than € 50,000 for each taxation period. This punishability threshold is a constituent component of the offence.

The term taxation period means the calendar year.

3. The Subjective Element

Mens rea (generic dolus) – the subjective intention or knowledge of wrongdoing – is a necessary element of the offence. The perpetrator must have been aware of two facets of his action: payment of less than that which was due, owing to his having offset a non-existent or non-applicable credit; non-payment of sums amounting to more than € 50,000 in the same year.

> The offence is equally punishable in the event of a contingent intention, that is to say when the main objective of the offender was not to avoid payment of what was due but to counterbalance a company's temporary shortage of cash or to create unjustified financial assets for the commission of other offences.

4. The Moment of Commission

The offence is deemed to have been committed at the moment a falsely completed Form F24 (resulting in the non-payment of a sum exceeding € 50,000) is filed.

In the event of the filing of several forms during the course of a year, each resulting in the non-payment of a sum less than the threshold of € 50,000, commission of the offence begins at the moment Form 24 is filed and whose unpaid amount, when added to the previous unpaid amounts, results in the crossing of this threshold.[2]

Effectuation of further unjustified set-offs aggravates the offence thus substantiated by the crossing of the threshold. It does not give rise to a further offence, irrespective of the amount involved.

III. Unjustified Set-Off as an Administrative Offence

A person who perpetrates an unjustified set-off also commits an administrative violation within the meaning of Sect. 13 of Legislative Order No. 471 of 1997. Application of the administrative sanction on the part of Inland Revenue is accompanied by proceedings for recovery of the tax not paid.

The administrative sanction for unjustified set-off of a non-applicable credit is 30% of the amount not paid.[3]

The administrative sanction for unjustified set-off of a non-existent credit ranges from 100% to 200% of this credit. It is also fixed at 200% for credits exceeding € 50,000.[4]

1. Relationship Between the Administrative and the Criminal Sanction: The Speciality Principle

Sect. 19 of Legislative Order No. 74 of 2000 lays down that, when the same offence is punishable in accordance with one of the provisions of this Order and a provision imposes an administrative sanction, the "special provision" is to be applied. This term is used for a provision that comprises all the components of the other (general) provision, plus one or more specialising features.

> According to Inland Revenue,[5] the criminal provision usually proves to be special on account of the specific elements it requires, e.g., specific *dolus,* crossing of the punishability threshold, and the particular ways and means of commission.

Application of the speciality principle presupposes identical nature of the act punished by one of the provisions of Legislative Order No.74 of 2000 with that punished by an administrative sanction.

In any event, Sect. 19 (2) prescribes that exclusion of the administrative sanction applies solely to a natural person to whom the offence is ascribed. The aim of this provision is to prevent punishment of the same subject twice for the same offence, while simultaneously retaining the possibility of splitting punishment between different types of offenders such as a director (the active offender) and the company (liable to the administrative sanction).

> In view of the fact, therefore, that Sect. 7(1) of Legislative Order No. 269 of 30 September 2003, converted into Law No. 326 of 24 November 2003, *prescribes that administrative sanctions relating to the fiscal relationship proper to companies or bodies with a legal personality are solely chargeable to the legal person*, whereas criminal liability is always personal, it follows that the speciality principle is only applicable to violations committed within the context of private firms or by artists, professionals, or associations, bodies or societies devoid of a legal personality in cases where the fiscal violation and the criminal violation can be attributed to the same natural person.

2. Relationship Between the Administrative and the Criminal Sanction: The Attenuating Circumstance

A taxpayer can correct his administrative offence by paying the tax due plus a reduced sanction. If he has received a *notification of irregularity* from Inland Revenue, he can regularise his position by paying an administrative sanction corresponding to 3% of the credits unjustifiably set off.[6]

He is also free to proceed to what is called *effective remediation* prior to receiving such a notification by spontaneously paying an administrative sanction corresponding to 3%. This step must be taken no later than 30 days after the violation or 3.75% is taken within the term for presentation of the income tax return for the year in the course of which the offence was committed.[7]

Settlement of the administrative offence prior to the opening of the criminal proceedings initially enables a person eventually found guilty of the criminal offence to take advantage of this special attenuating circumstance, and to pay only one third of the criminal sanction that would otherwise have been imposed.[8]

> Legislative Order No. 138 of 13 August 2011 introduced a significant amendment of the *corpus* of Legislative Order 74/2000. "Plea bargaining" within the meaning of Sect. 444 of the Code of Criminal Procedure[9] is only admissible for all tax offences in cases where the attenuating circumstance as per Sect. 13 are given. This amendment applies to offences committed after 17 September 2011.

IV. Conclusions

The introduction of the offences of non-payment and unjustified set-off has criminally sanctioned, according to the specific conditions prescribed, all possible ways and means of evasion in each of the stages in the process of determining and paying taxes:

- Quantification of the taxable amount, with the tax return offences (return not lodged, inexact or fraudulent return: Sects. 2 to 5 of Legislative Order 74/2000);
- Payment, with the payment offences (non-payment, unjustified set-off, and fraudulent underpayment of income taxes: Sects. 10 bis to 11 of Legislative Order 74/2000).

This deterrent scenario sets out to encourage all taxpayers to comply with their fiscal obligations. Maximum prevention is in the interest of the State in its upstream curbing of the tax evasion still rife in Italy.

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1. By Sect. 37 (7) of Legislative Order No. 223 of 2006↩
2. Inland Revenue Circular No. 28 of 4 August 2006↩
3. Sect. 13 of Legislative Order No. 471 of 1997↩
4. Sect. 27 of Law No. 185 of 29 November 2008↩
5. Circular No. 154/E of 4 August 2000↩
6. Sect. 2 of Legislative Order 462/1997↩
7. Sect. 13, Legislative Order 472/1997↩
8. Sect. 13, Legislative Order 74/2000↩
9. Sect. 444 of the Code of Criminal Procedure
   1. The accused and the public prosecutor may request the Court to apply, in the manner and measure indicated, an alternative sanction in the place of either a pecuniary penalty, reduced by up to a third, or punishment by way of imprisonment when this, in consideration of the circumstances and reduced by up to a third, does not exceed five years, whether alone or in conjunction with a pecuniary penalty.
   2. If there is also consent on the part of the party that has not formulated the request, and an acquittal is not to be pronounced within the meaning of sect. 129, the Court, on the basis of the record, may, if it regards the juridical qualification of the fact, and the application and comparison of the circumstances advanced by the parties as correct, and the penalty indicated as congruent, order the application of the same and state in its decision that it has been requested by the parties. In the event of the appearance of a civil party, the Court does not decide on the relative request; the accused, however, is ordered to pay the costs of the civil party in the absence of just reasons for their total or partial set-off.
   3. The party formulating the request may make its efficacy subject to the granting of conditional suspension of the punishment. In this case, the Court will disallow the request if it decides that conditional suspension cannot be granted.↩

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