Executive summary of the public audit report

ELECTRONIC COMMERCE CONTROL

30 April 2015 No. VA-P-60-12-7

Full audit report in Lithuanian is available on the website
of the National Audit Office: www.vkontrole.lt
www.vkontrole.lt

DEFINITIONS

Personal details refer to any information, related to a natural person-data subject, whose identity is known or may be directly or indirectly identified using such data as the personal code, one or several physical, physiological, psychological, economic, cultural or social characteristics[1].

Electronic shop refers to a location of electronic commerce on the internet, which has a unique address and a website, where the customer may choose and order goods and services. The website may offer an opportunity to pay for the goods and services purchased.

Electronic commerce platform refers to a system of software, which enables sellers to create, manage and place a digital shop, which offers an assortment of certain goods and (or) services, on a server.

Internet auction refers to an internet website, where registered users can announce about selling goods and the buyers compete by offering a higher price. It may also offer goods for a fixed price. The transactions and transfers take place on the internet and are managed by the administrator of the website. The most popular auctions in the world are also websites of electronic commerce.

Internet website refers to one or more interrelated web pages. They always have a home page, accessible on the internet using an internet address and (or) an IP *(Internet protocol)* address. Internet websites are usually prepared and managed as a set of information kept in one service station by a person, group or organisation.

IP address refers to a unique number, used for identification of an unambiguous data packet sender and receiver. On the internet IP addresses are allocated by delegated organisations managing IP address blocks. An IP address usually allows to identify the country or institution of a specific computer and find that computer.

MOSS *(mini one stop shop)* refers to a special taxation scheme of telecommunications, radio and television broadcasting and electronic services, applied in the European Union[2].

MOSS system refers to an information system, used by participants of a special scheme, implementing value added tax obligations[3].

Customs refers to the Customs of the Republic of Lithuania, which consists of the entirety of the customs institutions, responsible for implementing the customs legislation[4].

Remote communication tool refers to a tool that can be used to enter into a payment services contract, when the supplier and the user of the payment services are not physically present[5].

1 The Law On Legal Protection Of Personal Data of the Republic of Lithuania, 11-06-1996 No. I-1374 (the revision of the Law No. X-1444, 01-02-2008), Art. 2, pt. 1.

2 The rules regarding the registration of taxable persons as users of the taxation scheme for telecommunications, radio and television broadcasting and electronic services, as well as composition of the value added tax code and assigning it for such persons, approved by the Head of the State Tax Inspectorate under the Ministry of Finances of the Republic of Lithuania, by the order No. VA-2, 07-01-2015.

3 Ibid.

4 The Law on Customs No. IX-2183, 27-04-2004.

OECD refers to the *Organisation for Economic Co-operation and Development*.

Police refers to the entirety of police institutions and officers ensuring personal and public safety, as well as public order6. In this summary: The Police Department under the Ministry of Interior of the Republic of Lithuania, police institutions and specialised police institutions.

Website or web page refers to a file, prepared using hypertext markup language (HTML) and stored in a computer of web services, which contains text, graphs and hypertext links to other web pages on the same website or other websites7.

Third parties refer to countries that do not belong to the European Union.

STI refers to the State Tax Inspectorate under the Ministry of Finances of the Republic of Lithuania and county tax inspectorates.

Web hosting refers to a service, provided by internet service providers (ISP) and internet access providers, encouraging external companies to put their websites on ISP computers, which are connected to high-speed internet transmission channels. ISPs providing this service usually provide their clients with equipment and guarantee the necessary channel throughput8.

5 The Law on Payments of the Republic of Lithuania, 28-10-1999, No. VIII-1370 (revision of the Law No. XI-550, 10-12-2009).

6 The Law on Police Activities, No. VIII-2049, 17-10-2000.

[7] Valiukėnas V., Sabaliauskaitė R., Gabijūnienė J., Aiškinamasis telekomunikacijų terminų žodynas, Vilnius: Lietuvos telekomas, 2004

[8] Valiukėnas V., Sabaliauskaitė R., Gabijūnienė J., Aiškinamasis telekomunikacijų terminų žodynas, Vilnius: Lietuvos telekomas, 2004

EXECUTIVE SUMMARY

Electronic commerce (or e-commerce) is an increasingly popular method of selling goods and services. It has a number of advantages compared to traditional commerce, which make it attractive to both business and customers. In 2013-2014 every fourth citizen of Lithuania shopped on the internet, which is three times more than in 2009.9

E-commerce is subjected to the same requirements as traditional commerce: legal activity, income accounting, tax payment, legal administration of the customers' data, etc. That is a relatively new field of activity in Lithuania, therefore the institutions participating in e-commerce control require specific abilities and (or) appropriate technical equipment and software. The violations related to e-commerce are recorded by different institutions responsible for individual fields of activity according to their competence: STI, the Customs, the State Data Protection Inspectorate, the State Consumer Rights Protection Authority, etc.

Their expertise in e-commerce and applicable control measures also differ:

- As of 2013 the STI implements regular scheduled e-commerce control measures. The results of these measures in 2013-2014: individual persons declared an additional 639 000Lt of payable taxes and 18 persons registered their individual activity;
- The State Data Protection Inspectorate and the State Consumer Rights Protection Agency implements special measures for e-commerce control according to the need — an increased number of customer complaints, resulting from a growing number of electronic shops, etc.;
- The Customs only begin e-commerce control by appointing responsible officers (2014) and planning to approve the rules of e-commerce control at the Customs (2015).

Considering the fact that regular e-commerce control measures are implemented only by the STI, the Customs has only just started and other institutions participating in the control do not implement regular e-commerce control and do not accumulate related data, the goal of this audit was to evaluate the organisation of e-commerce control procedures and provide insights, which would help to improve this activity.

The audit was conducted at the State Tax Inspectorate under the Ministry of Finances of the Republic of Lithuania and at the Customs Department under the Ministry of Finances of the Republic of Lithuania. Information was gathered at the State Data Protection Inspectorate, the State Consumer Rights Protection Agency and the Lithuanian Criminal Police Bureau. The audit covered the period 2012-2014 and the data from the previous years was used for conducting the analysis of changes.

We found that there is a number of practical questions regarding the control of the value added tax income, received for telecommunications, radio and television broadcasting and electronic services, as well as regarding the conditions for the implementation of VAT tax obligations, because not all issues related to the changes in the procedure of VAT application to these services, adopted as of 2015, are solved on the EU level.

9 Eurostat data.

Moreover, there is no coordinated sharing of experience between the institutions implementing e-commerce control and their current cooperation is limited to conducting control actions and (or) studies.

Having evaluated the evidence gathered during the audit, we provide conclusions and recommendations, appropriate implementation of which could reduce the amount of unaccounted, undeclared and untaxed income received from e-commerce, as well as eliminate goods that violate the rights of intellectual property, drugs and other prohibited substances (goods), etc. in the EU market.

CONCLUSIONS

E-commerce in Lithuania is a quickly spreading phenomenon: in the period of 2009-2013 the number of citizens shopping on-line increased three times, although in 2013 this number still remains almost several times smaller than the EU average, while the turnover of the Lithuanian e-commerce between companies and customers constituted about 0.1% of the EU turnover.

1. The e-commerce control, conducted by the State Tax Inspectorate brings substantial results, but this area could focus more attention on human resources. E-commerce control requires specific knowledge: employees must know how to perform a website selection and data analysis, have experience in working with special software and smartphone applications. These technologies are rapidly changing, but the last training for the employees of the district departments of the State Tax Inspectorate took place in 2011 (chapter 1).

2. On the EU level, not all issues are solved, related to the changes in the procedure of VAT application to telecommunications, radio and television broadcasting and electronic services, applied as of 2015, by implementing the EU Council Directive 2008/8/EC of 12 February 2008. Therefore, EU countries may lose their income from value added taxes or receive less than they should for the telecommunications, radio and television broadcasting and electronic services, because:

   2.1. VAT payment by registered taxpayers using use MOSS system, under the supervision of other EU countries, is virtually uncontrolled (chapter 2);

   2.2. the State Tax Inspectorate has limited opportunities to check, whether the service provider registered as a MOSS participant in another EU country, has accounted and paid Lithuania the correct value added tax (chapter 2).

3. The State Tax Inspectorate, the Customs and the Police should share more experience — they cooperate only in cases of conducting control or studies. The lack of cooperation may result in a risk of work duplication — institutions may be burdened with developing working and employee training methods, which were already successfully applied in other institutions (chapter 4).

4. Personal data, provided by users for telecommunications and electronic service providers is not always managed according to the requirements of personal data protection. Some of the service providers may not even be familiar with the requirements of personal data protection, because collecting evidence to identify the location of the customer is a new requirement and there is no information about it on the website of the State Data Protection Inspectorate and,

according to the data of March 2015, only 9 service providers out of 21 Lithuanian service providers registered at MOSS system were registered at the Register of Personal Data Controllers for various data management purposes (chapter 5).

RECOMMENDATIONS

For the State Tax Inspectorate under the Ministry of Finances of the Republic of Lithuania

1. In order to improve e-commerce control, it is necessary to provide measures that would ensure appropriate preparation of human resources for e-commerce control (conclusion No. 1).
2. Considering the fact that the control of the income received from the value added tax for telecommunications, radio and television broadcasting and electronic services will have to be conducted in the nearest future, although not all issues related to the changes in the taxation procedure of these services, applicable as of 2015, are solved, it is necessary to prepare a manual for monitoring and control of the income received from the value added tax for telecommunications, radio and television broadcasting and electronic services (conclusion No. 2).

For the State Tax Inspectorate under the Ministry of Finances of the Republic of Lithuania and at the Customs Department under the Ministry of Finances of the Republic of Lithuania.

In order to improve the efficiency of the e-commerce control, as well as prevent e-commerce-related crimes, it is necessary to implement inter-institutional cooperation improvement measures, suggested while conducting the *Plan of the measures for non-observed economic phenomena control of 2012*, approved by the Commission, which was formed by the resolution of the Government for the purpose of coordinating the cooperation between state economic and financial control, as well as law enforcement authorities (conclusion No. 3).

For the State Data Protection Inspectorate

In order to make sure that the telecommunication and electronic service providers, registered at MOSS, administer personal data in a legal and safe manner, ensuring the rights of data subjects, it is necessary to:

1. Perform a planned inspection of these service providers and, upon finding violations, take appropriate measures to eliminate them (conclusion No. 4).
2. To provide preventive measures to make sure that telecommunications and electronic service providers administer personal data based on the requirements of personal data protection (conclusion NO. 4).

The measures and terms of the implementation of recommendations are provided in "The plan of implementation of recommendations", provided as the appendix 2 of this report.