

PricewaterhouseCoopers
Belgium

For the attention of: Ine Lejeune

By e-mail only

11 July 2011

Dear Sirs

Review of Article 37.3 of Directive 2006/112/EC: Expert study on the issues arising from taxing the supply of goods and the supply of services for consumption on board means of transport

I attach a paper, on behalf of the _____ in the UK, the Netherlands and Scandinavia, in response to the PricewaterhouseCoopers ("PwC") consultation on the identification and high-level assessment of different policy options for amending Article 37.3.

Please note that the comments on the various policy options included in the attached paper and below are without prejudice to _____ position that the existing exemptions for the supply of goods and services for consumption on board means of transport should continue and that before any restrictions to the existing exemptions are considered, a full economic impact assessment should be undertaken.

The review of Article 37.3 should carefully take into account the impact and unintended consequences on the ferry sector, a sector which is essential in pursuing European public interest objectives. _____ believes that any restrictions to the existing exemptions would seriously contribute to undermining the ability of the ferry operators to maintain quality services at competitive prices on certain routes and would create additional burdens for a sector which is already facing significant cost increases arising from high fuel prices and a wide range of severe regulatory challenges, such as the sulphur limits of fuels at berth and in Emissions Control Areas. We estimate that the introduction of VAT on our on board sales would lead to an increase in our costs of approximately SEK 170 million annually.

It is also worth adding that the resultant increase in prices from the imposition of VAT on the supply of goods and services for consumption on board ferries is likely to lead to a modal shift from sea to road with an increase in emission levels. Our Scandinavian routes, which compete with bridges will be most affected. This would clearly be at odds with the Commission's goal of a sustainable transport policy. Also, the impact on employment cannot be ignored with reduced demand for ferry services having a major impact on employment opportunities in areas of already high unemployment.

Furthermore, as mentioned in the attached paper, given the lack of harmonised VAT rates and rules, an EU-wide exemption for all goods and services consumed on board would represent the simplest and most practicable solution for operators.

In responding to the various policy options we do not consider that the proposed approach and methodology for evaluating these options, and specifically the proposed scoring of different Key Performance Indicators (KPIs), is a statistically sound basis for achieving valid conclusions on future policy. We have therefore concluded that it would be inappropriate to complete the matrices as requested. Instead, we have provided some detailed commentary on the one option that, in our view, clearly stands out as the most appropriate future policy solution, notwithstanding our comments above. However, in order to be as helpful and constructive as possible, we have presented our comments within the framework of the KPIs.

In summary, of the various options you have presented, we strongly favour option “4bis.” – to change the VAT place of supply rule to the point of departure of the transport operation (for all transport sections) and keep the existing option to exempt the supply of goods for consumption on board ships, aircraft or trains. In particular, we consider that only this option provides the necessary levels of certainty, practical simplicity and efficiency for which we, other affected companies and tax authorities alike, are striving.

We trust that you will find our analysis helpful and would be pleased to discuss our comments and conclusions in more detail if required.

Yours faithfully

Response from

Review of Article 37.3, Council Directive 2006/112/EC

Policy options in relation to the future treatment of supplies of goods and services (including restaurant and catering services) for consumption on board a means of transport.

Introduction

This paper is presented on behalf of the _____ in the UK, the Netherlands and Scandinavia.

_____ is one of the world's largest ferry companies, with a focus on the transportation of passengers and freight. At the end of 2010 _____ operated 17 routes in Scandinavia and around the UK, and had a fleet of 38 vessels. _____ also owns five ports. During 2010, 15.1 million passengers travelled with _____ also transported 3.2 million vehicles and 1.6 million freight units

The comments that are made in this paper on the various policy options are made without prejudice to _____ position that the existing exemptions for the supply of goods and services for consumption on board means of transport should continue and that before any restrictions to the existing exemptions are considered, a full economic impact assessment should be undertaken.

_____ has carefully considered the different policy options advanced by PwC and reviewed them against the selected Key Performance Indicators (KPIs). We have serious reservations about the proposed approach and methodology that will be used to evaluate the different policy options and to reach decisions on future policy. Moreover, we do not consider that the proposed scoring of each option will provide a statistically valid basis to gather consistent and objective data on which to reach firm and sound conclusions.

In light of these considerations, we have concluded that it would be more appropriate to provide a detailed evaluation of the one policy option that stands out as the best option (subject to the two assumptions below) based on the KPI's (simplicity, efficiency, certainty, non-distortionary, effectiveness and fairness) as we interpret and understand the intended meaning of those terms - Option 4 bis:

Change Place of Supply (PoS) rule to point of departure of the transport operation (all transport sections) + keep existing option to exempt the supply of goods for consumption on board ships, aircraft or trains.

The exact definition of this option was unclear to us, particularly in comparison to Option 5 (keeping the existing rules). In our response, we have assumed that Option 4bis relates to a single place of supply rule for all goods and services consumed on board a means of transport, irrespective of the type of service being supplied. In contrast, Option 5 refers to the retention of the current mix of PoS rules for different types of services (including, for example, Articles 45, 55 and 57).

We have also assumed that the reference to the point of departure in the context of Option 4bis means that in the case of a journey with stops in more than one country, the point of departure will be the first EU country from which the means of transport departs.

Simplicity

Advantages of Option 4bis

For simple journeys (A to B), which represent the majority of passenger transport operations, the place of departure is clear to operators and tax authorities alike, is immediately verifiable, and is not open to interpretation or argument. The same can be said for the new country of departure for the return leg.

In contrast, other PoS options, in particular the place of actual consumption, would be very difficult for operators to administer in practice, and for tax authorities to verify.

The country of departure is the current rule used for the supply of on-board restaurant and catering services and goods sold on board the means of transport during the section of a passenger transport operation effected within the Community (Articles 57 and 37.3 respectively). A common rule for all goods and services purchased on board a means of transport would be relatively easy to apply in practice, as accounting systems and processes will already be set up to implement and manage this rule.

For example, operators may account for revenue taken on board at the end of each journey for commercial and management accounting purposes and therefore may already have a platform to calculate the relevant turnover and any VAT due with relative ease.

This option would also avoid the considerable additional complexity were it necessary for operators to manage and apply differing PoS rules according to the type of supply and type of service being consumed.

Given the lack of harmonised VAT rates and rules, an EU-wide exemption for all goods and services consumed on board would represent the simplest and most practicable solution for operators.

Simplicity (continued)

If this cannot be agreed, at the very least, the existing option for Member States to apply an exemption to goods sold for consumption on board should be retained. This would ensure that compliance obligations are minimized

Potential disadvantages/points to watch

For multi-leg journeys with stopovers in EU or non-EU countries, the place of departure needs to be clearly defined with clear and harmonised rules throughout the EU.

Equally, return legs would need to be clearly and consistently defined.

It is assumed that the country of departure would relate to the entire transport operation - ie. the first port of embarkation within the EU - not the point of departure for each passenger. The latter would create considerable complexity.

It would need to be confirmed that cruises starting and finishing at the same port would be deemed not to contain a 'return leg'.

Efficiency

Advantages of Option 4bis

A 'country of departure' rule would ensure that EU VAT compliance obligations are mainly confined to countries with an operational base. This may mean that there are human resources present to facilitate such compliance, file returns, meet record-keeping obligations and respond to audit enquiries. In many cases the operator will already be registered and accounting for VAT in such Member States, so this option should have least impact on current compliance costs.

Where an operator has relatively few places of departure, compliance costs should be minimized. In particular, there would be lower costs and less administrative burdens associated with programming cash registers to cope with multiple VAT rates and local rules.

This contrasts with other suggested options, such as the place of actual consumption, where there may be a need to register and account for VAT in multiple, and sometimes 'unfamiliar', jurisdictions with differing rules and rates, creating increased compliance costs, complexity and inefficiency.

An EU-wide exemption for all goods and services consumed on-board would represent a consistent and harmonized approach and thus the most efficient solution for operators. However, failing this, the retention of the option to exempt goods sold for consumption on board enables operators, in those countries exercising the option, to minimize their compliance obligations.

Efficiency (continued)

With or without the exemption, a country of departure rule for all goods and services consumed on board would at least ensure that only one country's VAT rates and rules are applicable throughout each journey.

On the other hand, the place of actual consumption or a mix of different PoS rules would be more complex to administer, involving the application of different VAT rules and rates.

Potential disadvantages/Points to watch

If a journey with stopovers is deemed to have more than one place of departure, different VAT rates may apply at different legs of the journey. This may impose increased costs and burdens associated with VAT registrations and VAT accounting, programming cash registers to account for different VAT rates at different times, and the increased need to train staff to manage the changes.

Businesses will be required to register and account for VAT in numerous countries if the exemption is no longer permitted. This burden may be alleviated through the one-stop shop registration facility.

It is therefore important to maintain a simplified country of departure rule so that the first country of embarkation within the Community is the relevant country of departure for the entire duration of the journey.

A country of departure rule may have the effect of not taxing supplies that are consumed on board within the EU (ie. for ships departing from non-EU ports) and taxing supplies that are consumed outside the EU (for ships departing an EU port but destined for a non-EU port). Some "use and enjoyment" adjustments may therefore be required to achieve the correct fiscal result.

Certainty

Advantages of Option 4 bis

For simple journeys with only one destination (A to B), the place of departure is easy to establish and verify without the need for interpretation, judgment or discretion.

A country of departure rule would align with the existing rule for take-away goods and restaurant and catering services on intra-EU sections of journeys (under Articles 37.3 and 57 respectively), so there is already familiarity with its operation for both operators and tax authorities, and accounting processes have already been established.

Compared to other policy options, such as country of consumption, operators will have certainty in advance of departure as to the VAT rules and rates to be applied for all goods and services consumed on-board. This enables the operators to price products with greater certainty and to forecast margins.

Certainty (continued)

Operators are less exposed to unharmonised and potentially complex rules in different member states.

If the rule for the place of supply is the same for all goods and services consumed and purchased on board, there will be only one member state with taxing rights. This provides increased certainty and should prevent conflicts of jurisdiction.

Potential disadvantages/Points to watch

Complications may arise in determining the place of departure for journeys that have multiple destinations. For example, a journey from the UK to France to Spain: is there a single place of departure (i.e. the UK in the example given), or multiple places of departure (i.e. the UK for the UK to France leg of the journey, and then France for the France to Spain leg)? A clear rule to the effect that only the first country of departure is relevant should be retained.

The same point can be argued as to whether there is a "return leg" for a journey with multiple destinations, but where the ship, aircraft etc. will return back to the original country of departure.

Some uncertainty could arise from unscheduled stopovers. However, this should be the subject of a common rule that effectively ignores such stopovers. Such a rule should prevent any unforeseen liability to account for VAT in the countries concerned although it may need to be subject to conditions to prevent VAT avoidance or abuse.

If 'place of supply' adjustments or exemptions targeted at non-EU consumption are needed to achieve the correct fiscal results, they would need to be simple and clearly defined, otherwise the certainty, simplicity and efficiency of the country of departure rule could be undermined.

It will be necessary to ensure that countries do not operate "force of attraction" rules where companies are required to register for VAT in countries where they have no establishment. This would increase the uncertainty for operators as to the full extent of their overall tax accounting and compliance obligations, and increase burdens on business.

Non-Distortionary

Advantages of Option 4bis

A clearly understood and practicable rule will be a strong safeguard against double taxation or unintended non-taxation. It also means that the same VAT rules and rates will operate for each journey irrespective of the nationality of the service provider or transport operator.

Non-Distortionary (continued)

All transport operators, both EU and non-EU, will have a liability to register and account for VAT for journeys departing within the EU. This removes the potential for distortion of competition between EU and non-EU operators, in contrast to other suggested options, such as the place of establishment of the transport company.

A country of departure rule would also narrow the scope for distortion of competition between "buy-on-board" transactions and "buy-off-board" transactions.

Potential disadvantages/Points to watch

In theory, a place of departure rule may encourage greater use of non-EU countries of departure leading to distortion. For example, a ship could depart from a country outside the EU, such as Gibraltar rather than Spain, and would therefore not be liable to charge VAT on goods or services purchased on board.

Alternatively, a ship could depart from a Member State applying an exemption or a relatively low VAT rate to take advantage of being able to charge less VAT.

That said, in practice, there are major commercial considerations and potential increases in operational costs that would need to be taken into account before any switching of routes to gain a VAT advantage on on-board consumption could be implemented.

Finally, a country of departure rule does not of itself ensure that the objective of taxing consumption of goods and services within the EU is met (see above comments on "Efficiency").

Effectiveness and fairness

Advantages of Option 4bis

It is likely that the transport operator will have a presence in the countries of departure even if that presence does not amount to a fixed establishment. Operators are therefore better placed to understand and apply local VAT rules and for the authorities to enforce them.

On the other hand, if VAT was due in countries where an operator has no form of establishment or operational presence, which could be the case with the current PoS rules or the country of consumption option, the VAT compliance burden and hence administrative costs would increase. This may in turn lead to more extensive non-compliance and reduce the overall effectiveness of the VAT rules.

VAT is a tax on consumption, and should be due where the goods or services are consumed. It is almost impossible to determine the place of actual consumption of many goods consumed on board transportation, and therefore the place of departure provides a sensible and practicable proxy for consumption.

Effectiveness and fairness (continued)

This contrasts with other policy options such as the place of establishment of the supplier, which may be a country where no consumption has taken place, and possibly no transport operation either.

The operation of the current “where physically carried out” rule for restaurant and catering services on board international transport (Article 55) is complicated by the need to identify when the service commences. It can also mean that different VAT rates may apply to meals consumed in the same restaurant on the same journey depending on when people entered the restaurant, or when they were first shown to their table, or when food or drink was first consumed. In summary, this is not a fair, effective or practicable rule.

Potential disadvantages/Points to watch

Some on-board services (such as live entertainment) are currently taxed where they take place. This provides an effective “exemption” to the extent that those services are performed and consumed outside the EU. Any switch to a ‘country of departure’ rule would need to include an exemption or ‘use and enjoyment’ provision to remove the risk of over-taxation (see earlier comments under “Efficiency”).