



"Jacob K. Clasen"
<JC@shipowners.dk>
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To <ine.lejeune@pwc.be>, <sophie.claessens@pwc.be>,
<pascal.ceuterick@pwc.be>, <gill.van.damme@pwc.be>
cc "Alfons Guinier" <Guinier@ecsa.eu>, "Dario Bazargan"
<Bazargan@ecsa.eu>
bcc

Subject Response to VAT matrix

To PWC

Ine Lejeune ine.lejeune@pwc.be

And in copy:

Sophie Claessens - sophie.claessens@pwc.be
Pascal Ceuterick- pascal.ceuterick@pwc.be
Gill van Damme - gill.van.damme@pwc.be

Response to VAT matrix

On 5 May 2011, the Danish Shipowners' Association received, through ECSA, the matrix prepared by PWC on VAT and intra-EU ferry services. This topic is of key importance to our members and we therefore appreciate receiving the opportunity to comment and enclose the above mention matrix filled out on behalf of the Danish ferry operators Scandlines and DFDS as well as the Danish Shipowners' Association.

Most of the ratings in the matrix are accompanied by specific comments , which have been inserted directly into the document. In addition to these specific comments, we have made additional general comments on the impact of applying vat on consumption on board intra-EU ferry services, which is the subject of the study that the matrix exercise forms part of.

1. Overall comments on the questionnaire

1.1. VAT exemption for services and goods

The questionnaire is based on the assumption that only goods provided for consumption on board are exempt from VAT. Our advisors Ernst and Young do not find this to be correct.

Article 37(3) of Directive 2006/112/EC reads as follows:

"The Commission shall, at the earliest opportunity, present to the Council a report, accompanied if necessary by appropriate proposals, on the place of

taxation of the supply of goods for consumption on board and the supply of services, including restaurant services, for passengers on board ships, aircraft or trains.

Pending adoption of the proposals referred to in the first subparagraph, Member States may exempt or continue to exempt, with deductibility of the VAT paid at the preceding stage, the supply of goods for consumption on board in respect of which the place of taxation is determined in accordance with paragraph 1.”

The provision in Article 37(3) has been modified based on the last two paragraphs of Article 8(3)(c) of the then Directive 77/388/EEC – 6th VAT Directive. The present wording of the provision was made in connection with Directive 92/111/EEC.

In the European Commission’s proposal – COM (92)448 of 4 November 1992 – for the subsequent Directive 92/111/EEC, the last two paragraphs of Article 8(3)(c) did not exist. These paragraphs were incorporated in connection with the Council of the EU’s hearing of the European Commission’s proposal. We have not been able to find any material, including Council declarations, highlighting why the Council chose to amend the article.

A strict reading of the last paragraph of Article 37(3) could imply that the provision only allows VAT exemption for goods to be consumed on board. Consequently, the first paragraph of Article 37(3) would not make any sense. In addition, it would also have led to an absurd situation for the period 1 January 1993 to 1 July 1999, i.e. that all supplies of goods on board ships would be exempt from VAT irrespective of whether the goods were consumed on board or off board, whereas services, by their nature, would always have been subject to VAT.

It is, therefore, both the opinion of the Danish and the British authorities that the existing VAT exemption covers both goods and services.

In the House of Commons’ research paper 99/74 of 22 July 1999 on “Duty-free shopping”, the paragraph on “*Life after “duty-frees ”*” reads as follows:

“Bars and restaurants: Food and drink that you buy from bars or restaurants (our highlighting) on ferries, cruise ships or aircraft to consume on board stay duty and tax free.”

Similarly, the Danish Ministry of Finance mentioned in a report^{[\[1\]](#)} to the Danish

Parliament that the proposal – in so far as restaurant and catering services on board ships, aeroplanes and trains are concerned - *”would have no impact in terms of proceeds. At the moment, these services are not subject to VAT, and the place where VAT is levied will not be relevant unless the VAT exemption is abolished. Whether services are to be subject to VAT is still an open issue until a report from the EU Commission on the issue has been published (cf. Article 8(c). ”*

The Danish Ministry of Foreign Affairs confirmed this position in its report to the Danish Parliament of 20 November 2006 prior to the ECOFIN meeting of 28 November 2006.

The Danish or the British authorities have thus either misunderstood the VAT exemption for services *or* the wording of the last paragraph of Article 37(3) must not be understood word for word. It should rather be interpreted in a wider context in which the provision forms part of and is related to Article 37(1 and 2), with the purpose of postponing taxation of both supply of goods and services consumed on board until the European Commission might propose this after a thorough analysis.

1.2. VAT taxation of supplies outside the EU

The questionnaire focuses on a taxation system according to which taxation may also apply to supplies outside of the EU. We and Ernst and Young believe that this is unrealistic, as it would imply a breach of fundamental VAT taxation principles and result in universal taxation.

First of all, the VAT is a taxation of the consumption taking place within the EU, cf. Article 2 and the delimitation hereof in Article 5 of Directive 2006/112/EC. Secondly, a VAT charge on supplies taking place outside the EU would conflict with civil law as expressed in Article 89 of United Nations Convention on the Law of the Sea, according to which *”No State may validly purport to subject any part of the high seas to its sovereignty.”*

1.3. VAT taxation at common “low rate”, in which case the proceeds will be shared by the country of departure and the country of arrival

In our opinion, the analysis should include a solution with a common “low-rate” taxation of the entire passage.

2. The need for an analysis of the economic and social consequences of imposing VAT on consumption on board

No decision should be made regarding the possible imposition of VAT on shipping companies' sale of goods and services for consumption on board based *solely* on the fiscal principle that tax must be levied on all goods and services sold within the EU. The ferry companies are important employers and the onboard activities provide employment for a significant amount of seafarers, very often in remote areas. Their activity also leads to significant activity ashore in related industries. Moreover, the ferry lines carry a large amount of short sea freight and their competitiveness towards other modes of transport would be affected by an imposition of VAT on the services, not the least in the Northern part of the EU where a high VAT rate is applied.

Scandlines and DFDS estimate that the introduction of VAT on their on board sales intra-EU would mean a yearly additional cost of 100 million DKK. This cost would inevitably lead to adjustments in the amount of on board activity and employment as well as ticket prices, including for freight. In the worst case, the extra costs could lead to the closing or significant downscaling of certain routes.

Additionally, most European ferry lines already face increasing costs due to new environmental legislation e.g. sulphur regulation coming into force in 2015, which entail a serious risk of moving freight from sea to road, contrary to the intentions of the EU transport policy as expressed recently in the 2011 White Paper "Roadmap to a Single European Transport Area".

All these factors should be analysed further before a decision is made on whether or not a proposal for VAT on onboard sales should be put forward.

3. Evaluation — VAT rate harmonisation

The theoretic and fiscal basis is for tax to be imposed on *all* kinds of consumption taking place on EU territory. Consequently, a directive was adopted on the common system of VAT — the VAT Directive (Directive 2006/112/EC) — to ensure *harmonisation* of VAT taxation within the EU. One related important area in which there is no full harmonisation is the area of VAT rates.

Member States are required to apply a standard rate of at least 15% and may also apply one or two reduced rates of at least 5% for certain fixed supplies, including the supply of food, provision of accommodation, etc. In the directive, there are also a number of exceptions which in practice mean that there may

actually be a difference of up to 25% in VAT rates between Member States.

The theoretical view is, therefore, that all VAT rates being lower than the highest VAT rate constitute a relief in principle. Against this background, the existing VAT exemption with respect to the consumption on board ferries (and aeroplanes and trains) is not a rare sight. Such a relief also exists in the individual Member States (differentiated VAT rates) and between the individual Member States (in connection with differences in VAT rates).

It is also an established fact that consumers move their purchases from their home country to other Member States for financial reasons or, for the same reasons, omit to do so because of differences in the VAT rates. This practice has been ongoing to a far greater extent and with larger socioeconomic and occupational impacts than the relatively minimal impact that VAT exemption on the supply of goods and services for consumption on board has on the national economy.

It should be noted that the Danish Ministry of Taxation in its report on cross-border trading, the 2010 version, establishes a significant growth in land-based cross-border carriage of passengers, whilst the overall number of passengers on board ferries to/from Denmark has been declining for a number of years.

Irrespective of the kind of VAT taxation method applied, it is a recognised fact that the consumption in accordance with general consumer behaviour would move to the place of lowest taxation. This was also the conclusion of the European Commission when abolishing the VAT-exempt sale of goods in connection with disembarkation on 1 July 1999.

4. Domestic and non-EU services, specific comments

With regard to domestic services we see a clear need for the options that do not entail taxation in that country to be supplemented by additional corrective measures. Since these are not described in the matrix, we have not rated these options but added some verbal comments.

Finally, with regard to the non-EU services, we assume that taxation is only envisaged in national waters and that the present practical interpretations made by Member States regarding when national waters have been left will be maintained.

We hope that you will find these comments and the completed matrix useful for

the purposes of this exercise. Should you have any questions regarding this letter or the matrix, please feel free to contact us.

Yours sincerely,

Jacob K. Clasen
Kontorchef / Head of Division
Danmarks Rederiforening / Danish Shipowners' Association
Tel: +45 33 11 40 88 / Direct: +45 33 48 92 14
Fax: +45 33 11 62 10
Web: www.shipowners.dk

[\[1\]](#) Report of 30 May 2006 on items for the ECOFIN meeting of 7 June 2006, referring to Directive 2008/8/EC.

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