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signed by Mr Jordi AYET PUIGARNAU, Director

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to: Mr Uwe CORSEPIUS, Secretary-General of the Council of the European  
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of taxation of the supply of goods and the supply of services, including  
restaurant services, for passengers on board ships, aircraft, trains or buses  
drawn up in accordance with Article 37(3) of Council Directive  
2006/112/EC of 28 November 2006 on the common system of value  
added tax

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## **REPORT FROM THE COMMISSION TO THE COUNCIL**

**on the place of taxation of the supply of goods and the supply of services, including restaurant services, for passengers on board ships, aircraft, trains or buses drawn up in accordance with Article 37(3) of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax**

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### TABLE OF CONTENTS

1.	Background and scope of the report.....	3
2.	Description of the current rules governing the supply of goods and services carried out on board means of transport.....	3
2.1.	Necessity of particular rules for supplies of goods and services carried out on board means of transport.....	3
2.2.	Place of supply .....	4
2.3.	Exemption for on board supplies .....	5
3.	Main problems identified .....	5
3.1.	Implementation and understanding of certain concepts.....	5
3.1.1.	Concept of ‘the Community section’ of a passenger transport effected in the Community.....	6
3.1.2.	Treatment of "stopovers" .....	6
3.1.3.	Concepts of 'consumption on board' and 'restaurant and catering services'.....	6
3.2.	Services other than catering and restaurant services.....	7
3.3.	Scope of the exemption applied .....	7
3.4.	Particular issues highlighted by stakeholders .....	8
3.5.	The specific situation of supplies performed on board cruises .....	8
4.	The way forward .....	9

## **1. BACKGROUND AND SCOPE OF THE REPORT**

In accordance with Article 37(3) of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax<sup>1</sup> (hereinafter: 'VAT Directive') *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.*

Council Directive 2008/8/EC of 12 February 2008<sup>2</sup> (which amended the VAT Directive in particular on the rules on the place of supply of services), was accompanied by the following minutes statement: *"The Council and the Commission agree that this proposal is without prejudice to the review provided for in Article 37 of Directive 2006/112/EC of 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. This duty to review shall also explicitly cover services provided on board ships (including cruise ships), and shall also extend to the new rule determining the place of supply as laid down in Article 57 of Directive 2006/112/EC."*

This report focuses on the place of taxation of goods for consumption and of services, including restaurant services, supplied to passengers on board ships, aircraft or trains. However, in order to complete the picture of that segment of the market, it also addresses other issues such as the treatment of take-away goods supplied on board, supplies on board buses, as well as exemptions currently applied in this sector.

In preparing this report, the Commission took various steps to create the broadest possible overview of the situation in the sector. First of all, businesses that are active in this sector were invited to give their assessment of the current situation, including the problems they face and suggest possible solutions for the future. Member States were also invited to outline their current practices and their expectations in this field. Finally, an expert study (hereinafter: 'the expert study') was conducted by an external contractor<sup>3</sup> (published with this report).

## **2. DESCRIPTION OF THE CURRENT RULES GOVERNING THE SUPPLY OF GOODS AND SERVICES CARRIED OUT ON BOARD MEANS OF TRANSPORT**

### **2.1. Necessity of particular rules for supplies of goods and services carried out on board means of transport**

The nature of supplies of goods and services as such is the same, whether or not they are carried out on board. However, for goods and services supplied on-board means of transport, their physical place of supply is changing, as the supply takes place on a 'platform' which is normally moving from one place to another. In other words, the goods and services are not transported in order to be supplied, but are supplied while moving.

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<sup>1</sup> OJ L 347, 11.12.2006, p. 1

<sup>2</sup> OJ L 44, 20.2.2008, p. 11

<sup>3</sup> "Expert study on the issues arising from taxing the supply of goods and the supply of services, including restaurant and catering services, for consumption on board means of transport", of 8 February 2012 undertaken by PricewaterhouseCoopers.

Therefore, because of those special circumstances under which on-board supplies are performed, particular rules apply. Their aim is to ensure to the extent possible taxation where consumption takes place, without making the application of these rules overly complex.

Particular rules are justified, but it should be emphasized that although on-board supplies take place in a particular environment, when supplied within the territory of the EU, the actual consumption to which they give rise is on its territory and, as a matter of principle, they should not be treated differently for taxation purposes in comparison to the same supplies performed elsewhere in the EU.

## 2.2. Place of supply

Under Articles 37(1) and 57(1) of the VAT Directive, the place of supply of goods and catering and restaurant services supplied on board ships, aircraft or trains during "*the section of a passenger transport operation effected within the Community*" shall be deemed to be at the point of departure of the passenger transport operation.

According to Articles 37(2) and 57(2), 'the section' (hereinafter: 'the Community section') is defined as "*the section of the operation effected, without a stopover outside the Community, between the point of departure and the point of arrival of the passenger transport operation*". The 'point of departure' means "*the first scheduled point of passenger embarkation within the Community, where applicable after a stopover outside the Community*". The 'point of arrival' means "*the last scheduled point of disembarkation within the Community of passengers who embarked in the Community, where applicable before the stopover outside the Community*". It means that part of the journey of the means of transport between the EU border and the first scheduled point of passenger embarkation within the Community takes place outside 'the Community section'. The same situation occurs for part of the journey between the last scheduled point of passenger disembarkation and the EU border.

A 'stopover' means a stop which is not a scheduled point of passenger embarkation or disembarkation<sup>4</sup>.

Article 37(1) and (2) applies to all goods supplied on board ships, aircraft or trains, whether or not for consumption on board, during the Community section. Article 57 only applies to restaurant and catering services physically carried out on board ships, aircraft or trains. For other services supplied on board, no particular rules are laid down.

For goods supplied on board, but outside the Community section, Article 31 of the VAT Directive is applicable. According to this provision, *where goods are not dispatched or transported, the place of supply shall be deemed to be the place where the goods are located at the time when the supply takes place*. Article 31 also applies in the case where goods are supplied on board other means of transport, such as buses.

For catering and restaurant services supplied on board, but outside the Community section, Article 55 of the VAT Directive applies. According to this provision "*the place of supply of catering and restaurant services other than those physically carried out on board ships, aircraft and trains during the section of passenger transport operation, effected within the Community, shall be where the services are physically carried out*".

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<sup>4</sup> The question of how the notion of "the stop" should be understood was developed in more detail by the Court of the European Union in its judgment of 15 September 2005 in case C-58/04, Antje Köhler v Finanzamt Düsseldorf-Nord.

### 2.3. Exemption for on board supplies

In accordance with Article 37(3) of the VAT Directive "*pending the adoption of the proposals (...), 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 (...)*" ships, aircraft and trains when those goods were supplied during the Community section.

This provision only allows exemption for goods supplied for consumption on board and does not extend to goods to be taken away by passengers. Supplies on board other means of transport, such as buses, are not covered and can therefore not benefit from exemption.

No exemption is provided for services consumed on board, such as catering and restaurant services. However, Article 371 and Annex X, Part B, point 10, of the VAT Directive does allow Member States to continue to exempt "*the transport of passengers and, in so far as the transport of the passengers is exempt, the transport of goods accompanying them, such as luggage or motor vehicles, or the supply of services relating to the transport of passengers*". This is a standstill provision that can be maintained until the definitive arrangements are adopted, and is available only for Member States having applied it on 1 January 1978 or for Member States which acceded the Union after that date, having obtained a specific derogation upon accession (see Articles 375 to 390b). Whilst it can be argued that catering and restaurant services could be exempted on the basis of this standstill provision, other services, such as hairdressing services during cruises, cannot qualify as being "services related to the transport of passengers".

## 3. MAIN PROBLEMS IDENTIFIED

One of the main problems identified is the divergence of application between Member States. It is apparent that exemptions are applied differently by Member States and that some rules are not entirely respected or are understood differently. The expert study has highlighted practical problems put forward by stakeholders<sup>5</sup>. The difference in application is the main cause of complexity, and results in an increase in administrative burdens for business. Failure to harmonise exemption can also create distortions of competition.

### 3.1. Implementation and understanding of certain concepts

Problems have been identified with certain concepts to be found in Articles 37 and 57 of the VAT Directive. Notwithstanding existing definitions, certain Member States are applying these concepts in different ways. It appears that ships and aircraft on international routes are especially concerned.

In particular, it appears that there are situations where the national provisions implementing Articles 37 and 57 do not cover all three means of transport (ships, aircraft and trains).

For buses, the legal provisions are correct in all Member States. However, there are some doubts about their correct application in practice and how they can be controlled.

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<sup>5</sup> For detailed information, see chapter 4 of the expert study – in particular pages 48-50, 55 and 58.

### 3.1.1. *Concept of 'the Community section' of a passenger transport effected in the Community*

In at least three Member States the definition of the Community section is not entirely clear<sup>6</sup>. Typically certain elements of the definition are missing – for example, there is no definition of the point of departure and/or the point of arrival or the definition used is only a partial one. In one Member State there is no definition of the Community section at all.

In five Member States the onboard supply of goods and services is taxable to a different extent outside their territory, regardless of where – inside or outside the Community section – they should have been taxed in accordance with the rules<sup>7</sup>.

Council Implementing Regulation (EU) No 282/2011 (hereinafter: 'VAT Implementing Regulation')<sup>8</sup> has provided some clarification, but this differentiation remains complicated and leaves the door open to misinterpretation and inconsistency.

### 3.1.2. *Treatment of "stopovers"*

Divergences are observed between Member States in relation to the treatment of stopovers in comparison to the first point of embarkation or the last point of disembarkation of passengers within the EU. In at least ten Member States, the dividing line seems not to be correct.<sup>9</sup> According to the expert study, some Member States consider that when passengers can get off of a means of transport to visit a place and, after this excursion, get back on board to continue their journey, this is regarded as disembarkation and embarkation of passengers. This concerns the cruise industry in particular.

If no new passengers can get on and none of the passengers on board can permanently leave the ship, this should not be regarded as embarkation or disembarkation. Such a situation must be regarded instead as a stopover. Where a stopover is treated as a first point of embarkation or a last point of disembarkation, this may give rise to difficulties, where – because of varying interpretations of the Community section – more than one Member State wants to tax the same supplies.

Finally, the treatment of unscheduled stopovers might give rise to types of difficulties similar to those described above. However, the expert study does not gather any information on that point.

### 3.1.3. *Concepts of 'consumption on board' and 'restaurant and catering services'*

The expert study identified certain problems with these concepts.

Consumption on board: There is no definition in the VAT Directive, and only a few Member States have provided official guidance, which varies from one Member State to another.

Catering and restaurant services: A clear definition has only been available since 1 July 2011<sup>10</sup>. Prior to that, the understanding of this concept was based on guidance provided by the

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<sup>6</sup> Look chapter 4 of the expert study, in particular pages 39-40 and 42-43.

<sup>7</sup> Look chapter 4 of the expert study, in particular pages 42-43 and 52-55.

<sup>8</sup> See in particular Articles 35 to 37.

<sup>9</sup> Look chapter 4 of the expert study, in particular pages 40 and 42-43.

<sup>10</sup> According to Article 6 of the VAT Implementing Regulation, "Restaurant and catering services mean services consisting of the supply of prepared or unprepared food or beverages or both, for human

Court of Justice of the European Union (hereinafter: 'CJEU'), in particular by its judgment in the *Faaborg-Gelting Linien* case<sup>11</sup>. The concept was further developed in the *Bog* case<sup>12</sup> in respect of which the CJEU gave a ruling on 10 March 2011, where it was specified in more detail what should be the level of sufficient support services to recognise the supply as a catering service. Subject to these developments, the problems of definition should be minimised. However, one cannot rule out the possibility that further clarification will be needed, particularly in order to align the VAT Implementing Regulation with the recent case law.

### 3.2. Services other than catering and restaurant services

As only catering and restaurant services are covered by Articles 55 and 57 and taxed in accordance with the particular rules described above, all other services should be treated in the same way, whether or not they are provided on board means of transport. Some questions have arisen, particularly with regard to services provided to a person (such as hairdressers, beauticians...), but it has not as yet been possible to clearly identify those services for which a particular rule would be necessary.

### 3.3. Scope of the exemption applied

One group of Member States exempts goods for consumption on board ships, aircraft or trains as provided for in Article 37(3) of the VAT Directive. However, at least two Member States also allow exemption of on-board supplies of goods made whilst within the territory of the Community, but outside the Community section, which is not authorised by Article 37(3) of the VAT Directive<sup>13</sup>.

Furthermore, it appears that eight Member States also exempt services supplied to passengers on board ships, aircraft or trains, in particular restaurant and catering services<sup>14</sup>. The Commission considers that Article 37 only allows an exemption of the supply of goods for consumption on board ships, aircraft or trains carried out during the Community section. The exemption provided for in Article 37 does not cover goods which are to be taken away, or any services. Exemption in such cases is only possible pursuant to Article 371 and Annex X, Part B, point 10, which allow Member States to continue to exempt "*in so far as the transport of passengers is exempted, [...] the supply of services relating to the transport of passengers*". It appears that five Member States exclude on-board supplies from any taxation to a different extent through the way in which the place-of-supply rules are applied<sup>15</sup>. They consider those supplies to be outside the territorial scope of VAT. As a result they do not require any specific rules to provide for exemption.

The incorrect application of the rules on the territorial scope of VAT or of the exemption only seems to concern ships and aircraft. For trains and buses, the rules seem to be implemented

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consumption, accompanied by sufficient support service allowing for the immediate consumption thereof. The provision of food or beverages or both is only one component of the whole in which services shall predominate. Restaurant services are the supply of such services on the premises of the supplier, and catering services are the supply of such services off the premises of the supplier."

<sup>11</sup> Case C-231/94, judgment of the CJEU of 2 May 1996, *Faaborg-Gelting Linien a/s v Finanzamt Flensburg*.

<sup>12</sup> Joined cases C-497/09, C-499/09, C-501/09, C-502/09, judgment of the CJEU of 10 March 2011, *Bog and Others v Finanzamt Burgdorf, Hamburg-Barmbek-Uhlenhorst, Minden and Detmold*.

<sup>13</sup> Look chapter 4 of the expert study, in particular at pages 52 and 53.

<sup>14</sup> Look chapter 4 of the expert study, in particular at pages 54 and 55.

<sup>15</sup> Look chapter 4 of the expert study, in particular at pages 42-43 and 52-55.



correctly in all Member States. The divergence in actual taxation between Member States is seen as one of the main problems with the current situation, as it can have serious implications for the businesses concerned and distorts competition, especially between competitors established within the EU and outside the EU.

### **3.4. Particular issues highlighted by stakeholders**

The stakeholders who were consulted stressed that the current legal framework is complex (as it requires the application of different sets of rules – Articles 31 and 55 or Articles 37 and 57 – within the EU) and varies from one Member State to another. The various exemption schemes, although greatly appreciated, are applied differently by Member States and this is seen as a complication. Not surprisingly, a harmonised exemption is the preferred option.

Stakeholders also underlined the lack of clear-cut definitions as a cause of serious difficulties, in particular when a business operates in more than one Member State, which is normally the case in this sector. The divergent rates applicable were also mentioned.

Stakeholders highlighted the difficulties that they encounter when making onboard supplies of goods or services for which they are liable to pay VAT in a Member State where they are not established and have to register for VAT purposes. They pointed to difficulties linked with differences between Member States concerning technical requirements for cash registers and obligations, VAT rates and different currencies.

These difficulties are no different from those encountered by any other business liable to pay VAT in a Member State where it is not established, and stakeholders regret that there are no simplifications or schemes, like a one stop shop (OSS), available to them.

Some stakeholders admitted that they register in some Member States only, and not in all Member States in which they would be required to do so under the current provisions.

### **3.5. The specific situation of supplies performed on board cruises**

The particular feature of the cruise industry is that cruises often start and end in the same harbour. Therefore it seems that the prime purpose of a cruise journey is not to transport passengers from one place to another. Further, the itinerary of a cruise ship may vary and is more flexible compared to other means of transport.

During the process of collecting information on the current state of play in relation to on-board supplies, the cruise and ferry industry was the most active in terms of its response. That industry emphasized that, for its activities, the rules are particularly complicated and suggested that all on-board supplies of goods and services should be exempted.

On board cruise ships, a wider variety of goods and services are available than is the case for other means of transport. For example, services such as those of hairdressers, tailors, beauticians, entertainment and educational activities are on offer. The variety of goods is also much broader.

The cruise industry emphasized that there is strong competition between operators in that segment of the market. The way in which rules are formulated influences the competitive position, especially between competitors established within the EU and outside the EU.

During the process of consultation it was suggested that, for cruises, the boat could in many cases be considered to be a fixed establishment, as the supplies performed are complex and frequently require sophisticated arrangements<sup>16</sup>.

#### 4. THE WAY FORWARD

The goods and services covered by this report are typical consumer products on which VAT is normally charged when they are supplied within the territory of the EU. As a matter of principle, the fact that the same goods and services are supplied on board certain means of transport cannot be a sufficient justification for exempting those supplies within the EU from VAT.

This report is not presented as such in the framework on the VAT strategy set out in the Commission's Communication on the future of VAT. Nevertheless, the future treatment of the transactions involved should be consistent with the guiding principles of that strategy, in particular the need to increase the efficiency of the tax by broadening the tax base, but also the need for simple rules.

Given that the main purpose of VAT is to raise revenues and to tax consumption, the Commission is of the opinion that the actual taxation of supplies of goods and services taking place on board of means of transport should be an objective to be pursued in the future. Removing the exemption would also be in line with the need to make the tax systems more efficient. Preparing for the future work to be undertaken in that field, the Commission is aware that in the expert study almost all consulted stakeholders (in particular representatives of the cruise industry), who replied to the survey sent to them by the contractor of the study, indicated that it is desirable for them to keep the optional VAT exemption, as they fear a negative economic, social and environmental impact.

The Commission also acknowledges stakeholders' complaints about the complexity of the current situation. This complexity stems from the divergent application and interpretation of the current rules, the legal framework itself and the burden of administrative compliance resulting from the two previous factors, notably (i) the patchwork of exemptions, (ii) the definition of 'the Community section', (iii) the definition of restaurant and catering services, and (iiii) the understanding of notions of 'stopover' and 'non-scheduled stops'. In this respect, the Commission will verify which kind of clarifications could be agreed with Member States in order to address the current uncertainties. The VAT Committee could be used in this respect in order to reach common guidelines.

The Commission will also examine further the situation in order to assess if infringement procedures should be undertaken for some Member States.

Even if the abovementioned complexities can be solved, it is questionable whether the current rules laid down in the VAT Directive are satisfactory for ensuring the taxation of the transactions at stake in a simple, efficient and robust way. In the view of the Commission, the application of these rules would still be complex for businesses and, in many cases, difficult or even impossible to control for tax authorities.

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<sup>16</sup> It should be noted that the concept of a fixed establishment is defined in Article 11 of the VAT Implementing Regulation.

In the Commission's view, a change in the taxation of supplies on board means of transport giving rise to consumption in the EU cannot be achieved for the supplies on board alone, without putting these questions in the broader perspective of the design of a simpler and more neutral VAT framework for passenger transport activities in general.

In order to ensure such consistency, a legislative proposal in this field should be adopted, together with the proposals that will be made for passenger transport activities, following a comprehensive impact assessment

These proposals should ensure that the actual taxation of the supplies on board means of transport is simple and neutral.

Moreover, there is an acute need to make the rules less complex than is currently the case, and the obligations to be fulfilled by the operators should also be as light as possible. However, everything depends on the choice that will be made on the taxation system as such.

If the rules adopted mean that operators are liable to pay tax in Member States where they are not established, the case for a form of one stop shop (OSS) to simplify compliance would clearly have to be examined.

As the Communication on the future of VAT pointed out, such a measure could only be considered after 2015, based on the experience from the mini one stop shop (MOSS) that will be implemented for telecommunications, radio and television broadcasting and electronic services supplied by non-established suppliers to non-taxable persons (final consumers).

The Commission is of the opinion that the issues linked with supplies on board means of transport should be addressed in conjunction with the passenger transport activities where, in accordance with the Communication on the future of VAT, a more neutral and simpler VAT framework for passenger transport activities will be proposed<sup>17</sup>. First of all these issues are closely related and, secondly, the types of challenges and difficulties being faced are similar.

The Commission therefore considers that it is not opportune to accompany the present report with specific legislative proposals.

The Council is invited to express its views on the content of this report and, in particular, on the way the Commission suggests to take this file forward.

At the same time, other institutions are welcome to give their opinion on this report and the suggested way forward, if they wish to do so.

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<sup>17</sup> See COM(2011) 851 action n°9