

## January 2004

### This Year, Sometime Soon: Changes to Place of Taxation of Services Rules



A good part of the European Commission's "VAT Strategy" that it launched in December 2000 was implemented in 2001-2003.

The focus has now turned to perhaps the most fundamental change yet: the rules relating to the place of supply of services for VAT purposes. These are the rules that determine the country that has jurisdiction to collect any tax.

On 23 December 2003, the Commission presented its proposal to change these rules, together with a draft directive to bring the changes into effect. This proposal would reform only the rules where the customer is a taxable trader - i.e. B2B supplies. The Commission expects its proposal to become law before 1 May 2004, ahead of EU enlargement.

So what would the change involve and how would it affect yachting services providers?

Under the present VAT place of supply rules, services are taxed on the basis of where the supplier is established unless they are specifically defined as being taxed somewhere else. In this regard, a number of exceptions to the general rule exist. These exceptions (e.g. for immovable property, transport services, etc.) cause the place of taxation to change depending on the nature of the supply.

The proposed directive would shift taxation for services provided to taxable persons from where the supplier is established to where the **client** is established. A number of exceptions to this general rule would still be maintained, but these exceptions would be clearly linked to special features that make determination of the place of taxation administratively straightforward.

The overall effect of such a change to service providers across the Community would be to limit the instances whereby a supplier would be required to register for VAT purposes when performing services in a Member State other than where he is established. And it would increase the reliance on the reverse charge mechanism where a taxable

person receives services from a person not established in the same country.

A twofold direct impact on yachting services results:

First, a different treatment would apply to long-term hiring or leasing of yachts. 'Long-term hiring or leasing' is defined to mean "an agreement that provides continuous possession or use of movable property for a period of more than 30 days". This would be taxable where the business **client** is established. But where, for example, a taxable person hires a yacht for business use for a period of five days, the place of supply would be where the **supplier** is established.

Second, although the rules for the taxation of passenger transport services have not been changed in this first phase of the reform, the Commission has stated: "The existing [passenger transport services] provisions cause problems and therefore [the Commission] proposes to address this issue in its subsequent evaluation of B2C supplies."

### Yachting in the "VAT Gap"

Consider this familiar example:

A company, established in Member State A, operates a yacht for a charter in Member State B. Member State B treats the charter transaction as 'hire of a means of transport', which it zero-rates under current VAT rules, because the transaction is taxable in Member State A where the yacht operator belongs. Member State A, on its part, treats the same charter as the supply of 'passenger transport', and also zero-rates because this is taxable in Member State B where the charter takes place.

The yacht operator can take advantage of a "VAT gap". The gap is afforded by the scope of the law as it stands in different Member States. And it would appear, from its stance on the recent Cookies World case concerning differing treatment in Austria and Germany, that the Commission currently views such cross-border arbitrage as permissible.

But, what if Member State B above discovered (through the 'VIES' system) that Member State A had not charged VAT? And then used the existing provisions of Article 9(3) of the Sixth Directive to claw back the VAT from the yacht operator?

*This bulletin is prepared by Moore Stephens Consulting (Isle of Man) Limited. Yachting VAT Note is designed to keep readers abreast of current developments. But it is a general guide only and is not intended to be comprehensive. No liability is accepted for the opinions it contains, or for any errors or omissions. In all cases you should seek professional advice specific to your circumstances.*

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