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**GROUP ON THE FUTURE OF VAT**

**GFV No 125**

**Review of the VAT rules applicable to travel and tourism sector**

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## **1. INTRODUCTION**

The Commission announced in the “Action Plan for fair and simple taxation to support the recovery strategy”<sup>1</sup> its intention to assess and revise the special VAT scheme for travel agents and the VAT rules on passenger transport. Furthermore, with a view to broadly supporting the travel and tourism sectors, hard hit by Covid-19 restrictions, a revision of the VAT exemption regime for non-EU travellers and duty-free rules is being considered.

The functioning of the current VAT rules applicable to the travel and tourism sectors has been assessed on separate occasions. This initiative in particular builds on the evaluation<sup>2</sup> of the special scheme for travel agents published in 2021 and on a public consultation<sup>3</sup> carried out specifically on that subject in 2020. Furthermore, it takes into account the 2014 study<sup>4</sup> on the economic effects of the VAT rules for passenger transport, and the outcome of the work of a FISCALIS Project Group that examined the implementation of the VAT exemption to non-EU travellers in 2017.

The assessment carried out so far has revealed the need to reconsider the overall VAT regime applicable to travel and tourism in a comprehensive manner. Overall, the VAT rules applicable to the travel and tourism sectors are not fit for the digital market of travel services. Digital technologies have radically transformed the sectors creating new business models (e.g., online travel platforms, digital refund systems) that both pose challenges and offer opportunities for tax administrations and businesses, such as new possibilities to facilitate VAT compliance.

Given both the importance of travel and tourism for the EU economy and the hit from the pandemic, the Commission will assess the possible need for a legislative VAT package that would focus on three interlinked sets of provisions of the [VAT Directive](#):

1. Special VAT scheme for travel agents (Articles 306-310),
2. VAT rules on passenger transport (Articles 48 and 148), and
3. VAT exemption on the supply of goods to non-EU travellers (Articles 146, 147 and 158).

The objectives of the initiative are to address the distortions arising from the current VAT rules and provide the sector with modernised rules based on fair, simple and more efficient taxation. Any future proposal will also aim at ensuring a more uniform application of the VAT rules applicable to travel and tourism services, while adapting regulations in place to the digital dimension of the travel and tourism market, as well as to the objective of promoting greener passenger mobility.

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<sup>1</sup> COM(2020) 312 final of 15 July 2020.

<sup>2</sup> Commission Staff Working Document – Evaluation – Special Scheme for travel agents of the Council Directive 2006/112/EC on the common system of value added tax ([SWD\(2021\) 32](#) of 17.2.2021) accompanied by an executive summary ([SWD\(2021\) 33](#) of 17.2.2021)

<sup>3</sup> [Results](#) of the Public Consultation.

<sup>4</sup> [Study](#) on the economic effects of the current VAT rules for passenger transport (Final Report of December 2014, TAXUD/2010/CC/104).

## 2. STUDY

In preparation of this initiative, the Commission services have commissioned an economic study which will provide data and an evidence-based analysis to feed into the Impact Assessment underpinning a possible proposal.

The study covers three parts, any of which will form the subject of a separate assessment:

1. Part 1 – Special VAT scheme for travel agents,
2. Part 2 – VAT rules on passenger transport,
3. Part 3 – VAT refund to non-EU travellers and duty-free shop.

The main objectives of the study are to:

- evaluate the functioning of the current VAT rules applicable to travel and tourism sectors,
- develop options for the simplification and modernisation of the VAT rules applicable to those sectors, and
- analyse benefits and costs, opportunities, and risks, as well as impacts, in respect of each of the options for review, with the expectation that the analysis will feed into preparations for a possible future legislative proposal.

The geographical coverage of the assignment is the EU 27, while field work is carried out on a sample of 13 Member States based on both geographical and project-specific considerations (e.g., tourism destination; international hub). The sample is largely the same across the three Parts of the Study. The only exception is Czechia, in which only Part 3 is covered, and Greece, in which only Parts 1 and 2 are covered. The study will also look at some neighbouring countries (e.g., UK and Switzerland). The sample is shown in the table below.

Sample of Member States	Region	Size	Tourism destination	Number of travel operators	Int. travel hub	Digital refund	Part 1	Part 2	Part 3
Belgium	West	S/M				+	+	+	+
Croatia	Centre-East	S/M	+				+	+	+
Sweden	North	S/M					+	+	+
France	West	L	+	+	+	+	+	+	+
Germany	West	L		+	+		+	+	+
Italy	South	L	+	+		+	+	+	+
Malta	South	S/M	+	+			+	+	+
Poland	Centre-East	L		+			+	+	+
Portugal	South	S/M	+			+	+	+	+
Spain	South	L	+	+	+	+	+	+	+
The Netherlands	West	S/M		+	+		+	+	+

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Greece	South	S/M	+				+	+	
Czechia	Centre-East	S/M				+			+

The contractor<sup>5</sup> completed the targeted consultations which involved tax authorities, VAT experts and business' representatives. The interim report submitted includes a complete analysis of the application of the relevant VAT rules and provides an overview of the main legal issues and discrepancies. For each part, the contractor has also examined the sector and the VAT rules at stake.

The policy options under consideration are presented below and may be adapted following further analysis and feedback. For all the three parts, the options will be assessed against the status quo.

### **3. OPTIONS FOR REVIEW**

#### **3.1 Part 1: Special VAT scheme for travel agents**

Since its introduction in 1977, the VAT special scheme for travel agents has never been updated. The 2021 evaluation identified a number of shortcomings of the special rules, while suggesting the need of a substantial reform. Notably, the application of the scheme by Member States is far from being uniform but is rather fragmented. Furthermore, the place of supply rule in place does not ensure equal treatment between EU and non-EU travel agents organising travels in the EU. These problems lead to legal uncertainty and additional costs for travel operators and mostly create distortions and an uneven playing field in the EU market of travel services.

The main inconsistencies that result from the provisional analysis can be grouped in the following four areas where is it worth considering legal intervention:

- A. Scope of the special scheme. The interim report of the study has confirmed that the treatment of B2B supplies, in particular wholesale supplies and MICE (Meeting, Incentives, Conference and Events) services, is very fragmented across the EU, resulting as the main cause of competitive distortions in the Member States.
- B. Place of supply rule. In most Member States, non-EU travel agents are covered by the special scheme, but their margin is not taxed because of the rule of taxation at the place where the travel agent is established. The price advantage for non-EU tour operators is valued in the study to be around 2-4% of the final price of the travel facility.
- C. Definition of concepts: Despite being mandatory, the concepts of the special scheme (e.g., what falls under the definition of travel facility; when a travel agent is deemed to act in his own name; treatment of mixed supplies) are not clearly defined in the VAT Directive. The different interpretations adopted at national level can be a serious

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<sup>5</sup> A group of consulting firms and research institutions led by Economisti Associati Srl, including Oxford Research AB, Center for Social and Economic Research (CASE), Wavestone, Mazars, TISpt, DALE Conseil and Karl-Heinz Haydl.

concern, in particular for large operators and online travel agents that operate across the EU.

- D. Margin calculation: Article 308 of the VAT Directive, as interpreted by the Court of Justice of the European Union (CJEU), requires that the margin is calculated by each transaction, but this approach is difficult to apply and represents an additional burden which particularly affects micro and small businesses.

The options concerning the scope of the special scheme, Area A, are described in table 1. These options aim at addressing intra-EU distortions deriving from the incorrect application of the scheme and would, as an effect, limit or clarify the scope in line with the current practice in the Member States.

Table 1: Options Area A

Area A: Scope of the scheme	Brief Description
0. Status quo	The scheme applies to all supplies of travel facilities, including B2B, wholesale, MICE, and occasional services
A1. Exclusion of wholesale supplies	The scheme applies only to supplies of travel facilities to travellers (both private and business customers taxable)
A2. B2B optionality	Travel agents may decide whether to apply the scheme to supplies of travel facilities to taxable persons, on a transaction-by-transaction basis
A3. Exclusion of MICE	MICE services to taxable persons are excluded from the scheme unless the organisation of the event is ancillary to the provision of accommodation and transport
A4. Occasional supplies	Supplies of travel facilities when these represent a marginal share of the supplier's turnover (e.g., 1-5%) are excluded from the scheme

The exclusion of wholesale supplies from the scheme would revert to the traveller approach. The B2B optionality would solve the problem of hidden VAT for travel agents' customers and bring the flexibility advocated by the sector. The option that limits the scope of the scheme to cover only B2B services other than MICE services is more coherent with the current situation. Finally, the treatment of incidental supplies under the normal VAT rules would bring further simplification for businesses (e.g., holdings, hotels, other service providers) carrying out activities that are very different from those of travel agents.

The options concerning the place of supply rule, Area B, are described in table 2. These options would aim at removing the competitive disadvantage faced by EU travel agents and ensure fair taxation of all travel services enjoyed in the Union. Depending on the option, there would be costs, benefits and trade-offs that need to be assessed.

Table 2: Options Area B

Area B: Place of supply	Brief Description
0. Status quo	Travel facilities remain taxed at origin and margins of non-EU travel agents are not taxed.
B1. Place of traveller’s residence (only non-EU travel agents)	The place of supply of travel facilities by non-EU travel agents becomes country of residence of the travellers. The status quo remains for EU travel agents.
B2. Place of destination (only non-EU travel agents)	The place of supply of travel facilities by non-EU travel agents becomes the country in which the travel takes place. The status quo remains for EU travel agents.
B3. Place of Traveller’s residence (all travel agents)	The place of supply of travel facilities by any travel agent (EU and non-EU) becomes the place of residence of the traveller.
B4. Place of destination (all travel agents)	The place of taxation of travel facilities by any travel agent (EU and non-EU) becomes the place where the travel takes place.

The place of the traveller’s residence, for instance, would reduce the tax base (as services taking place in the Union and sold to non-EU residents would not be taxed) but would promote the attractiveness of EU as a tourist destination. Conversely, taxation at destination would have a positive effect on the revenue but would increase the administrative burden. With regard to options B1 and B2, which suggest a change only for non-EU operators, the compatibility with rules of the World Trade Organisation will need to be assessed. On the other hand, options B3 and B4 could ensure equal treatment for all travel agents, but would remove the current simplification for EU-established operators linked to taxation at origin and generate VAT revenue shifts.

Any change in the place of supply rule would in any event require, including also for B2B transactions, the implementation of compliance and enforcement mechanisms for non-EU operators, similar to the existing One-Stop Shop (OSS) arrangements but adapted for the special scheme.

The policy elements concerning the definition of concepts used for the special scheme, Area C, are described in table 3. These elements could result in implementing measures that could increase legal certainty and improve harmonisation. Based on Member States’ practice, two alternative approaches are proposed, which may result in a narrower or broader scope of the scheme.

Table 3: Policy elements Area C

Area C: Definitions	Approach 1	Approach 2
Agent vs. Principal	Status quo. No definition is introduced.	A list of presumptive behaviours determining when the travel agent is a disclosed agent or principal is introduced (black- and/or white- list).
Travel facilities (services and conditions)	A travel facility consists in a bundle of services that includes at least two of the following items: <ul style="list-style-type: none"> <li>- Accommodation,</li> <li>- Passenger transport,</li> <li>- Other travel services to the benefit of the traveller</li> </ul>	A travel facility consists in a bundle of services that include at least two touristic services, listed in the Implementing Regulation (i.e., no obligation for either accommodation or transport to be required)
MICE	Status quo. MICE fall within the scope of the scheme if the event organisation is supplied together with accommodation or transport.	Event organisation is not considered a travel facility, unless it is ancillary/marginal to the provision of transport or accommodation
Single item	Any service supplied as single item is out of scope	Accommodation supplied as single item is covered by the scheme
Mixed supplies	The scheme only applies to bought-in services. In-house services are not covered must be invoiced separately.	Mixed supplies are covered; the margin is apportioned based on market value or, if not available, on a cost-basis.

The options concerning the margin calculation are described in table 4. These options would largely consolidate the current practice. A linked issue to be taken into account is the treatment of payments on account, as ruled by the CJEU<sup>6</sup>. Businesses are in general not able to calculate margins at the time the advanced payment occurs, except for large travel operators with specialised IT software. The study will assess the impact of offsetting negative margins.

Table 4: Options Area D

Policy options	Brief Description
0. Status quo	Margin is calculated per each transaction and VAT is chargeable on receipt of payments on account
D1. Mandatory global margin	Margins must be calculated via a global approach annually with ex-port adjustments; VAT becomes chargeable on the date of commencement of the travel facility
D2. Optional global margin	Travel agents can decide whether to use a global or transaction-by-transaction approach to the calculation of margins; VAT becomes chargeable on the date of commencement of the travel facility

### 3.2 Part 2: VAT rules on passenger transport

The VAT rules on passenger transport services are in part difficult to apply and thus likely to create distortions in the internal market and lead to the widespread application of VAT

<sup>6</sup> C-422/17, Skarpa Travel.

exemptions (e.g., on international flights) which contrast with the objectives of the “Fit for 55” package. These rules are also a source of complexity for transport service providers given that a wide range of reduced rates apply across the EU.

The following options have been identified as a way to address these issues:

**Options 1a and 1b** would, respectively, make the place of supply either the country of departure (i.e., the country where a passenger begins his / her trip<sup>7</sup>) or the country of destination (i.e., the country where the trip ends for a passenger).

**Option 1c** would divide the place of supply evenly between the Member States where an international transport service takes place. For the hypothetical rail journey from Denmark to France via Germany, this would mean that one third of the supply would be made in each of these three countries.

A final **Option 1d** would not change the place of supply rules as such, but rather relates to VAT registration requirements for non-established suppliers. In order to alleviate the problem whereby transport service providers (especially relatively small bus and coach companies) need to obtain multiple VAT registrations, this option would entail extending the scope of the OSS to allow its use also for B2B transactions and to reclaim deductible input VAT through the OSS mechanism.

**Option 2a** would entail introducing modifications to the wording of Article 148 so as to increase legal certainty and uniformity of practices between Member States where needed. This could be implemented either as the only option from this policy element to form part of a final policy package, or together with Option 2c, which would involve expanding the scope of the exemptions provided for under Article 148. Indeed, the changes to be made would depend on which types of transport services would be exempt.

**Option 2b** would only be implemented in conjunction with Options 3b and 3c (described below), and entail abolishing the exemptions for input supplies related to any transport services that would no longer be exempt.

In contrast, **Option 2c** would extend the exemptions for corresponding input supplies to all international passenger services.

**Option 3a** would eliminate any distortions and discrepancies identified by zero-rating all international transport services supplied in the EU. This would take VAT out of the equation for land transport, placing rail and bus and coach companies on a level playing field with airlines (and maritime transport, for a limited number of routes).

**Option 3b** would take the opposite approach, seeking to increase uniformity of treatment and pursue green policy objectives by *increasing* the proportion of services that is taxed. To avoid disturbing international agreements or the competitiveness of the EU travel and tourism sector, it would focus on intra-EU services. Rather than standard VAT rates (which would be out of line with most Member States’ approaches), it would entail taxing all such services at a

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<sup>7</sup> One could also consider defining the country of departure as the country where the physical transport starts. However, this could create complications, e.g. passengers taking a domestic service on a transport that passes through several countries would need to pay VAT in a country that they have not visited as part of the trip.



minimum rate – for analytical purposes, it is proposed that minimum rates of both 8% and 3% be considered.

Finally, **Option 3c** would prioritise environmental considerations by taxing passenger transport services at different rates depending on their environmental impact. In practical terms, it is proposed that this be done by only allowing the application of reduced VAT rates to services meeting certain criteria (in terms of e.g., volumes of carbon emitted per passenger kilometre). All domestic and intra-EU services not meeting the criteria (with exceptions for services where greener alternatives are unavailable) would then be subject to the standard VAT rate of the Member State of supply.

The options identified in the different policy elements could be combined into distinct packages that could form a final policy choice. Four such packages are summarised below.

**Policy packages for the VAT rules on passenger transport**

<b>Policy package</b>	<b>Options included</b>	<b>Overview</b>
Package 1: Administrative simplification	<ul style="list-style-type: none"> <li>- 1a, 1b or 1c on the place of supply rules, and / or</li> <li>- 2a on clarifying the definitions of Article 148</li> </ul>	<p>While avoiding major changes to the current VAT treatment of passenger transport, this package would aim to address issues related to legal certainty and compliance. Versions of this package will be examined composed of only policy element 1 and policy element 2, or a combination of elements.</p> <p>Aside from any benefits that would be realised in the short term, implementing Options 1a or 1b (which make the place of supply either the country of departure or destination, respectively) would also make it easier to consider taxing intra-EU air and sea services in the future.</p>
Package 2: Exempt international services	<ul style="list-style-type: none"> <li>- 2a on clarifying the definitions of Article 148, and</li> <li>- 2c on increasing the scope of the exemptions in Article 148, and</li> <li>- 3a on zero-rating (exemption with credit) all international transport services supplied in the EU</li> </ul>	<p>The purpose of this package would be to level the playing field by essentially giving all international transport services the VAT treatment currently enjoyed by the air and sea sectors. Since this would make it harder to justify the exemptions on input supplies only on air and sea transport, this would be combined with Option 2c on increasing the scope of these exemptions. Clarifications of the definitions (Option 2a) would also be important to ensure a common understanding of which input supplies would and would not be covered.</p>

<b>Policy package</b>	<b>Options included</b>	<b>Overview</b>
Package 3: Taxed intra-EU services	<ul style="list-style-type: none"> <li>- 1a or 1b on the place of supply rules, and</li> <li>- 2a on clarifying the definitions of Article 148, and</li> <li>- 2b on reducing the scope of the exemptions in Article 148</li> <li>- 3b on taxing all intra-EU passenger transport services at a minimum rate (either 8% or 3%)</li> </ul>	The crux of this package would be to tax all intra-EU passenger transport services, including those international air and sea services that are currently exempt with credit. Implementing this in practice would necessitate simplifications to the place of supply rules, either to make the place of supply the country of departure (Option 1a) or destination (Option 1b). In a situation where such outputs were taxed, it would also be difficult to justify the continued exemption for certain input supplies, leading to the inclusion of Option 2b in this package, as well as Option 2a on clarifying the definition of the supplies covered.
Package 4: Green transport promotion	<ul style="list-style-type: none"> <li>- 1a or 1b on the place of supply rules</li> <li>- 2a on clarifying the definitions of Article 148</li> <li>- 2b on reducing the scope of the exemptions in Article 148</li> <li>- 3c on taxing services according to their environmental impact</li> </ul>	To the extent that intra-EU air and sea services are relatively highly polluting, this package would also tax services that are currently exempt, with a view to incentivising the production and consumption of greener transport. As with package 3, this would require flanking measures to enable such services to be implemented in practice, most importantly requiring changes to the place of supply rules, but also with regard to the exemptions for input supplies defined in Article 148.

### **3.3 Part 3: VAT refund and duty-free shop**

VAT export exemption via the personal luggage of a traveller is organised via VAT refund, or via a direct exemption on supplies in duty-free shops.

It would appear from the interim report that the VAT exemption for non-EU travellers is not applied uniformly by Member States. In fact, the current regulatory environment is rather general, leaving room for Member States to adopt dissimilar approaches in a rather uncoordinated way.

Moreover, the national refund procedures may be perceived as burdensome, could be prone to fraud and may restrict market competition (e.g., where particular refund operators are so placed that they play an essential part in the refund system). Particular (control) problems might occur when goods, bought in one Member State, exit via another Member State. Reference is, in this context, to be made to the lack of data sharing between traditional and digitalised systems and the subsequent problems in relation to form validation of tourists that travel through several Member States.

Stakeholders have expressed their interest in extending the legal scope for duty-free shops. This has to be seen essentially in the light of the EU duty-free sales that in particular have

been affected by the consequences of Brexit and the Covid19 pandemic. Ferries and ports with links to the UK could increase their turnover while international stations could not (with the exception of the Shuttle terminal at Coquelles (but not the other Eurostar terminals)). This has also re-started the debate on the need for inbound duty-free shops (upon arrival in the EU) which, however, raises issues of fair competition with high street shops and of compatibility with the overarching principle of taxation in the place of consumption. The expansion of duty-free shops could also conflict with other European policies, such as Europe's Beating Cancer Plan that highlights the pivotal role of taxation in reducing alcohol and tobacco consumption.

In order to address these issues, the study foresees a number of policy options, respectively for VAT refund systems and for duty-free shops, as set out below.

### **VAT refund**

**Option 0** would be the continuation of the status quo. No harmonisation measures would be proposed. Digitalisation would remain at the initiative of Member States and the overall legislative framework would remain fragmented. It would, for example, imply that cross-border validation (in relation to goods bought in one Member State but exiting via another one) would remain limited to confirming that the traveller has left the EU without being able to verify the claim as such. To note that visitors, travelling through different Member States during one trip, account for a much larger share of the market value and, therefore, potentially foregone VAT revenue because of fraud.

**Option 1** would establish interoperability amongst existing national digitalised systems for VAT refunds and ensure mutual recognition of different digital systems by agreeing on minimum common format of contents to exchange information. By establishing interoperability between digitalised systems on the basis of a common data format (i.e., semantic, syntactic, technical, and legal interoperability), the benefits of introducing digitalisation to VAT refunds in terms of fraud prevention and convenience for travellers would be further extended. To note that this option is not considering a fully centralised mandatory EU digital system.

This option might be envisaged with two sub options:

- a. Basic interoperability on voluntary basis
- b. Advanced interoperability setting up a permanent consultative governance mechanism (e.g., a committee chaired by the Commission). Member States could use the committee for discussion of pilot projects, technological innovations, national developments, etc. or for agreeing on guidelines on best practices to, e.g., prevent fraud. This option could include a central depository which would facilitate better control and foster advanced risk assessment.

**Option 2** would entail the full digitalisation of VAT refund systems. This option as well could include a central depository which would facilitate better control and foster advanced risk assessment.

**Option 3** would consist in a technical and legal harmonisation of VAT refund implementation requirements. In particular, it would regulate certain aspects of the functioning, the role and the responsibilities of VAT refund organisations and their relationship with merchants and tax authorities. Three models, as set out below, are presented.

A] B2C model: The VAT refund provider has no contractual relationship with the merchants (and thus does not retrocede any commission to them) but concludes a contract directly with the traveller, whom he represents before the tax authorities. Fiscal liabilities would have to be shifted from merchants to refund providers.

B] Double Sale Model: Under this model, the goods are deemed to be sold first to the refund operator who is then supposed to have them supplied to the traveller. Before making a purchase, the traveller enters a contract with a refund operator and provides his identity details to the merchant who issues an invoice in the name of that operator. Subsequently, the goods are purchased by the traveller from the refund operator for the same price.

C] Split Model: Under this model, the traveller enters into a contract with a refund operator which provides the merchant with a secure unique identifier. In turn, the merchant issues on the basis of that identifier an invoice without VAT to the traveller who provides confirmation of exit to the refund provider.

Finally, a separate annex in the study will assess the hypothesis of abolishing the current form of travellers VAT refund procedure.

### **Duty-free shops**

**Option 0** is the continuation of the status quo with the possible risk that a certain shift in purchasing patterns could take place (e.g., in relation to the UK via the Channel).

Within each of the following options, two sub-options can be considered: sales of both non-excisable and excisable goods (alcohol and tobacco) would be allowed, or excisable goods are excluded from the exemption.

**Option 1** is the extension the VAT exemption for duty-free shops to travel hubs other than airports and ports. This option would increase the scope of duty-free operations insofar secure travel hubs could be established in other places e.g., where passport and customs controls are already available (e.g., certain railway stations).

**Option 2** is the extension of the VAT exemption for tax-free shops selling to airport inbound passengers within the limits of the personal allowances at import. A derogation from territoriality principles of VAT could be considered as a substitute for duty-free sales made outside the EU.

**Option 3** is to establish a level playing field between duty-free shops and high street shops by applying the same VAT refund system.

**4. QUESTIONS TO THE DELEGATES**

The delegates are invited, for each of the 3 parts of the study, to:

- express their views on the options for review and their possible impacts,
- provide any further suggestions as regards the avenues to explore, and
- submit any relevant data that might contribute to the assessment of the options.

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