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INTERNATIONAL

Confusion and complexity surround the rules for applying VAT to the costs of chartering a yacht in the European Union. Although the European Commission looks for harmony, the member states have their own ideas. Barrister Benjamin Maltby provides a guiding hand through the maze with the help of some of Europe's leading tax lawyers

Must charterers be charged VAT?

Value Added Tax, and its variously named equivalents, is a form of sales tax payable throughout the European Union on certain goods and services. Whether or not the tax applies to payments in respect of a yacht charter has always caused confusion. Although the fundamental framework is common to all member states, different ideas abound as to how the tax should be applied.

The potential exists for VAT to become payable either because a yacht is to be chartered in the territorial waters of a certain country or because the owner or charterer has some connection with the place. When any such a possibility arises, the laws of the relevant jurisdiction(s) must be carefully considered. Uncertainties come about because the various tax authorities do not always use the same tests to determine whether VAT will be payable. The standard rates of VAT also vary considerably throughout the EU, and are set out in the table below.

Spain	16	The Netherlands	19
Portugal	15	Germany	*16
(Madeira, Azores)	(21)	Denmark	25
France	19.6	Sweden	25
Italy	20	Finland	22
United Kingdom	17.5	Poland	22
Malta	18	Estonia	18
Cyprus	15	Latvia	18
Belgium	21	Lithuania	18

(*19% from 1 January 2007)

Let us first consider the scenario where the legal ownership (as opposed to the beneficial ownership) of the yacht is held by a company based outside the particular EU country concerned, either in another EU member state or, as is typical with larger yachts, in one of the classic offshore jurisdictions.

VAT will generally not be payable when a yacht belonging to a foreign owner is chartered in the territorial waters of the following countries: Malta, The Netherlands, Finland, Poland, Estonia and Latvia. This is because, although it is the place where charter services are supplied that is paramount, these countries consider this place to be where the owner is based rather than where the charter actually takes place.

Certain member states, however, take a different view. VAT will be payable when a yacht belonging to a foreign owner is chartered in the territorial waters of the following countries: Spain, Portugal, France, Italy, the UK, Cyprus, Belgium, Germany, Denmark, Sweden and Lithuania.

However, VAT will not be payable in Portugal, Italy, Belgium, Denmark, Sweden or Lithuania when the foreign owner is based in another member state. The liability for accounting for the VAT to the tax authority may be the duty of the charterer, rather

than the owner, in Portugal, Italy and Germany under their respective 'reverse charge' mechanisms.

When a yacht is chartered in United Kingdom waters, VAT need only be charged by a foreign owner if his total payments received for such charters has exceeded £60,000 in the previous 12 months. While charging VAT normally requires registration, when chartering to a party already registered to charge VAT in the UK, the owner need not register as well, as the charterer will have to account for the VAT instead.

Cyprus has a similar system to the UK, although the annual charter income need only exceed CY£9,000. Further, if the yacht's next port of call is outside the waters of the EU, the charter may be seen as 'international' and be entirely subject to Cypriot VAT at 0 per cent.

Now let us consider how the various tax authorities of these countries handle the issue of VAT on charter payments where local owners charter their yachts. An owner may be considered to be local if he is a resident taxpayer, is domiciled or (unusually in this context) has just a permanent local establishment. The approach is far more uniform. In fact, most member states oblige owners to charge VAT no matter where the yacht is chartered. As ever, there are exceptions.

In Cyprus and Latvia, VAT will only apply to a local owner when chartering in local waters (the Cypriot rate of 0 per cent for international charters will still apply to a local owner). In Italy, the UK, Belgium and Denmark, VAT will only apply where the yacht is chartered within EU waters. Establishing the precise amount of time spent by the yacht inside and outside the EU is difficult, and usually a matter for the owner to prove. The Italian tax authority, therefore, will allow a local owner to use specific fixed percentages, according to the yacht's length and propulsion, to determine what proportion of the charter hire rate is subject to VAT. For example, the VAT could be reduced from the standard Italian rate of 20 per cent to just 6 per cent for a yacht over 24 metres in length. It may also be possible for the charter payments to be exempted from Italian VAT altogether, where the owner is an Italian company with the formal objective of chartering yachts, and the yacht is provided, with a crew, to a corporate charterer.

Portuguese law requires a local owner to be providing charter services on a regular basis before a liability arises. For Latvian owners, VAT will be charged at 0 per cent where the charter service is provided outside Latvia.

It is important to note that while the charterer's or yacht's nationality – or whether a crew is supplied – generally makes no difference as to whether VAT is levied on charter payments, there are exceptions, aside from the reverse charge arrangements outlined above.

Legal matters

If owners or their managers are not absolutely certain as to their position, up-to-date legal advice should always be taken in the relevant jurisdictions

Although the owner of a non-Spanish flagged yacht will not be liable to charge VAT if the yacht enters Spain briefly, for example to pick up charter guests, longer stays while under charter will require re-flagging into the Spanish Registry and the payment of an importation tax of 12 per cent of her value. If a yacht is chartered to Spanish residents, she must fly the Spanish or the Canary Islands flag. A Spanish charterer with residence outside Spain may charter a non-Spanish flagged yacht and cruise in Spanish waters without having to import the yacht into Spain. Of course, a non-Spanish flagged yacht not under charter is still free to enter and cruise Spanish waters.

In France, charter payments may be exempted from VAT if the yacht has been officially registered in the *inscription au commerce* to undertake permanent trading activity both in France and elsewhere, has a permanent crew and is permanently engaged in charter activities.

Where a yacht is both crewed and designed or adapted to carry 10 or more passengers, it may be deemed by the UK tax authority to be a supplier of 'passenger transport services', meaning that the charter may instead attract VAT at 0 per cent as long as the service is provided in UK waters or to the extent that the service is provided in such waters where the yacht is proceeding to or from the UK.

To benefit from the exemption from VAT charges conferred by registration in Malta's new Commercial Yacht Registry, a Maltese-based owner must register for VAT, a Maltese-registered company must be formed specifically to charter the yacht in the first instance, and the yacht must fly the Maltese flag. This may seem laborious, but it does give the owner additional relief from Maltese income tax on the chartering of the yacht.

Belgian VAT will apply, albeit at the reduced rate of 6 per cent, to all crewed charters taking place in Belgian waters, wherever the owner is based.

In The Netherlands, if the charterer is based outside the EU, the provision of a crew could, under the circumstances, be seen as a separate supply of services and one that is outside the scope of VAT.

The Danish tax authority will also view the provision of a

crew as a separate service, exempt from VAT, in a wide range of circumstances. In Sweden, a crewed yacht may be seen as a passenger conveyance, thereby reducing any applicable rate on the charter to 6 per cent.

Owners from outside the EU may bring their yachts into the EU without paying import duties and VAT on the yacht itself, as long as they remove the yacht from the EU within a certain period of time, typically 18 months. This is known as temporary importation. Whether the yacht has been temporarily or permanently imported will have no effect on the VAT liabilities set out above.

Although the waters in which a yacht is used is a decisive factor in many jurisdictions, contrary to popular belief the specific port(s) or location(s) where the charter starts and ends tend to have little bearing on VAT, other than forming part of the overall picture of where the yacht is being chartered.

The laws of all member states on VAT are based on the Sixth Directive of the Council of the European Communities, which is supposed to harmonise such laws. It's a crude system, which, as this article shows, is open to different interpretations and does not always work smoothly. Double taxation can occur, and some member states prefer to give themselves the benefit of any doubt. The Commission has therefore suggested that a mechanism is needed to eliminate cases of double taxation for VAT which may be caused by the different treatments of a transaction by the various authorities. Some countries, however, are still not convinced that there are sufficient cases of double taxation to warrant any such formal mechanism.

In spite of the complexities of the VAT system, some tax authorities can be unforgiving. If owners or their managers are not absolutely certain as to their position, up-to-date legal advice should always be taken in all the relevant jurisdictions.

Benjamin Maltby is an English barrister. He began his career as a lawyer in the City of London with an International Group P&I Club, before moving to Cyprus to practise with the leading Mediterranean marine and offshore law firm. He now specialises in all aspects of the ownership and operation of large yachts, and is a keen sailor.

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