



APPLICATION OF VALUE ADDED TAX TO CARGO TRANSPORTATION SERVICES IN LATVIA

Gunta KAULIŅA

KPMG Baltics SIA
Balasta dambis 1a, LV-1948, Riga, Latvia
E-mail: gkaulina@kpmg.com

Aivars KRASTIŅŠ

Riga Technical University, Faculty of Engineering Economics
8a Indriķa St., Riga, LV-1004, Latvia
E-mail: Aivars.Krastins@rtu.lv

Summary. Starting from 1 May 2004 Latvia like all other 10 new EU member states had to introduce all requirements of the Sixth Council Value Add Tax (VAT) Directive which regulates application of value added tax in EU. Generally Latvia has implemented these requirements but there are some areas where still some misunderstandings exist in Latvian VAT legislation and practical life. One of such areas is application of VAT to cargo transportation services. Main requirements and problems existing in Latvia are described in this article. Since application of VAT on transportation services depends on the status of business partners involved in the transaction, schemes are included in the article, which demonstrate how VAT should be applied. There are three different treatments in the Latvian VAT law on application of VAT on transportation services. The first explains the application of VAT on international transport and services provided by international transport. This explanation has already been in force before Latvia's accession to EU. The second treatment regulates application of VAT to internal transportation services. And the third treatment is in force only from 1 May 2004 and explains how VAT must be applied to transportation services between EU member states. Since transportation services between member states also could be treated as international transportation a lot of misunderstandings and disputes between taxpayers and tax administration take place. Simultaneously disputable interpretations of government institutions, and issues that are not clarified leave room for different interpretations.

JEL Classification: F190.

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Reikšminiai žodžiai: pridėtinės vertės mokestis, krovinių vežimas, tarptautinis transportas.

1. Introduction

Accession to the European Union (EU) has resulted in significant amendments to the Latvian indirect tax legislation. Unfortunately, we still may encounter various uncertain issues that make the lives of businessmen risky.

In regard to the application of Value Added Tax (VAT), the most significant uncertainties and contradictions are found in the normative acts regulating the application of VAT to transportation services. While the requirements of the 6th EU Directive have been implemented in the law, it still contains the previous rulings, which has given rise to contradictions and different interpretations.

2. VAT on Cargo Transportation

Analysis of the VAT application to cargo transportation shows that no changes have been made to the legislation with respect to transportation activities related to export, import and transit of goods. After 1 May 2004, such transportation activities are carried out only with third (non-EU) countries such as Russia, Ukraine, Bulgaria, Switzerland etc.

The observance of certain aspects relating to cargo transportation between EU countries may ease the taxpayers' understanding of the statutory requirements. Those are as follows:

Make sure that transportation is carried out between EU member states (begins in a EU member state and end in another EU member state),

Clarify the status of the recipient of services (taxable or non-taxable entity of a member state, or third country entity).

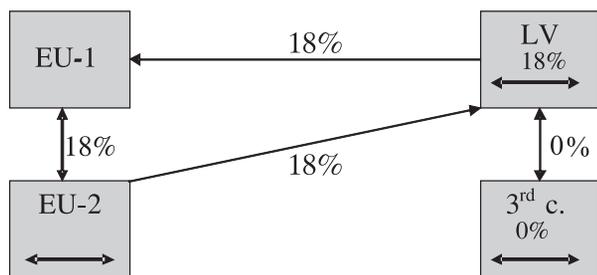
Based on the above, the Latvian taxable entity that transports goods determines the applicable VAT rate and member state where those services are taxable.

If cargo is transported within one member state (embarked and disembarked in the same member state) VAT of that member state is applicable irrespective of the recipient's status. The carrier must be a registered VAT payer of that member state.

When the cargo crosses borders of EU member states, application of taxes depends only on the status of the services recipient. In all cases when the recipient is registered as a taxable entity in a different member state than the provider of services, a 0% VAT is applicable and tax payments are the responsibility of the services recipient irrespective of the EU member state where the transportation is carried out.

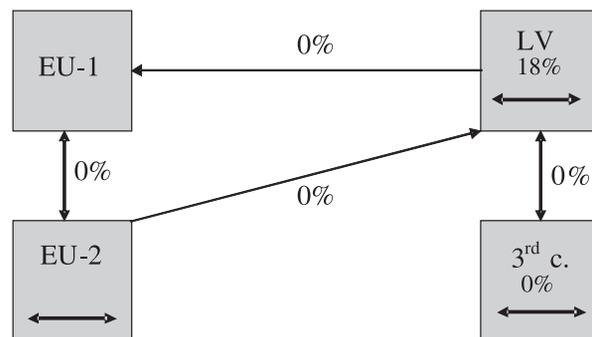
However, when the recipient is a non-taxable entity of any EU member state or an entity of third country, taxes are applicable in the country where the transportation is commenced.

The following schemes are drawn for understanding purposes: The "EU-1" and "EU-2" designations used in the scheme denote any EU member state other than Latvia but "3rd c." denote any third (non-EU) country.



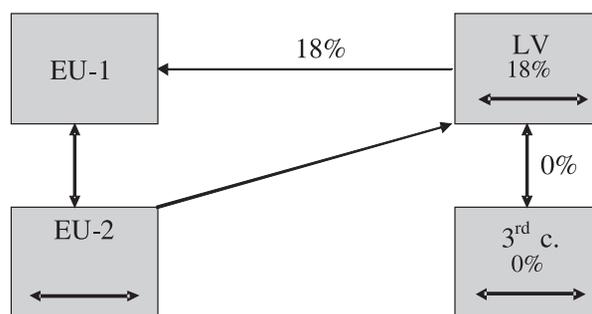
Scheme 1. VAT application when the provider and recipient of cargo transportation services is a taxable entity registered in Latvia.

In view of the above considerations regarding the VAT 0% application, only one condition is met in the examples discussed in Scheme 1, i.e. transportation is carried out between several EU member states but the provider and recipient is registered in the same EU member state (Latvia). As a result, an 18% VAT is applicable. However, VAT for services provided within any other EU member state (for example EU-2) is applicable in accordance with the legislation of the respective member state after registration as a VAT payer in that member state.



Scheme 2. VAT application when the provider of cargo transportation services is registered as a VAT payer in Latvia, but the recipient is a registered taxpayer of another member state.

Scheme 2 reflects a situation, when the both conditions are met, i.e. the transportation is carried out between EU member states and the recipient is a registered taxpayer of a different EU member state than the provider. Please note that in these cases it does not matter in which member state services are provided as long as the cargo is carried over the borders of a EU member state. For example, a 0% VAT rate is applicable when the provider of services, a Latvian taxable entity, provides transportation services to a registered taxable entity of Poland, and the cargo is carried from Hungary to Austria.



Scheme 3. VAT application when the provider of cargo transportation services is registered as a VAT payer in Latvia, but the recipient is either a non-taxable entity of Latvia, non-taxable entity of another EU member state, or registered in a third country.

In Scheme 3, the recipient is a EU non-taxable entity or even not registered in the EU. As a result, the transportation services are taxable in the country where they were commenced. Therefore, when the cargo is carried from EU-1 to EU-2, the provider of services, which is a Latvian taxable entity, should register in EU-1 and apply the tax rates of that member state. Likewise, VAT registration is required in EU-2 when cargo is carried from that member state to Latvia.

3. VAT Application to Services Provided via International Transport

Legal requirements and interpretations of government institutions regarding services provided via international transport require special attention as this area contains contradicting legal norms, disputable interpretations of government institutions, and issues that are not clarified and leave room for different interpretations.

To begin with, the VAT law contains special norms relating to taxation of international cargo transportation. Namely: Article 1 of the law contains the definition of international transportation, and Part 1 of Article 7 defines the VAT rate applicable to transactions related to international transportation. The above norms prescribe that the 0% VAT rate is applicable in all cases when the cargo is transported via international transport (such as airplane or ship of foreign traffic). As a result, legal norms included in these Articles do not require application of taxes based on the recipient's status (taxable or non-taxable entity of Latvia or other EU member state).

In addition, international transport is not even mentioned in Article 22 of the law, which contains a general definition of the place of provision of transportation services in the EU. According to this Article, the place of provision of transportation services is the country of the recipient's registration. Therefore, the Latvian VAT law prescribes that in case cargo transportation services are provided by a Latvian taxable entity via international transport within the EU territory, and such services are provided to another Latvian taxable entity, the place of provision is Latvia; however, it does not mean that the standard tax rate will be applied, as the applicable tax rates are determined by Articles 5, 6², and 7 of the law. Consequently, cargo transportation via international transport also in the EU territory should be taxable at the 0% rate irrespective of the country of the recipient's registration.

Considering that the current treatment is rather contradicting to the ruling of the 6th EU Directive, the Ministry of Finance (MF) has attempted to provide in their letters a different interpretation of tax application, whereby they indicate that rulings of Article 1 and 7 of the law regarding international transportation do not apply to transportation within the EU. This interpretation is underpinned by the fact that VAT application to transportation services within the EU is a special ruling, which is newer than the norms of Part 1 of Article 7. In my opinion, this interpretation is contradictory to the legal norms applicable in Latvia. However, companies should assess the risks and consequences of not complying with the MF written instructions on the VAT application.

Another important MF interpretation permits tax application to international transportation transactions irrespective of the country of the recipient's registration. For example, the 0% VAT rate is permitted on the rent of international transport vehicles irrespective of the country where the recipient of services is registered as a VAT payer.

The above inconsistent interpretations result in new issues in the VAT application to other transactions, as in one case the special ruling for international transportation is permitted, but in other cases it is not. As Part 1 of Article 7 of the law also prescribes VAT application to vehicle supplies, import, repairs, maintenance and other, it is not clear when this legal norm should be interpreted as special and when as general. For instance, it is not clear whether supply of a ship is treated as supply of an international vehicle with the 0% rate applicable, or it is the supply of goods within the EU, which is taxable at the 18% VAT rate as prescribed in Articles 19 and 20 of the law.

Unfortunately, government institutions do not hold a common opinion on these issues as we have received different interpretations of this issue from the State Revenue Service and Ministry of Finance. In view of the above, it would be very useful for companies to obtain a coherent and publicly announced opinion of the respective government institutions on the issue as soon as possible, as the current practice shows that each company applies this tax according to their understanding, which increases the risk of penalties from the tax authorities in case their understanding is different.

Conclusions

The present study was designed to explain application of VAT to cargo transportation services in EU according to the Sixth Council VAT Directive. The results of the study showed that Latvia has introduced main requirements of the Directive in this

area and application of VAT depends on the status of provider of service and receiver of service as well as from particular place of transportation. As a result sometimes transportation companies need to register for VAT purposes in more than one EU member state.

The present study has disclosed problems existing in Latvia with interpretation of term "international transport". Since Latvian legislation provides specific treatment for application of VAT to transport services provided via international transport, it is not clear understandable how tax must be applied on transportation services between member states.

Only explanation how to separate application of VAT to transportation services provided via international transport and transport services between member states is given in letters issued by Ministry of Finance of the Republic of Latvia and by State Revenue Service but not included into legislation. This makes problems disputable.

Sometimes government institutions do not hold a common opinion on the issues and tax payers have received different interpretations of this issue from the State Revenue Service and Ministry of Finance which makes mentioned problems more complicated.

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PRIDĒTINĒS VERTĒS MOKESČIO UŽ KROVINIŪ VEŽIMO PASLAUGAS TAIKYMAS LATVIJOJE

Gunta KAULIŅA
KPMG Baltics SIA, Latvija

Aivars KRASTIŅŠ
Rygos tehnikos universitetas, Latvija

Santrauka. Nuo 2004 m. gegužes 1 d. Latvija ī PVM īstatymā ītraukē visus Tarybos šeštosios direktyvos, Nr. 77/388/EEB, kuri regulioja PVM taikymā ES, reikalavimus. Autoriai pažymi, kad pagrindiniai minētos direktyvos reikalavimai krovinū vežimo paslaugū sityje yra paslaugū tiekējo ir paslaugū gavējū statusas, transporto paslaugū suteikimo vietas apibrēzimas, transporto bendroviū registravimosi PVM mokētojaus kitose ES valstybēse narēs.

Tačiau PVM īstatyme palikus kai kurias ankstesnes nuostatas atsirado ginčitynū sričū, kurios nevienareikšmiškai traktuojamos PVM administruojamū valstybēs institucijū ir verslo praktikos. Viena iš tokiū sričū yra PVM taikymas už krovinū vežimo paslaugas. Būtent šią problemā autoriai ir nagrinēja savo straipsnyje. Vežimo paslaugoms apmokestinti Latvijos PVM īstatyme numatytos trys schemas. Pirmoji nustato tarptautiniū vežimo paslaugū apmokestinimā PVM. Antroji regulioja PVM taikymā vidinēms transporto paslaugoms. Trečioji, īsigaliojusi nuo īstojimo ī ES datos, nustato, kaip PVM turi būti taikomas už vežimo paslaugas, teikiamas tarp ES valstybiū nariū. Kadangi vežimo paslaugos tarp ES valstybiū nariū gali būti traktuojamos ir kaip tarptautinēs, šioje srityje daug ginčū kyla tarp mokečū mokētojū ir mokesčū administratoriū.

Naujame PVM įstatyme pateiktos nuostatos dėl krovinių vežimo paslaugų, teikiamų tarp ES valstybių narių, apmokestinimo PVM yra naujos. Kad jos būtų taikomos, mokesčių administratoriai ir vežėjai, autorių nuomone, privalo:

- įsitikinti, kad krovinių vežimas vyko tarp ES valstybių narių (prasidėjo ES valstybėje narėje ir pasibaigė kitoje ES valstybėje narėje),
- išsiaiškinti paslaugų gavėjo statusą (apmokestinamas ar neapmokestinamas asmuo),
- jeigu krovinyms gabenamas vienos valstybės narės teritorijos ribose, tos valstybės narės PVM tarifas taikomas neatsižvelgiant į gavėjo statusą. Vežėjas privalo būti registruotas PVM mokėtoju toje šalyje.

Straipsnyje autoriai atskleidė problemą, susijusią su transporto paslaugų, teikiamų tarptautiniu transportu (pvz., lėktuvais ir laivais užsienio maršrutais), apmokestinimo PVM. Kadangi Latvijos teisės aktuose yra nuostata dėl transporto paslaugų, teikiamų tarptautiniu transportu, apmokestinimo PVM, neaišku, kaip šis mokeskis turi būti taikomas tokioms paslaugoms, teikiamoms tarp ES valstybių narių.

Šį klausimą Latvijoje valstybės institucijos aiškina skirtingai, vyksta ginčai tarp mokesčių administratorių ir verslininkų – mokesčių mokėtojų. Nors Latvijos finansų ministerija išaiškino, kaip atskirti PVM taikymą vežimo tarptautiniu transportu paslaugoms nuo vežimo tarp ES valstybių narių paslaugų, problema išlieka diskutuotina, kadangi minėto išaiškinimo nuostatos neįtraukto į Latvijos Respublikos pridėtinės vertės mokesčio įstatymą.

Aivars Vilnis Krastiņš – Professor, Dr. (Econ.), Chair of Customs and Taxation Department International Business and Customs Institute, Riga Technical University. Member of Editorial board of the *World Customs Journal*. Fields of interest – customs activity, international business.

Rygos technikos universiteto Tarptautinio verslo ir muitinės instituto Muitinės ir mokesčių katedros vedėjas, profesorius, ekonomikos daktaras. Pasaulio muitinių žurnalo redaktorių kolegijos narys. Mokslinių tyrimų sritis – muitinių veikla, tarptautinis verslas.

Gunta Kauliņa – Dr. (Econ.), Tax manager KPMG Baltics SIA. Fields of interest – tax issues, development of the Value Added Tax System in the European Union and Latvia.

Firmos KPMG Baltics SIA mokesčių ekspertė, daktarė. Mokslinių tyrimų sritis – mokesčiai, pridėtinės vertės mokesčio sistemos Europos Sąjungoje ir Latvijoje tobulinimas.