the territorial scope of value added tax must be determined in relation to the basic rules laid down in Articles 2 and 3 which establish the principle of strict territoriality and not to the provisions of Article 9 which provide for derogations therefrom.

2. Although the territorial scope of Council Directive No 77/388 corresponds to that of the EEC Treaty as defined for each Member State in Article 227, and although the rules laid down in the directive have binding and mandatory force throughout the national territory of the Member States, the directive, and in particular Article 9 (2) (b) thereof, in no way restricts the freedom of the Member States to extend the scope of their tax legislation beyond their normal territorial limits, so long as they do not encroach on the jurisdiction of other States. Accordingly, Article 9 (2) (b) does not prohibit a Member State from levying value added tax on a transport operation effected between two points within its national territory, even where part of the journey is completed outside its national territory, provided that it does not encroach on the tax jurisdiction of other States.

OPINION OF ADVOCATE GENERAL SIR GORDON SLYNN
delivered on 12 December 1985

My Lords,

Trans Tirreno Express SpA carries passengers and goods by sea from the port of Livorno on the Italian mainland to the port of Olbia on the island of Sardinia, which is Italian territory and part of the Community. On 1 October 1981 the VAT office at Sassari required Trans Tirreno to pay LIT 943 479 000 in respect of VAT said to be due on the whole of the charges made for such transport during 1980. Trans Tirreno objected that this was unlawful — VAT was not due on that proportion of the charges which related to such part of the crossing, by far the greater part, as took place in international waters.

The dispute came before the Appeals Board of the Tax Commission at Sassari which stayed the proceedings and referred to this Court the question whether 'Article 9 (2) (b) of the Sixth Directive (i.e. the Sixth Council Directive of 17 May 1977, 77/388, Official Journal 1977, L 145, p. 1) makes only distances crossed within the territory of Member States in the course of international transport (from State to State) subject to VAT or whether national transport (from one point to another in the same Member State) which is carried out, as in this case, mainly by extra-territorial waters is also subject thereto'.

The Directive is described in the title as being 'on the harmonization of the laws of the Member States relating to turnover

taxes — Common system of value added tax: uniform basis of assessment'. By Article 1 it requires Member States to modify their present value added tax systems in accordance with its provisions.

The Directive also provides *inter alia*:

'Article 2

The following shall be subject to value added tax:

(1) The supply of goods or services effected for a consideration within the territory of the country by a taxable person acting as such;

(2) The importation of goods.'

'Article 3

(1) For the purposes of this Directive, the "territory of the country" shall be the area of application of the Treaty establishing the European Economic Community as stipulated in respect of each Member State in Article 227.'

'Article 9

(1) The place where a service is supplied shall be deemed to be the place where the supplier has established his business or has a fixed establishment from which the service is supplied, or, in the absence of such a place of business or fixed establishment, the place where he has his permanent address or usually resides.

(2) However: ...

(b) the place where transport services are supplied shall be the place where transport takes place, having regard to the distances covered;'

By Article 7 (4) (c) of Decreto del Presidente della Repubblica No 633 of 26 October 1972 (Ordinary Supplement to Italian Official State Gazette No 292, p. 2) as amended by Decree No 94 of 31 March 1979 (Italian Official State Gazette No 93 p. 3011), transport services are regarded as supplied within the territory of the State in proportion to the distance covered within that State.

The question raised is not relevant only to Italy. It applies also to transport between e.g. the mainland of France and Corsica (where exemption is granted in respect of passenger transport pursuant to Article 28 paragraph 3 (b) and Annex F, item 17 under existing conditions); the mainland of Denmark and Bornholm, the rest of the Federal Republic of Germany and Berlin. It will become relevant to Greece.

Trans Tirreno and the Federal Republic contend that the Directive only requires and empowers VAT to be charged in respect of transport within the territory of a Member State and its territorial waters even if the voyage begins and ends in the territory of that State. Any other result amounts to exercising sovereignty over territory which is not part of a Member State.

The Federal Republic in particular relies on the terms of the Commission's proposal for a Nineteenth Council Directive relating to turnover taxes (Official Journal 1984, C 347, p. 5), which recites that 'certain differences of interpretation concerning the principles of territoriality relating to certain air and sea transport services should be resolved', and provides by Article 1 that the following shall be added to Article 9 paragraph 2 (b) of the Sixth Directive: 'A journey by sea or air shall be deemed to take place entirely within a country when the place of departure and the place of arrival are in that country, provided there is no stop in another country'.

France contends that Member States are not obliged to impose VAT in respect of transport through international waters. If imposed, a tax on such transport would put at a disadvantage shipments from e.g. Nice to Corsica, where the whole journey would be subject to VAT, as compared with shipments from Genoa to Corsica when there would be no power to impose VAT in respect of the journey through international waters.

Italy, Denmark and the Commission take the opposite view. Whilst accepting that the rule is not expressly spelled out in the Sixth Directive, they contend that there is nothing to exclude transport through international waters when the journey begins and ends in the same Member State. If it were otherwise, ships would seek to pass as far as possible through international rather than national waters. It is contended that the law of the flag should be applied to carriage on a ship of the country in which the journey begins and ends so that the goods and passengers are deemed always to be on national territory. If it were otherwise it is said that an absurd result would be produced in that goods would be considered to be exported from and imported to the same Member State.

So far as goods are concerned, the Commission contends that by virtue of Article 8 of the Directive, when goods begin and end the journey in the same Member State, the place of supply is the place where the goods are at the time of despatch or the transport begins and, by virtue of Article 11 A paragraph 2 (b), the taxable amount shall include 'incidental expenses such as commission, packing, transport and insurance costs charged by the supplier to the purchaser or customer'. So far as persons are concerned, the place where transport services are supplied shall be the place where transport takes place, having regard to the distances covered, and by Article 11 A paragraph 1 (a) the taxable amount shall be 'everything which constitutes the consideration which has been or is to be obtained by the supplier' from, *inter alios*, the purchaser. The position is quite different where goods and persons are carried from one Member State to another. By virtue of Articles 11 B paragraph 3 and 15 paragraphs 1 and 13, goods are taxed in the country of importation in an amount including the full price of transport and are exempt in the exporting country. For passengers, each Member State charges tax on that part of the journey completed within its territory.

I do not consider that any assistance as to the construction of the Sixth Directive is to be derived from the proposal for the Nineteenth Directive. It is plain that views differ and that the Commission wants to spell out what it considers to be the correct position under the Sixth Directive to resolve those disagreements. The Sixth Directive must be considered alone.

In Case 168/84 *Berkholz* v *Finanz Hamburg-Mitte-Altstadt* (judgment of 4 July 1985) the Court had to consider Article 9 of the Sixth Directive. It found that the aim of that provision was to establish a rational arrangement of the spheres of application of national rules relating to VAT, fixing in a uniform manner the place where the tax fell to be paid. The object is to prevent two countries being free to tax, so that the tax

might be demanded twice, and in certain cases to prevent tax being avoided. The Court also, on the basis of Article 3, found that the field of application of the Directive coincided for each Member State with the field of application of the relevant fiscal legislation. Thus Article 9 did not limit the freedom of Member States to impose tax, outside the territory over which they were sovereign, on ships subject to their jurisdiction. In that case it was held that it was open to the Member State to tax the owners of slot machines, installed on ferry boats, at the owner's principal or fixed place of business.

That case, however, concerns paragraph 1 of Article 9, the general rule which fixes the supply at the place of the supplier's business, or a fixed establishment which he has, or at his permanent address or usual residence, and not paragraph 2, which by way of exception, fixes the place of supply as the place where the transport takes place.

I consider that the Commission is right in its general approach to the directive. For goods which are supplied within a Member State, the place where the goods are when dispatch or transport begins is deemed to be the place of supply, and the taxable amount includes the cost of transport (Articles 8 and 11 A paragraph 2 (b)). If goods are supplied from one Member State to another, the amount of the cost, including transport, is not liable to tax in the country of exportation but that tax is payable in the country of importation on an amount including the cost of the transport (Article 15 paragraphs 1 and 13, Article 10 paragraph 3, Article 11 B paragraph 3 (b)). For the carriage of persons within a Member State, VAT is payable on the journey within the Member State, 'the supply' taking place over the whole journey and tax being paid on the consideration. If a person is transported through two or more Member States at the present time, tax is payable in each Member State on the part of the transport which occurs there, each part being respectively a place of supply. Eventually by virtue of Article 28 paragraph 5 passenger transport will be taxed in the country of departure in respect of the whole transport within the Community.

On one point, however, I do not accept the Commission's argument. It is said that Article 9 paragraph 2 only applies to the transport of passengers. However, that paragraph, unlike other articles, does not specifically distinguish between the transport of persons and goods. It is in general terms. It seems to me to be perfectly capable of applying to the carriage of goods as an independent transaction, although not to the transport of goods which is an integral part of the supply of the goods. If that were not so, there would be an obvious gap in the directive. I do not consider that there is such a gap.

As the preamble makes clear, an essential object of the directive was to remove conflict between jurisdictions. Articles 8 and 9 thus set out to define the place of supply, principally in order to remove arguments as to the Member State in which the supply takes place. When the whole supply takes place within a Member State there is no such conflict: the crucial decisions then are (a) when the chargeable event occurs —

which by virtue of Article 10 paragraph 2 is 'when the goods are delivered or the services are performed' and (b) what is the taxable amount, which, by virtue of Article 11 A paragraph 1 is 'everything which constitutes the consideration which has been or is to be obtained by the supplier from the purchaser' including, under Article 11 A paragraph 2 (b), transport costs. Although these are the crucial questions, I read Articles 8 and 9, contrary to the argument of the Italian Government, as defining the place of supply for the purposes of all supplies including those taking place exclusively within one Member State.

On the basis that the field of application of the directive coincides with the field of application of the relevant fiscal legislation, as was said in Case 168/84 it seems to me that the essential question is whether anything in the directive prevents a Member State from imposing VAT on the whole of the transport between two points in its territory, even though part of the transport is through international waters. So long as no part of the transport takes place in the territory, including the territorial waters, of another Member State, I cannot find anything in the directive which prevents a Member State from so doing. Moreover, a power to do so seems to me to be consistent with Article 10 paragraph 2 where the transport services are to be taken to have been 'performed' when the transport begins (on the mainland) or, as I am inclined to think (by analogy with the delivery of goods), when it is completed (in Sardinia).

Accordingly, Italy is at liberty, so far as the directive is concerned, to regard the whole transport from the mainland to Sardinia as constituting the supply of transport services subject to VAT even though part of the journey is through international waters. I do not regard this as being derived from any international law rule relating to the flag of the vessel, even if a ship carrying an Italian flag could additionally be regarded as constituting Italian territory for the purposes of ascertaining the place of transport. The rule is the same for goods or persons transported on vessels carrying other flags. It derives not from legal rules relating to the flag but from a proper interpretation of the scope of the directive.

Administrative difficulties in seeking to calculate which part of the transport is through international waters would not constitute a reason for interpreting a directive contrary to its clear terms, but they do go to support the interpretation that the whole journey between two points in a Member State, which does not cross other territory, is to be covered.

France accepts this result, that a Member State is at liberty to charge VAT on the whole transport including passage through international waters. Italy, Denmark and the Commission go further — it is obligatory to tax the whole of the transport. The Federal Republic says it is forbidden to include the passage through international waters as part of the transport.

For the purposes of its decision in the present case, the Italian tribunal does not need to know whether such tax must be charged; it is sufficient that it may be charged. For that reason, and because it is possible that an application under Article 169 of the EEC Treaty may be brought before the full Court against another Member State, it is perhaps undesirable, as

well as unnecessary, that the Chamber should decide whether the imposition of such tax on the whole voyage is obligatory. Lest the Chamber take the view that this should be decided, I must deal with it.

This point is not decided in Case 168/84. The Court there held that the directive did not limit the freedom of a Member State to impose tax on the relevant event. It did not say that a Member State was obliged to do so.

There is, as has been seen, nothing in the directive which expressly says that the whole transport, including that through international waters, must be so taxed. On the other hand, the essential aim of the directive is to harmonize Community rules dealing with VAT; the subheading 'Common system of value added tax: uniform basis of assessment' gives the indication. Once it is found that the transport is between two points in one Member State, the rules ought to be the same in all Member States. By attaching the liability to tax in one Member State by reference to the place of supply and the chargeable event, it seems to me, on the basis of the arguments advanced in this case, that tax must be charged on the whole transport even if part of it is through international waters. It would be extraordinary if the method of assessment of tax differed according to whether transport was by land or by sea between the same two points in a Member State.

Different considerations, however, come into play if part of the transport is through the territory, including the territorial waters and the air space, of another State whether Member of the Community or not, so that the views here expressed do not bear directly on transport between Berlin and the rest of the Federal Republic of Germany.

In the circumstances, however, I consider that the question posed should be answered on the basis that:

The Sixth Council Directive of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of assessment, and in particular Article 9, paragraph 2 thereof, is not to be read as preventing a Member State from subjecting the transport of goods and persons from one point to another in the territory of that Member State to VAT, albeit that transport takes place mainly or partly in international waters, provided that no part of the transport takes place in the territory, including the territorial waters, of another Member State or a third State.

The costs of the parties to the main proceedings fall to be dealt with by the national court: the costs of the intervening Member States and the Commission are not recoverable.