

# THE PROPOSAL OF TAXATION OF INTERNATIONAL PASSENGER TRANSPORT WITH RESPECT TO THE INCLUDING INTO THE TRAVEL SERVICES

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**Received: January 16, 2012**

## Abstract

OTAVOVÁ, M., SOBOTKOVÁ, V.: *The proposal of taxation of international passenger transport with respect to the including into the travel services. Acta univ. agric. et silvic. Mendel. Brun.* Acta univ. agric. et silvic. Mendel. Brun., 2012, LX, No. 4, pp. 299–306

Generally, international passenger transport is exempt from the value added tax, in the case of air transport. International road passenger transport is however liable to taxation. However, the Council Directive on Value Added Tax contains a number of variations in the frame of the taxation of international passenger transport both for the states that joined the Community after January 1, 1978 and also for countries that were members of the Community on January 1, 1978. The international passenger transport is therefore rather problematic field due to a number of exceptions for individual Member States. It is on the providers or recipients of transport services to inform correctly about the taxation of international road transport and to pay properly the tax. The aim of the article is to evaluate the possibilities of the taxation of international passenger transport in the Czech Republic, Austria, Slovak Republic, Germany and Poland and to determine how the taxation of international passenger transport affects the tax liability and price of travel services provided in this country. From the comparative analysis it is evident that the tax paid abroad should be included in the total price of the purchased service. Based on the comparative analysis there will be a proposal for the taxation of international passenger transport so that the tax collection in the monitored countries would be simplified. The proposal recommends to unify an approach during the taxation of international passenger transport for all Member States of the European Union in order to reduce administrative costs on the part of the governments and individual entities.

VAT Directive, international passenger transport, margin scheme, special regime for travel services, customer travel service

Legislation of the European Union were implemented into the Czech law by accession of the Czech Republic to the European Union on May 1, 2004 in order to ensure uniform rules for all Member States in application of tax laws. For that reason Act No. 235/2004 Coll. on Value Added Tax entered into force, as amended (hereinafter the "Act on Value Added Tax"), based on Council Directive 77 / 388/EHS from May 17, 1977 on the common system of the value added tax: uniform tax basis. Based on this directive, which has been

amended several times, a provision on a special regime for the taxation of travel services were incorporated into Value Added Tax Act. Transport of persons is also a type of travel service. Based on Article 48 of EU Council Directive, the place of fulfillment for passenger transport services is the place where the transport occurs according to the covered transport distance. International passenger transport is, however, a service for which the EU Council Directive does not establish a uniform approach to Member States, ie. each State may have

set a different tax regime eventually exemption of this service. These variations are obvious under Article 370 of Directive on Value Added Tax. Berger (2010) says that Member States may apply national variations from the directive regulating the field of the value added tax, i.e. undergo certain fulfillments of taxation instead of the applications of exemptions from the taxation or contrary to exempt certain fulfillments from the tax instead of their taxation by the value added tax. Legislation of the Member State under which the international passenger transport by aircraft is according to Article 371 of the Directive, which would be otherwise liable to standard tax rate, exempt from tax, while international passenger transport by buses is liable to taxation, is not at the current stage of harmonization contrary to the principle of equal treatment applied in the Community law. Article 371 Directive states that: "Member States which on January 1, 1978, exempt from the tax fulfillments listed in Annex X, Part B, may continue in exemption of these fulfillments under the conditions existing in the Member State at the same day." Annex X contains a list of fulfillments liable to variations. In Part B in section 10 there is given transport of persons and goods, such as luggage or motor vehicles accompanying such persons, or services provided in connection with the passenger transport, if the passenger transport is exempt from tax, i.e. if this fulfillment before January 1, 1978 was exempt fulfillment in this country, this exception is remained also in the future.

The international passenger transport is rather problematic field due to a number of exceptions for individual Member States. It is therefore on providers or recipients of transport services, to inform correctly about the taxation of international road transport and to pay properly the tax. The aim of the article is to evaluate the possibilities of the taxation of international passenger transport in the Czech Republic, Austria, Slovak Republic, Germany and Poland and to determine how the taxation of international passenger transport affects the tax liability and price of travel services provided in this country.

## MATERIALS AND METHODS

The aim of this paper is based on comparative analysis of the taxation of international passenger transport in the countries neighboring the Czech Republic, i.e. Germany, Austria, Poland and the Slovak Republic, to evaluate the possibilities of the taxation of the international passenger transport in these states and to determine how the taxation of international passenger transport affects the tax liability and price of travel services provided in this country. Partial aim is to propose appropriate regulations for the taxation of the international passenger transport so that there would be a reduction in administrative costs on the side of

individual governments, as well as on the side of businesses.

This paper deals specifically with the taxation of bus transport, which appears as the most often used in connection with the provision of travel services. Carrier is considered as a provider of transport that provides its services to entities that includes them into travel services, most often travel agency.

The principle of applying the value added tax on the international passenger transport both in the Czech Republic and in countries bordering the Czech Republic was determined in this paper. Subsequently there was made a comparison of the monitored issues and an evaluation of the fundamental differences between the taxation of international passenger transport in individual countries. Based on the comparative analysis there was designed a proposal for the taxation of international passenger transport so that the tax collection in the monitored countries would be simplified.

There were used standard scientific methods that allowed objective and systematic qualitative and quantitative description of the issue. The method of analysis, comparison, description and modeling were used in order to meet the aim of the paper. Method of synthesis was applied in order to suggest results.

## RESULTS AND DISCUSSION

### Comparative analysis of the taxation of international passenger transport in selected countries

#### *Czech Republic*

Czech Value Added Tax Act solves the problem of the taxation of international passenger transport in § 70. According to this provision, passenger transport and their luggage between Member States and between Member States and third countries, including services directly related to the transport, is exempt from tax in the Czech Republic with claim to deduct the VAT. Return transport is considered as a separate transport, which is also exempt from tax in the Czech Republic. Exemption for international passenger transport is therefore related only to the part of transport that is carried in the Czech Republic. And as Galočík and Paikert (2011) add, transport carried outside Czech Republic is taxed according to the regulations of the individual Member States that may, as well as the Czech Republic, but also may not exempt the international passenger transport.

For proper quantification of the tax liability with regard to the international passenger transport is very important to establish the place of the fulfillment, in accordance with § 10a of Value Added Tax Act. The place of the fulfillment in providing services of passenger transport is the place where the relevant part of transport is carried

out. According to Pitner and Benda (2011), type of vehicle is not decisive, it may be train, bus, plain and also ship transport in terms of exemption. Duty of every carrier should therefore be to determine the taxation process or the possibility of exemption in the individual Member States and in the third countries, where the transport is carried out.

Exemption from the value added tax in the Czech Republic is then related to both scheduled and charter international passenger transport and both national operators as well as to persons who are registered for the VAT in another Member State or to a foreign person liable to taxation. Air transport is, however, always exempt from tax.

However, passenger transport carried out only in the Czech Republic (not international transport) is not exempt from the value added tax and the tax payer is liable to declare the tax from realized fulfillment in the Czech Republic. The tax rate is determined according to § 47 paragraph 4 and Annex No. 2 of Value Added Tax Act. Reduced tax rate is applied to a regular public passenger transport<sup>1</sup> and their luggage and the standard tax rate of tax is applied on irregular passenger transport (trips) and individual passenger transport (taxis).

In case of the international passenger transport there is an exemption from the tax with the claim to deduct tax only to that part of the transport, which was carried out in the Czech Republic. Carriers or travel agencies have to find out how they should proceed in the international passenger transport, which is carried out in other countries, under specific statutory provisions of the country through which the transport is carried out.

#### ***Slovak Republic***

In the Slovak Republic there is a similar regulation of the international passenger transport as in the Czech Republic. The place of the taxable fulfillment is the place where the transport takes place. Meanwhile, the international passenger transport carried out in the territory of the Slovak Republic is exempt from tax with claim to deduction, according to § 46 of Slovak Value Added Tax Act.

#### ***Germany***

The air, see and water transport of persons is exempt from tax in Germany. Road and rail transport of persons is not liable to exemptions. Bus passenger transport carried by the carrier from another Member State is then taxed at a tax rate of 19% if it is the irregular transport. Tax rate of 7% is applicable for allowed regular transport, when the transport route in Germany does not exceed 50 km.

In cases when a Czech bus operator is providing international passenger transport service, which is also given partly in the territory of Germany, to

a travel agency or another business entity, this part of the journey undertaken in Germany is liable to the German tax rate. Under current legislation of the German Value Added Tax Law, the liability to declare and pay the tax is transferred to the customer, i.e. to the travel agency. The liability of the carrier is to report its customer to the German tax authority. When issuing the invoice for their services, they will charge the German part of the route with a zero tax and at the same time they will indicate in the invoice that recipient of the service is liable to declare and pay the tax in Germany. The invoice must not also missing data for tax assessment, such as a number of traveled kilometers in the Czech Republic and in Germany and the corresponding division of the total price to the Czech and German part of the route. Czech customer is then liable to register for tax in Germany at the tax office in Chemnitz (Chemnitz Finanzamt – Sud), which is the competent tax authority for the Czech Republic, and declare and pay the tax.

#### ***Austria***

Within the Austrian Value Added Tax Act it is not decisive whether it is the international passenger transport or not, as the place of fulfillment in providing transport services is always a place where the transport is carried out. If, therefore, it is an international passenger transport, which is partially carried out also in the territory of Austria, so the proportional part of the passenger transport in the Austria is liable to the value added tax in amount of 10% under the Austrian law. Recipient of the service (i.e. the economically active person) has to declare and pay tax from this part of the transport according to § 19 of the Austrian Value Added Tax Act unless the provider of transport service does not have place of business activities or permanent establishment in Austria. If the transport service would be provided to non-business entity (private person), the provider of service would be responsible for paying the tax from the Austrian part of the transport regardless of whether he would have or have not the place of business activities in Austria.

Provider or recipients of transport services carried out in Austria are liable to register with the tax authority in Graz-Stadt and to report the tax here (tax return) on the basis of which they declare and pay appropriate tax. It is possible to apply a claim to deduction under the rules of the Austrian law within the tax return.

#### ***Poland***

Poland belongs to the EU member countries which have negotiated an exception within the accession treaties in Article 388 of the VAT Directive with regard to the international passenger transport,

<sup>1</sup> Regular public passenger transport is transport of passengers over predetermined routes in which passengers are getting on and off at designed stops or places according to predefined approved timetables.

i.e. they can continue in the exemption for this transport. In Poland there is international passenger transport defined on the basis of national regulation as a transport between Poland and other countries, with exception of road transport. Exemption can therefore be used only for air, water and rail transport.

For international road passenger transport there are not defined any specific conditions, however, the Polish Value Added Tax Act determines the place of the fulfillment for these services where there are carried out. Bus companies from other European Community Member State which do not have a seat in Poland, are liable to pay tax from the part of the transport service carried out in Poland in amount of 8%. Furthermore they are also liable to register for the VAT at the appropriate tax authority in Warsaw, where they will submit relevant tax report and pay the tax. Here, in any case the tax liability is not transferred onto the recipient of the service.

In Poland, however, with effect from June 21, 2010 there was a regulation regarding the rules relating to the payment of taxes by foreign entities in the performance of bus transport in Poland. These changes resulted from the decision of the European Court of Justice, No. C-311/09 from May 6, 2010, in which Poland was sued for violations of the Article No. 73, 168 and 273 of the VAT Directive with regard to the national treatment of the international passenger road transport. According to this judgment, foreign carriers paid the value added tax under the lump sum rate system only based on the number of persons transported in Poland without the claim to deduct this tax.

On the basis of the mentioned judgment, the entities already registered for the VAT in another Member State when they are carrying out the passenger transport in the territory of Poland, they also register for the VAT in Poland and apply the claim to a tax deduction. However registration in Poland is a complex process. According to the Embassy of the Czech Republic in Warsaw, the Polish regulations require among other things for registration to tax to open a bank account in Poland or the company statement that it would not ask for a tax refund. Submission of the contract with accounting companies in Poland is also required, which will represent a foreign entity in Poland or

at least a statement about where it is possible to find accounting documents and who is in case of control in charge to deliver them to the relevant tax authority in Poland (the body / person in Poland). The method of registration is relatively complicated compared with registrations in other states and it can only be described as "unfair" competition for Polish carriers, accounting companies and banking institutions.

I: *Taxation of international passenger transport in selected countries – absolute terms*

State	VAT rate
Czech Republic	VAT-exempt
Slovakia	VAT-exempt
Germany	19%
Austria	10%
Poland	8%

Source: own results

From Tab. I, it is evident that taxation of passenger transport is different in the monitored countries either with regard to the application of the taxation system, as well as of the applicable tax rate, which depends on the particular national regulation.

These can be verified on the specific values in case of the bus tours on the route Czech Republic – Poland – Germany – Austria – Slovakia – Czech Republic. An assumption is that the bus travels a total of 2 900 km and the total cost for transport provided by an external Czech supplier to Czech travel agency is € 3 500. Table II shows data on the number of traveled kilometers in selected countries including the amount of tax for the relevant part of transport in the monitored countries.

The carrier must be in Poland, Germany and Austria registered at the relevant tax authority. In Poland it is a carrier who pays the tax. In Germany and Austria the carrier must also report the travel agency that ordered the transport. Travel agency must also register with the relevant tax authorities and the liability to pay the German and Austrian tax is transferred onto it. According to Rambousek (2005) it is necessary to divide a payment for the service provided according to a number of traveled kilometers in each country. It results from the

II: *Taxation of international passenger transport in selected countries – relative terms*

State	Number of km	Price	VAT rate	VAT	Registration	Tax levy
Czech Republic	240	288 €	VAT-exempt	-	-	-
Poland	590	708 €	8%	57 €	Tax Office Warszawa	By a supplier of transport services
Germany	1 550	1.860 €	19%	355 €	Finanzamt Chemnitz	By a recipient of transport services
Austria	280	356 €	10%	36 €	Finanzamt Graz - Stadt	By a recipient of transport services
Slovakia	240	288 €	VAT-exempt	-	-	-

Source: own results



decision of the European Court of Justice in case of *Reisebüro Binder* (C-116/96), which implies that no other method of dividing is permitted.

### **International passenger transport as a part of travel service**

It is necessary with regard to the Czech Value Added Tax Act to proceed under § 89, which determines the special regime of taxation of the travel services provided by travel agencies within the travel services, in which is also provided the passenger transport. Application and interpretation of § 89 of Value Added Tax Act is not always obvious and clear. The main problem is proper identification of items that are included in travel services, from which is then calculated a tax in the form of surcharges.

Passenger transport which can be carried out from own capacities or can be ordered with an external carrier forms one from many items of the travel service for most tours. If it is a passenger transport carried out from its own capacity so normal regime is applied and it is possible to claim a deduction of tax on input, as this transport does not form part of the travel services. According to Havel (2011) the travel agency is liable to apply tax on output for this taxable fulfillment under the relevant tax rate, when the tax base is the price found out in accordance with the Law on Property Evaluation, which is understood as the amount including taxes.

It is no longer part of the travel services in the case of passenger transport purchased from an external carrier. The price of purchased transport must then be included in travel services and special regime must be applied here. It is not possible to claim a tax deduction neither eventually ask for a tax refund from another Member State from the transport purchased from external suppliers.

Attention is drawn to situations that occur in some cases for purchased international bus passenger transport by an external supplier carried out in states where transport is liable to the taxation - some travel agencies then apply for a refund of taxes paid in that State<sup>2</sup>. Alternatively, if a liability to the registration to tax arises in that state, they indicate a claim to deduction from that transport in their tax return. In their defense they argue that the carrier issue them an invoice for provided transport such as a fulfillment without foreign taxes, and that the actual tax that travel agency pay, it is not a service purchased and that is the reason why it should not be included into the price of travel services.

Although the above introduced procedure of the travel agencies is not correct, applications for tax refund from other Member States are dealt with positively or eventually submitted tax returns are accepted, where there are given together with a tax liability in respect of the passenger transport

also a claim to tax deduction. These are positively accepted by providers of travel services, who may because of this provide their tours more cheaply.

But if we take into account the interpretation of § 89 of Value Added Tax Act, which is based on the Directive, it is necessary to understand the travel service as a service provided to the customer, which includes a combination of travel services, or goods, if the individual services of tourism and goods are purchased from other persons liable to tax. Deduction on tax on input is not applied when buying individual services and goods forming travel service neither individual service on output are not taxed. Travel agency therefore has no claim to tax refund in another Member State of the European Community for goods and tourism services purchased in another Member State, which are included in the package of travel services, according to the Czech VAT Act, but by extension also from Directive. Since the transport is a part of the package of travel services (it should be part of it, because it is purchased from another person liable to tax) it is not possible to claim a tax refund from another Member State.

It is also possible to argue with provision § 89 paragraph 3 of the Czech Value Added Tax Act, which implies that the surcharge is the difference between the total amount of money that the provider of travel services receives from customers for provided travel services and the sum of the amounts that he paid for purchased services included in the travel services. From this it can be concluded that the purchased service in form of passenger transport must be included in the price of travel services including tax, even if the tax is paid by a travel agency as the recipient of services. The same regime as for other purchased services such as accommodation or food, when the price of accommodation or meals is charged including foreign taxes and the entire invoiced amount is then included in the calculation of surcharge of provider of travel services, should be remained (i.e. including foreign taxes).

Likewise, there is also a liability to pay the value added tax for passenger transport in some states, even if an invoice from the carrier for the service provided would be issued to an amount without tax, since the travel agency should be liable to pay the tax. The tax should be seen as well as tax on accommodation and catering services, as it is the tax that is assessed from the service, which forms a part of the travel services. If the provider of travel services does not include tax on passenger transport into travel services, so his behaviour is inconsistent with the Czech Value Added Tax Act and also inconsistent with the Article 310 of Council Directive 2006/112/EC.

<sup>2</sup> It is result from the completed oral interviews with accountants and tax advisers who represent travel agencies.

**Example, when the price for transport without tax is included into travel service<sup>3</sup>**

Travel agency provides travel services in the form of the international passenger transport from Brno to Vienna for CZK 400 including tax. However transport is not ensured from own capacities, but by purchasing from an external Czech carrier (the taxpayer) for 200 CZK without VAT. The part of the transport is carried out in the Czech Republic – 80 km and part in Austria – 70 km. Given the fact that transport is exempt in the Czech Republic and in the territory of Austria it is a travel agency that declares a tax, a carrier is invoicing correctly the price without taxes. What tax will the travel agency pay from the price of the service in the Czech Republic?

Price of service provided	400 CZK
Price of purchased service (without tax)	– 200 CZK
Surcharge	200 CZK
Tax on output = $200 \times 0.1667 = 33.34$ CZK	

**Example, when the price for transport including foreign tax is included into price of travel service**

Travel agency provides travel services in the form of the international passenger transport from Brno to Vienna for CZK 400 including tax. However transport is not ensured from own capacities, but by purchasing from an external Czech carrier (the taxpayer) for 200 CZK without VAT. The part of the transport is carried out in the Czech Republic – 80 km and part in Austria – 70 km. Given the fact that transport is exempt in the Czech Republic and in the territory of Austria it is a travel agency that declares a tax in amount of 10% from the price of transport in Austria (i.e. from the price of 93 CZK), a carrier is invoicing correctly the price without tax. What tax will the travel agency pay from the price of the service in the Czech Republic?

Price of service provided	400.00 CZK
Price of purchased service (with tax)	– 209.30 CZK
Surcharge	190.70 CZK
Tax on output = $190.70 \times 0.1667 = 31.79$ CZK	

Tax saving is 1.55 CZK in the case that travel agency will also include paid foreign tax on the unchanged price of travel services into the price of purchased service. Tax saving does not exceed the tax paid abroad, thus travel agency rationally behaving increases the price of the travel services at least by paid foreign tax. The payment of tax does not change in the Czech Republic, so the travel agency will not pay more on the tax in the Czech Republic. You can also say that this fact should not affect customers, because increase in price in trip

by tax paid abroad would not be so dramatic and it would be only hundreds of crowns.

**Possible proposals for taxation of international passenger transport**

Based on comparative analysis, it is evident that already in the small sample of the monitored countries, the conditions for taxation are very different and also entities that pay the tax are different in each country. In some of these countries, it is a carrier who pays the tax, but in others it is a business entity for whose benefit the transport is carried out. Therefore, it would be appropriate to clearly define a person who will pay the tax and this person should be same in all states. That person should be in our opinion a carrier because its registration at the tax authorities is also required in states in which subsequently an entity for which the transport was carried out and to whom is then transferred the liability to pay the tax, must then register.

We suppose that if this principle would be contained in the Directive, administrative burden would be reduced for both entities that are participants in this transport, as well as for the country where the transport is carried out (a smaller number of entities submitting a tax return). Then only carriers would submit a tax return and it would contain all the fulfillments for transport carried out during the given period in a particular country.

The Directive on Value Added Tax in Article 393 contains the definitive regime according to the Article 402, under which the variations in the individual EU countries should be solved. With regard to the passenger transport it should be valid in the final regime that it will be taxed in the state of initiation of transport to that part of route, which will take place in the Community. This solution would, in our opinion, avoid excessive costs that arise in connection with the assessment of tax. The final regime is definitely less complicated, because it would prevent on the one hand, tax evasion and further it would simplify the administrative complexity of this type of service. As a problematic field we can see the definition of the return transport, which is understood as a separate service, i.e. the place of initiation of transport, which is crucial with regard to the fulfillment of the tax liability, it would depend on the state where the return transport begins. Again we would know the tax laws of that country, there would be a registration and then we (the carrier or ordering party of passenger transport) have to fulfill our tax liability in this country.

Another possible solution, that is not contained in the Directive within the definitive regime, would be the taxation of the transport in the country of

3 Even provided transport itself is considered to be a travel service according to Czech Value Added Tax Act that is the reason why only transport is considered in the example (in this case it is completely irrelevant whether travel service includes other services such as an accommodation, meals or other services, because the result is always the same).

the provider or, conversely, of the order party of the transport. In our view it is the simplest solution. There would be the unification of the rules for cross-border provision of services. If the services are provided across borders, according to Council Directive 2008/8ES, there is a question where is the place of the fulfillment. This question is increasingly important with regard to the globalization, deregulation and technological changes in trade with services. If we support in our proposals the taxation of the passenger transport in the state of establishment of service providers, this would be a simple fulfillment of the liability to pay the value added tax in the state of the establishment. It would be a solution that would be administratively convenient, but we also believe that it could be challenged with regard to the distortions of competition. In this context it should be noted that the Report on results of parallel control of the administration of the value added tax made in the Czech Republic and Federal Republic of Germany says that the tax revenue during passenger transport, if it is carried out, is rather low for non-

residents in Germany. We also think that in the case of international passenger transport there is often refund of paid tax, eventually tax returns are submitted, where there is a claim to deduction from this transport since paid tax should remain in the state of tax collectors only in cases where passenger transport is part of the travel services. Collection of tax is therefore really negligible for the given state. There is a lot of paperwork, both on the side of the tax collector, as well as on the side of provider of transport or on an entity which ordered the relevant service with little or no effect for that state. Based on the above mentioned, we will support the proposal to tax the passenger transport in the place of the establishment of the provider of travel services in the future.

Currently it would be appropriate with regard to the above mentioned facts to unify at least a person who is liable to register and pay tax in the given state when the place of the fulfillment during the passenger transport is the place where the relevant part of the transport takes place.

## SUMMARY

Generally, international passenger transport is exempt from the value added tax in the case of air transport. However international road transport of passengers is generally liable to taxation. However, the Council Directive on Value Added Tax contains a number of variations in the taxation of international passenger transport both for the states that joined the Community after January 1, 1978 and also for countries that were members of the Community on January 1, 1978. The international passenger transport is therefore rather problematic field due to a number of exceptions for the individual Member States. Considering this fact, it would be appropriate if there were uniform rules for this field. It means to modify the Directive on Value Added Tax so that there would be equal conditions for all countries and at the same time an entity that is liable to pay tax would be precisely defined. Even in the small sample of the monitored countries, it is evident that the conditions for taxation are very different and also entities that are paying tax are different in each country. In some of these countries it is a carrier who pays the tax, but in others it is a business entity for whose benefit the transport is carried out. Therefore, it would be appropriate to clearly define a person who will pay the tax and this person should be the same in all states. That person should be in our opinion a carrier because its registration with the tax authorities is also required in states in which subsequently an entity for which the transport was carried out and to whom is then transferred the liability to pay the tax, must then register. The above mentioned facts would certainly simplify the tax collection with respect to the administrative burden.

Variations in the individual EU countries should be solved on the basis of the final regime contained in the Directive on Value Added Tax. With regard to the passenger transport, it should be valid in the final regime that it will be taxed in the state of initiation of transport to that part of route, which will take place in the Community. It is a solution that can be described as simplistic measures and also measures that would, in our opinion, prevent tax evasion and tax avoidance. This is a regime that would be less complicated and also, as already mentioned, it would prevent on the one hand, tax evasion and further it would simplify the administrative complexity of this type of service.

Currently it would be appropriate with regard to the above mentioned facts to unify at least a person who is liable to register and pay tax in the given state when the place of the fulfillment during the passenger transport is the place where the relevant part of the transport takes place.

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