

Rapport 2011:8

The significance of duty-free sales on board ferries to the transnational transport system in the Baltic Sea Region



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Preface

This report is the result of a project funded under the EU's Baltic Sea programs in 2007 - 2013. The project has been commissioned by the transnational cooperation project TransBaltic: Towards an integrated transport system in the Baltic Sea Region.

TransBaltic boasts more than 35 partners and associated members in nine countries around the Baltic Sea Region. The partnership is composed of regional authorities and specific organisations (logistics associations, transport administration, universities and research institutes) providing competence in transport and logistics issues. The regions co-financing the project include: Skåne (SE), Västerbotten (SE), Blekinge (SE), Västra Götaland (SE), Lahti (FI), Pomorskie (PL), Warminsko-Mazurskie (PL), Sjaelland (DK), Vest Agder (NO) and eastern Norway County Network (NO). The lead-partner of TransBaltic is Region Skåne in Sweden.

The overall objective is to provide regional level initiatives for the creation of a comprehensive multi-modal transport system in the Baltic and Scandinavian region. The concrete outcome of the TransBaltic initiative will be an Action Plan addressing the internal transportation and logistics constraints of the Baltic Sea Region from a sustainable development perspective. The forthcoming Action Plan will include sea transports in the northern and central parts of the Baltic where tax-free based ferry traffic between Sweden, Finland and Estonia via Åland is an important part of the transnational and interregional transport system. In order to improve the knowledge of the impact of tax-free supported ferry traffic on the transport infrastructure in the Baltic Sea Region, Region Västerbotten as the leader of TransBaltic's Work Package (WP) 3 issued (May, 2011) a request for tenders on a proposed research project: "Tax-free based ferry traffic and transnational transport logistics in the Baltic Sea Region".

Statistics and Research Åland (ÅSUB, lead partner) together with the Åland International Institute of Comparative Island Studies (AICIS) won the bid. The aim of the project on offer was, and has been, to highlight the consequences for the transnational transport of goods and people in the Central and Northern Baltic Sea area if duty free sales on board the ferry traffic via Åland, were to disappear.

The analysis, assessments and conclusions presented in this report are based on a combination of qualitative information and quantitative data. The quantitative part of the research is primarily based on national and regional transportation and trade statistics. The analytical part of the project is built on a number of in-depth interviews with top-executives of leading

shipping companies and representatives of other related logistics firms, actors and responsible authorities.

The undersigned has acted as project manager and the main author of this report. Richard Palmer, also from ÅSUB, has compiled and analysed the statistical base-line data of the project. Palmer has written Chapter 3 and designed all the maps, graphs and tables in the report. He has also checked and corrected the English language of the report. Stefan Lång, AICIS, has implemented and documented all the top-executive interviews. He has also contributed written inputs to Chapters 4 and 5 of the report.

The research team wishes to express many thanks to those persons mentioned in the Appendix for their invaluable contribution to the report through their in-depth knowledge of the tax-free ferry traffic logistics and overall transport impact. We also wish to thank Stig Hjerppe, WP 3 Manager, TransBaltic, and Hans Brattström, Regional planner, Stockholm County Council, for their role as initiators of the project.

Mariehamn, December 2011

Bjarne Lindström
Project Leader
Director, ÅSUB

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Abbreviations

BSR	Baltic Sea Region
CBSR	Central Baltic Sea Region
CBT	Central Baltic Triangle
BTKM	Billion Tonne-Kilometers
FTIA	Finnish Transport Infrastructure Agency
IMO	International Maritime Organisation
SAI	<i>Sjöfartens Analysinstitut</i> (The Institute of Shipping Analysis) (Sweden)
SC	<i>Statistikcentralen</i> (Statistics Finland)
SCB	<i>Statistiska centralbyrån</i> (Statistics Sweden)
SIKA	<i>Statens institut för kommunikationsanalys</i> (Swedish Institute for Transport and Communications Analysis)
TRAFA	<i>Trafikanalys</i> (Transport Analysis)
ÅSUB	<i>Ålands statistik- och utredningsbyrå</i> (Statistics and Research Åland) ÅSUB

1 Summary

Today, a significant part of the seaborne transport infrastructure in the northern and central Baltic Sea region (including the *Nordic Triangle*, and the *Baltic Palette*) is built around and sustained economically by tax-free sales on board ferries travelling along the sea lanes via the Åland Islands to and from Sweden, Finland and Estonia - and recently also to Russia (St Petersburg).

The autonomous Åland is one of the few territories in EU where tax-free sales on board ships sailing to and from the rest of the Union are allowed. This is made possible by a permanent exemption from the European VAT-rules in Åland's accession protocol to the EU.

This report highlights the main consequences for the transnational and interregional transport of goods and people in the Baltic Sea Region (BSR) if duty-free sales on board the ferry traffic via Åland, were to disappear. What would remain of today's extensive ferry traffic? What new routes and modes of transportation would evolve? How would the traffic to existing population centres, ports and terminal areas be affected? Who would we expect to lose, and who would win? How would the overall transport logistics between the BSR and the wider EU be affected?

The tax-free based business model of ferry shipping

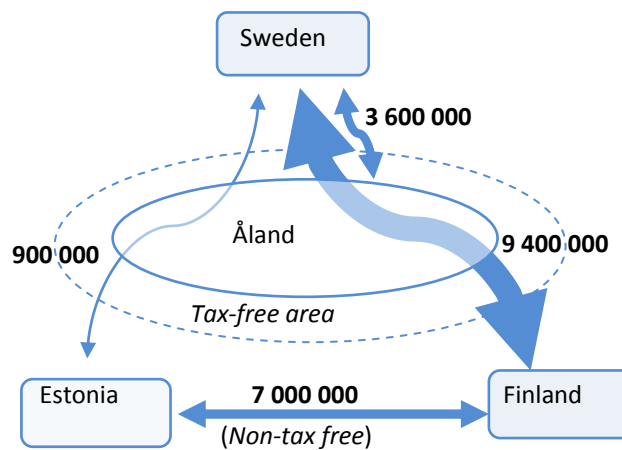
The tax-free based ferry shipping in the central Baltic Sea Region (CBSR) is formed around four main business areas: 1) Passenger/car transportation 2) short cruises 3) freight and 4) conference/business meetings. These four areas of business complement each other in a model that provides an efficient and economically effective transport system for people, cars and cargo.

The different business areas are closely connected, and thus level out fluctuations in demand for the different services offered by the cruise ferry companies. During the summer, passengers and cars are the main segments and during autumn and winter, transportation of cargo functions as a complement. This flexibility provides the means to sustain year-around traffic on the main sea routes in the CBSR and it provides for a frequency and a time table that makes it possible for large volumes of people and cargo to be transported throughout the year, both during high and low season.

The triangle of central Baltic ferry shipping

Åland's tax exemption, combined with a strong expertise in the international ferry and cruise shipping industry, has made Mariehamn, the capital city of Åland, the geographical and commercial centre of the tax-free supported traffic in the CBSR. All the main tax-free supported sea lanes between Sweden, Finland and Estonia are thus routed via ports in the Åland Islands, constituting a Central Baltic Triangle of seaborne transportation. The principal logistics of this seaborne passenger and car traffic area is illustrated in the figure below:

The Central Baltic Triangle: Major tax-free and non-tax free links and passengers* in 2010



*) Arrivals and departures. Approximate figures

Source: Statistics Estonia, Statistics Finland, Statistics and Research Åland

Interestingly, the non-tax free route between Helsinki and Tallinn constitutes a substantial part of the passenger flows within the traffic area. However, unlike the tax-free traffic, price differences in alcohol appear to be the main reason for this. Most of the passengers traveling from Finland to Estonia do day-trips to Tallinn in order to buy cheap Estonian alcohol.

The flow of passengers on board ferries in the Central Baltic Triangle in 2010 is summarized in the map below:

Major tax-free and non-tax free sea routes between Sweden, Åland, Finland and Estonia 2010



Source: Statistics Estonia, Statistics Finland, Statistics and Research Åland

The ferry and cruise traffic between Sweden and Åland is entirely tax free. In 2010 approximately 3.6 million passengers were transported along these routes. Secondly, the major tax-free connections between Sweden and Finland carried approximately 9.4 million passengers the same year. The route between Sweden (Stockholm) and Estonia (Tallinn) carries approximately 0.9 million passengers annually. Finally, the non-tax free lines running between Finland and Estonia carry approximately 7.0 million passengers annually. All together the annual flow of passengers in the CBT exceeded 21 million, of which 15 million on tax free routes.

Åland is heavily dependent on tax-free supported shipping

The tax-free supported ferry transport system and logistics is of fundamental importance for the economic welfare of Åland. The largest cluster of maritime activity in the Central/Northern Baltic is located in Åland. Economic growth, population growth, employment, household income, basic comparative advantages etc., all depend on the continuance of the opportunity to sell tax-free goods on board on the ferries between Åland, Sweden, Finland and Estonia. The Åland society and economy is also strongly dependent on the highly developed and cheap transportation to and from mainland Finland and Sweden that the tax-free supported ferry traffic offers.

Tax-free routes important parts of the wider BSR and EU transport logistics

The tax-free supported ferries supply important parts of the infrastructure linking the logistical flows between the different countries, regions and cities within the CBSR and also between BSR and the rest of EU. Specifically, passenger transport along tax-free routes remains highly important for Sweden and Finland. More than a third of Sweden's maritime passenger transport is along routes sustained by the profitability of tax-free sales and more than half of Finland's maritime passenger transports are tax-free supported.

The tax-free supported routes are also used for shipping cargo on board ferries. The share of tax-free supported transport of goods from Sweden to Finland is approximately one seventh, and the corresponding share of transport from Finland to Sweden is about one sixth. The tax-free supported routes and shipping thus play an important role in Finnish and Swedish – and especially Åland's – transport logistics.

The high frequency of departures of ferries along the tax free routes between Finland, Åland and Sweden function as a 'highway of the seas' connecting the Eastern part of the BSR (Finland, Russia, and Estonia) with the central and western parts. The 'Åland tax-free corridor' therefore functions as an integral link between today's two main transport routes connecting Scandinavia and the western part of Russia and the European continent – i.e. the corridor via Sweden/Denmark to Germany and the *Via Baltica* route from Finland/Estonia and western Russia through Poland and farther down to the central European markets.

Tax-free sales abolished on the Åland routes: The main Losers

Inevitably, major changes not only create winners but unfortunately also some losers. This would most certainly apply to the effects of a possible future abolishment of the tax free on-board sales on the sea routes to and from Åland. The obvious group of losers from such change is the firms and individuals that are currently the most closely connected to, and the ones benefitting the most from the specific economy and logistics that the tax-free supported shipping in the CBSR has created:

- Companies that operate tax-free ferry business
- Suppliers and logistics firms specialized in CBSR tax-free shipping
- Cruise passengers and motorists using the tax-free ferries for transportation and leisure purposes

- Export and import firms using the tax-free supported ferries and their logistic infrastructure

The major losers are the shipping companies and employees with their core business in the tax-free segment. This also holds for the ports and terminal operators whose operations are dominated by these companies and their passengers. This group of companies, including related suppliers, currently represents the largest maritime cluster in the northern and central Baltic Sea. The Åland-based shipping companies within the cluster alone, generate a demand in the regions along the tax-free routes of up to one billion euros and contribute - directly and indirectly - to over 10 000 jobs. These companies have very few alternatives to their current operations, and would therefore be very hard hit if the sale of duty-free products and services would be abolished.

The considerable number of individuals that have become accustomed to today's comprehensive range of cheap and convenient ferry connections between Sweden, Åland and Finland can also be considered to be among the main losers. Indisputably, an abolishment of the duty free on-board sales would lead to a sharp reduction in the number of departures, to higher fares and less and more expensive on-board service.

Another category that would suffer is the businesses which regularly use the ferries on the tax-free routes for their shipments. However, these would probably have the opportunity to use alternative modes of transport. In some cases, though, the high frequency of departures and the option of direct delivery to ports in the very center of the region's metropolitan areas, is a competitive advantage that is difficult to achieve with the conventional freight shipping's less frequent schedules and with ports of calls located in the outskirts rather than in the central parts of the large consumer markets.

... and the main Winners

The most obvious actors benefitting from a non-tax free CBSR-scenario are companies specialized in Ro-Ro and Ro-Pax liner services and cruise ferry companies that can successfully compete on the remaining tax-free routes and the routes to destinations where on-shore prices are significantly lower than in Finland and Sweden. Other winners are the logistics companies, port and terminal operators that would benefit from a transfer of transport capacity from the previous tax-free routes to new routes and ports.

The main groups of potential winners from an abolition of the Åland tax exemption are:

- Cargo and Ro-Pax shipping companies and logistics operators in the CBSR
- Ports and terminal areas specialized in cargo shipping located close to the shortest sea routes between important hubs along the BSR's shores

- Cruise ferry companies that are able to expand their operations on the remaining tax-free routes
- Cruise ferry companies that can profit on differences in tax rates on alcoholic beverages and tobacco between the departing and arrival destinations

Unlike the concentration of potential ‘tax-free losers’ to Åland, and to some extent also to the centrally located metropolitan ports in Sweden and Finland, the group of potential winners from an abolishment of tax-free sales would be much more geographically dispersed.

The sea routes that would benefit from an abolishment of tax-free on board sales are primarily those with departures in Helsinki and the Baltic States; especially the two capitals of Tallinn (Estonia) and Riga (Latvia). Already today, these two destinations are among the main ports in the Baltic States for transport of cargo and people. Estonia and Latvia have lower tax levels on alcohol and tobacco than Sweden and Finland. Hence, they have become interesting destinations for cruise ferries, and also for other types of Ro-Ro and Ro-Pax ferries. Moreover, the two countries are an important part of the eastern Via Baltica-route.

An interesting shipping market in the outskirts of the main cruise ferry area is constituted by the routes between Helsinki, Tallinn, Riga and St. Petersburg. This easternmost part of the CBR would provide an opportunity for the ferry operators to continue tax-free on-board sales after a future abolishment of Åland’s special tax status. Since Russia is not an EU-member state it is considered as a third country from an EU tax perspective. Another reason for the growing market potential in this part of the region is that Russia offers a large cruise passenger market which is still not fully exploited. Thus, the main ports in the Baltic States in general and Russian St Petersburg in particular, would probably all be winners in the context of this scenario.

Overall BSR impacts: Losers in the West, winners in the East

The strongest impact of the abolition of duty-free sales on the sea routes via the Åland Islands would no doubt be on the ferry traffic area along the Sweden-Åland-Finland route connecting the two main transnational transport corridors between Scandinavia, western Russia, the Baltics and the European continent. If tax free sales were to terminate, the ferry traffic volume would be significantly reduced, and the remaining ferry transport would become considerably more expensive for customers. The first and most obvious effect of this would be a substantial reduction in the volume of passenger transport between Sweden, Åland and Finland as well as a decline in the supply of seaborne transport capacity for certain types of freight.

The western corridor from Stockholm to the European continent via Denmark and Germany, with its highly developed infrastructure, would probably retain most of its current traffic volume. The route might lose some of the shipments to/from the eastern parts of the CSBR, which now use the tax-free subsidized ferry service on the sea lanes between Sweden and Finland.

The map below presents an overall picture of the traffic and terminal areas, ports and regions that would suffer most from a deterioration of their transport logistics due to abolition of Åland's tax exemption - and those that could gain from such a future development.

Grisslehamn Eckerö Naantali Helsinki
Kapellskär Mariehamn Hanko Turku
Stockholm Tallinn
Nynäshamn Riga St. Petersburg

Baltic Sea

Winning area
Losing area

17

current role as the financial and logistic centre for ferry traffic between Sweden and Finland.

The principal winners are the major passenger- and cruise destinations in the northern parts of the *Via Baltica* corridor (i.e. St. Petersburg, Tallinn, Riga). Some of the specialized Ro-Ro ports and terminals outside the Finnish and Swedish capital region's central areas (i.e. Hanko and Nynäshamn) would probably also belong to those gaining some traffic and economic activities as a result of an abolishment of tax-free sales.

2 Introduction

2.1 Tax-free based ferry traffic in the central Baltic Sea Region

One of the main logistic systems for transports of people, cars, and cargo in the Baltic Sea Region (BSR) is built around car/cruise/cargo ferries, providing a link and motorway of the sea. These ferries supply an important part of the infrastructure linking the logistical flows between the different countries, regions and cities in the Central Baltic Sea Region (CBSR) and between BSR and the rest of EU.

Accordingly, passenger ferry operations are of great importance for the current transportation and logistics system in the CBSR. Ferry transports were originally introduced at the end of the 1950s as an option for travelling between Finland and Sweden. Subsequently, rapid growth in the Swedish economy during the 1960s boosted demand for labour for the manufacturing industry in the country, providing new opportunities for Finnish workers to immigrate to Sweden in search for work. This immigration, in turn, created a demand for transportation of people and cars between the two neighbouring countries and offered a new market opportunity for shipping companies to introduce new traffic alternatives and routes. The possibility of offering duty-free sales on board, granted early on revenue and profits for the shipping companies, supplying the means to expand their business.

Since the early 1960s, tax-free sales have been of crucial importance for ferry operations on the routes between Sweden, the autonomous island territory of Åland, and Finland. The new concept emerged around tax-free sales, entertainment and the possibility to transport cars and goods on scheduled time tables. The tax-free based ferry industry offered new opportunities for the logistics system in the CBSR and brought about a large expansion of capacity for transportation of passengers, cars and cargo.

Today, a significant part of the seaborne transport infrastructure in the northern and central BSR (including *Nordic Triangle*, *Baltic Palette*) is built around and sustained economically by tax-free sales on board ferries travelling along the sea lanes via Åland to and from Sweden, Finland and Estonia - and recently also to Russia (St Petersburg).

The reason for this is that Åland is one of the few territories in EU where tax-free sales on board ships traveling to and from the rest of the Union are allowed. This is due to a permanent exemption from the European VAT-rules in Åland's accession protocol to the EU.¹

2.2 Purpose and the main research question

The aim of this report is to highlight the consequences for the transnational and interregional transport of goods and people in the Central and Northern Baltic Sea region if duty free sales on board the ferry traffic via Åland, were to disappear.

What would remain of today's extensive ferry traffic on the routes between Stockholm-Mariehamn-Turku-Helsinki-Tallinn-St Petersburg? What new routes and modes of transportation would evolve? How would the traffic to existing population centres, ports and terminal areas be affected? Who would we expect to lose, and who would win? How would the overall transport logistics between the Baltic Sea Region and the wider EU be affected?

2.3 Research method and sources

This project combines qualitative information and analysis with quantitative data concerning sea borne transportation flows in the BSR. The qualitative part of the research is built on a number of in-depth interviews with top-executives of leading shipping companies and representatives of other related logistics actors (see Appendix p. 68). The interviews were conducted between June and September 2011.

The overview of the present sea borne transport infrastructure, routes, nodes, flows of people and goods in the Baltic region is primarily based on national and regional transportation and trade statistics from various sources.

The Finnish Transport Infrastructure Agency has data on seaborne international transport to and from Finland of passengers and goods by country (Sweden, Estonia, Russia, Germany, foreign cruise ships and others), by port (all major ports in Finland and Åland). Most of these data are available by year and month.

Statistics and Research Åland (ÅSUB) provides data on sea passengers and vehicles

¹ The European Commission has granted several similar exemptions to the general rule within the Union concerning the abolishment on tax-free sales on internal routes after June 30, 1999. These territorial exemptions included e.g. German Helgoland, Spanish Ceuta, Melilla the Canary Islands, Italian town of Livigno and the Lake Lugano area. See Terra & Wattel (2008).

handled at Åland ports, by year. The report uses *Eurostat* for data on maritime transport of passengers at regional EU level and other transport statistics, including trade by mode of transport.

Transport Analysis (TRAFA, Sweden) provides data on goods handled in Swedish ports by type of traffic, etc. Moreover, *Statistics Estonia* has data on shipping traffic (goods and passengers) through Estonian ports by country (Finland, Sweden, Germany, foreign cruise ships and others) and by year and quarters.

3 Sea transport logistics and tax-free sales in the Baltic Sea Region

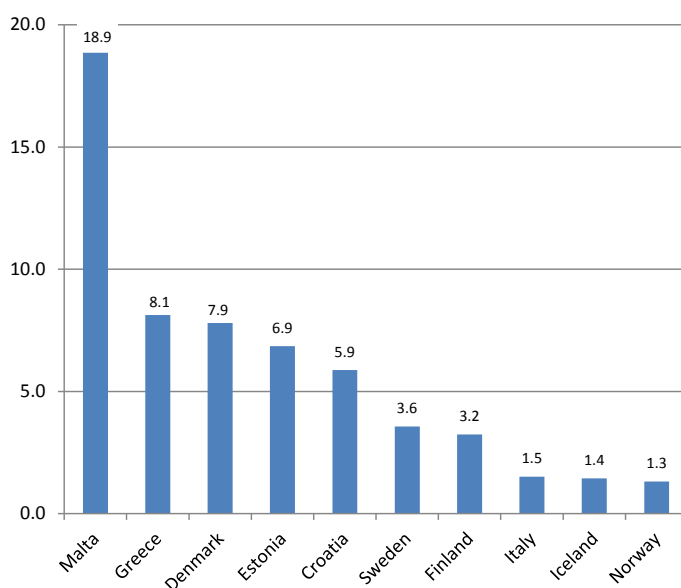
3.1 Introduction

This chapter presents an overview of baseline facts and statistics regarding seaborne transportation in the Baltic Sea region (BSR). It focuses primarily on the tax-free ferry traffic in the Central Baltic Sea Region (CBSR) and relates that to the EU and the various national and regional levels. We also seek to establish the relative significance of maritime transport of passengers and goods in the CBSR. How important is the ferry traffic across the sea of Åland, the Northern Baltic and the Gulf of Finland? How important are the tax-free routes in relation to other routes in the Baltic Sea area? What is the role of the duty-free supported shipping business in the transport system connecting Sweden and Finland?

3.2 Sea passenger transport in EU and the Baltic Sea Region

The relative intensity of sea passenger transport of a country or a region is revealed by simply calculating the number of sea passengers per inhabitant in the territory. *Figure 1* illustrates sea passenger transport intensity of the top ten EU27 countries.

Figure 1. Sea passenger transport intensity in EU27 and Norway. Passengers per inhabitant 2008. Top ten countries



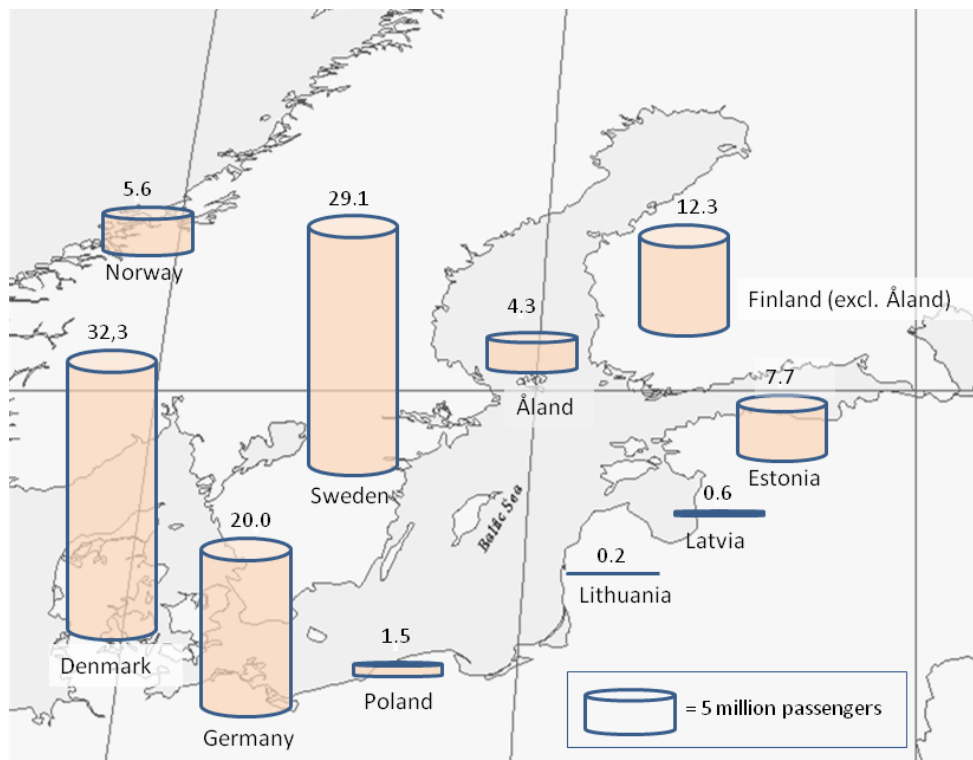
Source: Eurostat

Four countries situated in the BSR rank among the top ten most intense countries in this respect within EU27, that is, Denmark, Estonia, Sweden and Finland. In 2008, Denmark had 7.9 sea passengers per inhabitant, which was close to the relative intensity of Greece. Intensity of Estonia's maritime passenger traffic was 6.9. Moreover, Sweden and Finland ranked 6th and 7th within EU27.

The Åland Islands, the autonomous part of Finland, which is excluded from the EU tax area, exhibits a far higher intensity of maritime passenger traffic than all of the countries mentioned above. There maritime passenger traffic intensity was higher than 150 seaborne passengers per inhabitant in 2008.

The obvious conclusion of these data is that maritime passenger transport to countries situated in the BSR is a decidedly important part of the transport infrastructure of the region. Consequentially, seaborne passenger traffic in the Baltic Sea is a significant means of travelling between countries, regions and cities in the area. According to data from Eurostat, approximately 120 million passengers are transported between countries in the BSR (excluding Russia) (See *Figure 2*).

Figure 2. Number of seaborne passengers in the Baltic Sea Region 2009 (millions), by country



Source: Eurostat

More than a quarter of maritime passenger transport in EU27 is carried out in the Baltic. Danish port of Helsingør, Swedish Helsingborg, and Finnish Helsinki, are the largest

passenger transport nodes in the area (*Table 1*), each of them accounting for in excess of 9 million arrivals and departures in 2009. *The significance of the tax free area of the Åland Islands is demonstrated by the disproportionate number* (in relation to the number of inhabitants (circa 28 000) of the area) *of seaborne passengers travelling to and through that location* (4.3 millions, *Figure 2*).

Table 1. Seaborne passenger traffic to and from major Baltic ports of the EU 2000-2009 (1 000 passengers, embarked and disembarked)

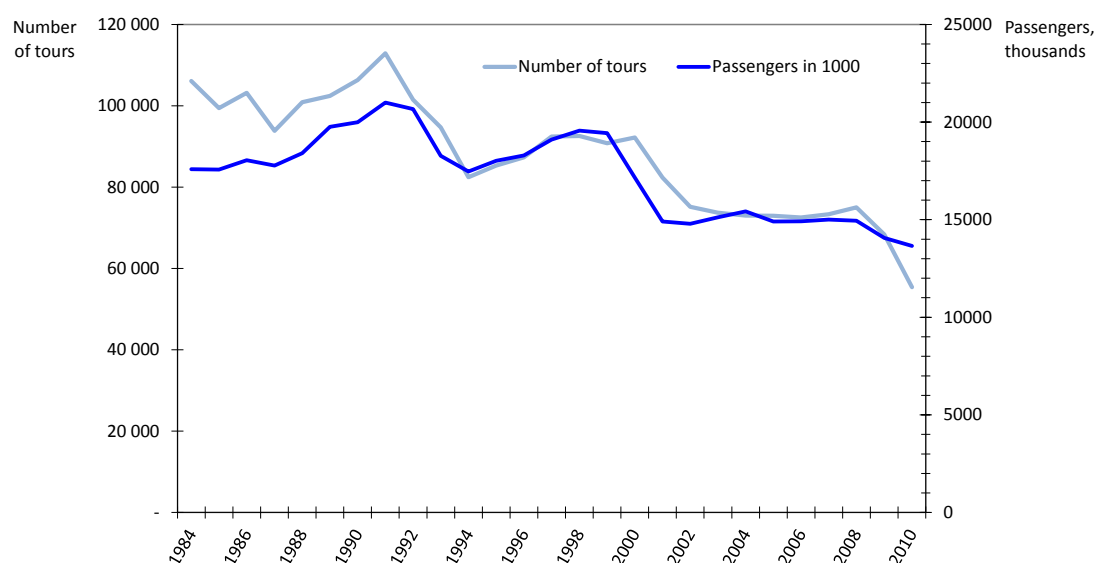
Port	Country	2000	2005	2006	2007	2008	2009	% change
								08/09
Helsingør	DK	13 322	11 023	10 721	10 966	10 912	9 415	-13.7
Helsingborg	SE	13 525	11 102	10 776	10 966	10 911	9 415	-13.7
Stockholm*	SE	7 746	8 211	8 054	8 127	8 677	9 089	4.7
Helsinki	FI	9 251	8 854	8 548	8 561	8 976	9 085	1.2
Tallinn	EE	..	6 701	6 447	6 220	6 870	6 841	-0.4
Puttgarden	DE	5 430	6 760	6 789	7 069	6 768	6 305	-6.8
Rødby (Færgehavn)	DK	5 430	6 761	6 789	7 058	6 756	6 305	-6.7
Turku	FI	3 514	3 697	3 620	3 480	3 488	3 520	0.9
Mariehamn	AX	1 885	3 192	3 099	3 125	3 306	3 394	2.7
Rostock	DE	1 767	2 417	2 557	2 585	2 713	2 431	-10.4
Ystad	SE	1 136	1 815	1 937	1 878	1 857	1 823	-1.8
Kiel	DE	1 108	1 485	1 474	1 559	1 761	1 772	0.6
Visby	SE	1 291	1 460	1 472	1 565	1 583	1 629	2.9
Trelleborg	SE	2 086	1 691	1 697	1 816	1 821	1 556	-14.6
<i>Total</i>		<i>67 491</i>	<i>75 169</i>	<i>73 980</i>	<i>74 975</i>	<i>76 399</i>	<i>72 580</i>	<i>-5.0</i>

*) Including Kapellskär and Nynäshamn

Source: Eurostat

3.3 Passenger traffic at Swedish ports

Although the number of seaborne passengers traveling through Swedish ports has gradually diminished since the beginning of the 1990s the number is still significant in a European perspective. *Figure 3* shows the number of passenger ships and ferries, and passengers entering Swedish ports 1984-2010, which is roughly half of the number of passengers traveling annually. The sharp decline in 2000 is due to the opening of the bridge over Öresund that year.

Figure 3. Arrivals of passenger ships and ferries at Swedish ports 1984-2010

Source: TRAFKA (2011)

Seaborne passenger traffic to and from Swedish ports is highly concentrated to the Central Baltic and the Öresund regions.² In 2010 passengers to and from Denmark accounted for 42 per cent of total, passengers to and from Finnish ports for 35 per cent, passengers to and from German ports for 8 per cent of total (*Table 2*). The large part, almost 90 per cent, of international maritime passenger traffic in to and out of Swedish ports is to and from ports in the Baltic Sea.

Table 2. Seaborne passengers entered into and cleared from Sweden 2010, by country (number of passengers and percentages)

	Passengers	Share of total (%)
Total 2010	26 814	100
Denmark	11 146	42
<i>Danish ports in Öresund</i>	<i>8 540</i>	<i>32</i>
<i>Other Danish ports</i>	<i>2 607</i>	<i>10</i>
Finland (incl. Åland)	9 391	35
Germany	2 050	8
Other countries	4 227	16

Source: TRAFKA (2011)

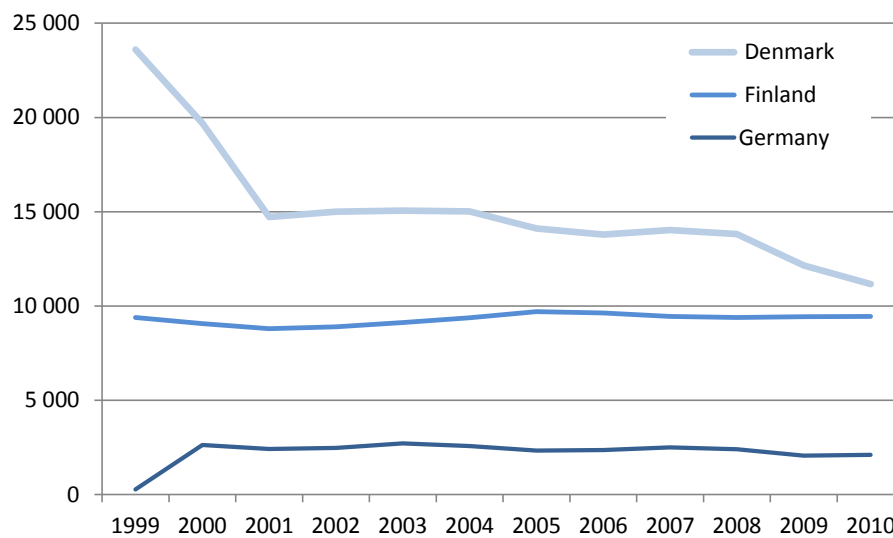
Since almost all maritime passenger traffic between Sweden and Finland takes place along routes that benefit from on-board tax-free sales, we can conclude that *more than a third of Sweden's maritime passenger transportation occurs along routes sustained by*

² The bridge across Öresund opened 1 July 2000 reducing the number of arrivals from Denmark to Sweden from approximately 24 million in 1999 to 15 million in 2001 and 11 million in 2010. See Swedish Passenger Ship Association (2011).

tax free sales.

The intensity of southward going passenger traffic on board ferries from Sweden has gradually declined since the mid-2000s (*Figure 4*). Moreover, the intensity of passenger traffic on routes to and from German ports has declined slightly during the same period, whereas traffic on Finland has stagnated.

Figure 4. Arrivals and departures on board ferries in Sweden to and from Denmark, Finland and Germany 1999-2010 (thousands of passengers)

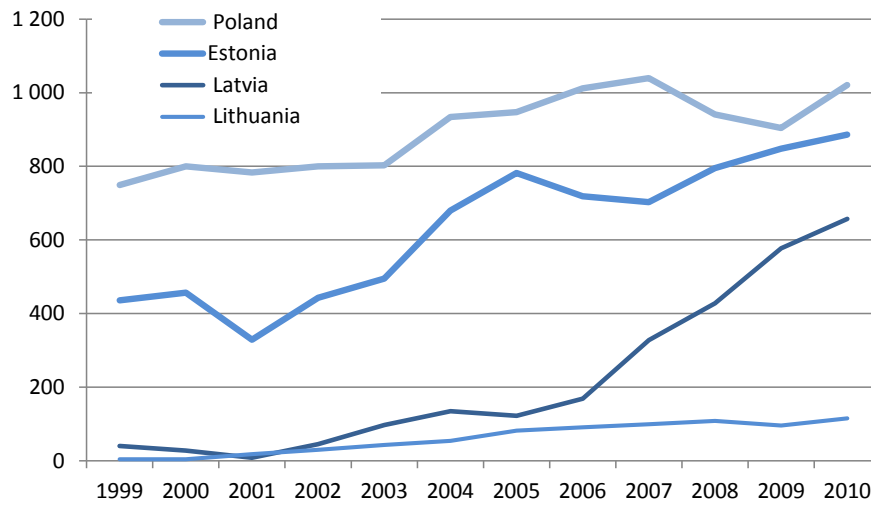


Source: Swedish Passenger Ship Association (2011)

Obviously, as illustrated by *Figure 5* below, growth in Sweden's passenger traffic during the 2000s has occurred in the routes to Poland, and especially in the traffic to and from the Baltic states; Estonia, Latvia and Lithuania.

To sum up, ferry passenger transportation to and from Swedish ports has declined with Denmark and Germany, stagnated with Finland, and increased significantly with Poland and the Baltic states.

Figure 5. Arrivals and departures on board ferries in Sweden to and from Poland, Estonia, Latvia and Lithuania 1999-2010 (thousands of passengers)

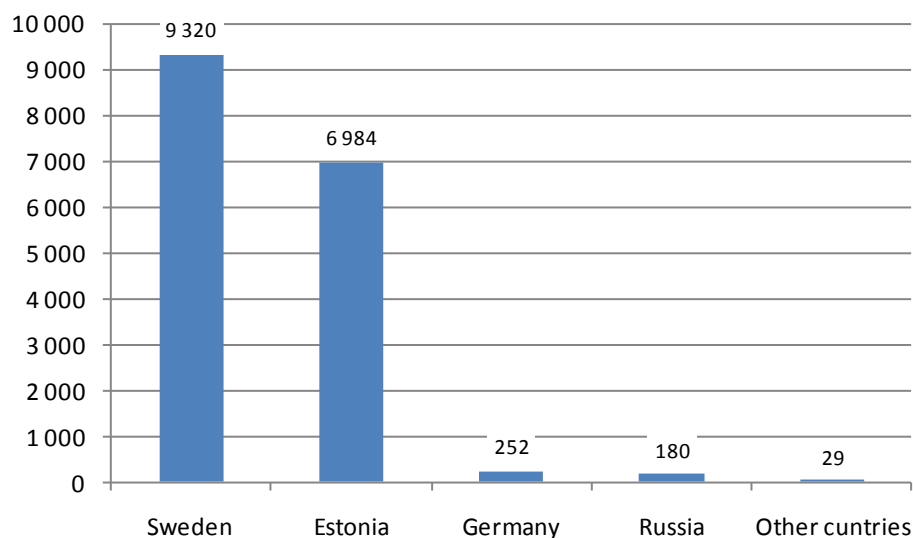


Source: Swedish Passenger Ship Association (2011)

3.4 Passenger traffic to and from Finnish ports

Maritime passenger traffic into and out of Finnish ports is highly concentrated to the Central Baltic Triangle (see section 3.8 and *Figure 12*, p. 36); namely to Sweden and Estonia (*Figure 6*). Sweden accounts for 56 per cent of passenger traffic to and from Finnish ports, Estonia for 42 per cent.

Figure 6. Passenger traffic into and out of Finnish ports (incl. Åland) by country 2010 (Thousands of passengers). Excluding foreign cruise passengers



Source: Finnish Transport Infrastructure Agency

As mentioned previously, all passenger traffic between Finland and Sweden occurs along routes that benefit from on board tax-free sales.

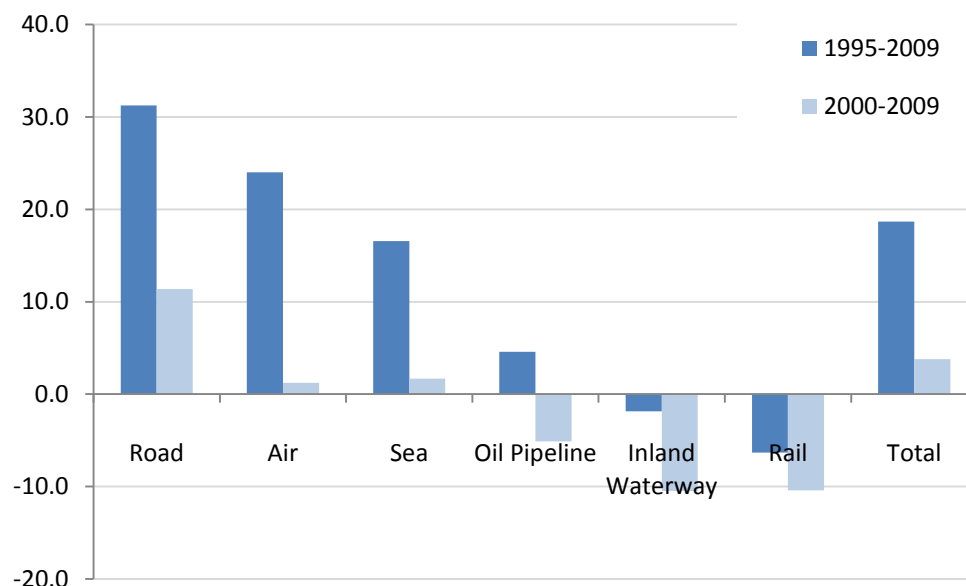
Consequently, *more than half of Finland's maritime passenger transports are tax-free supported.*

3.5 Seaborne goods transports in EU and the BSR

Statistics on the foreign trade of EU27 member states by mode of transport show that annual growth in transport by road and by air outpaced that by sea during the 1995-2009 period (*Figure 7*). In 2000-2009 transport by road increased by 11.4 per cent whereas transport by air grew by merely 1.2 per cent and transport by sea by no more than 1.7 per cent.

Hence, during the last decade and a half, sea transportation in the European Union has lost ground. Total EU 27 international transport growth expressed in billion tonne-kilometres (BTKM) grew by 18.7 per cent compared with road transport, which grew by 31.3 per cent during the 1995-2009 period and by 11.4 per cent in 2000-2009.

Figure 7. EU27 growth of various modes of freight transport (BTKM)* 1995-2009 and 2000-2009 (per cent)



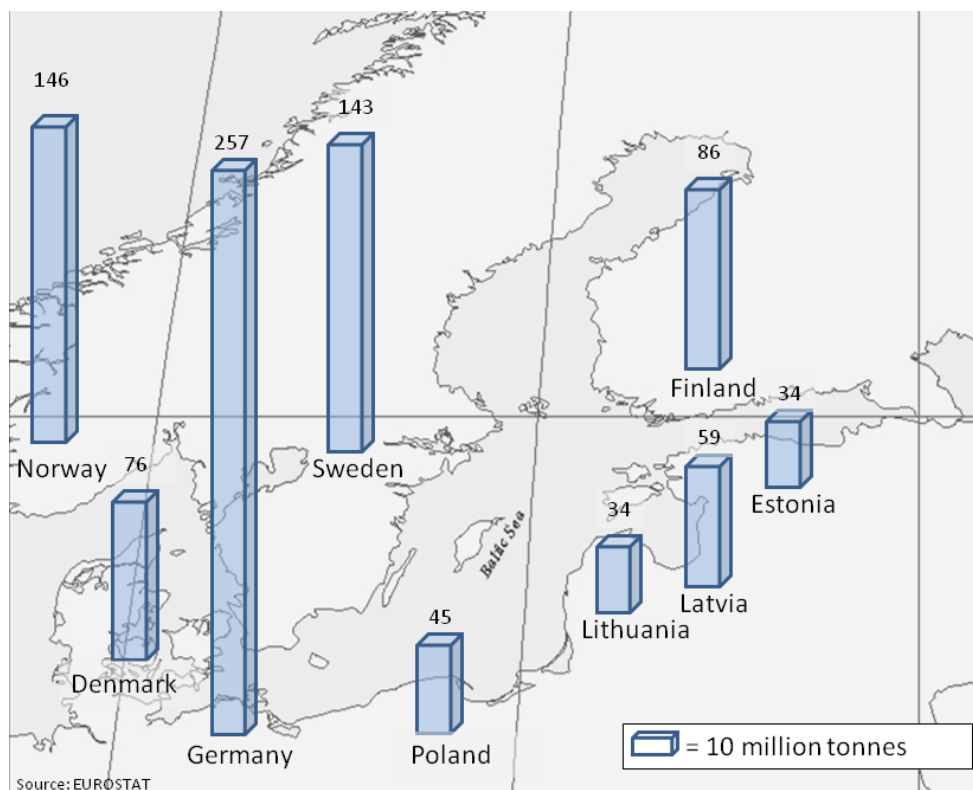
*) Billion tonnes per kilometre

Source: European Commission, Mobility & Transport (2011). Authors' own calculations

However, the staples in *Figure 8* illustrating the weight of goods transported, tells us that in the BSR, shipping is still a significant means of transportation. This, of course, is due to geographical proximity and a high level of commercial and cultural integration especially among the Nordic countries.

‘Short sea shipping’ is a term frequently used to denote maritime transport of goods that does not cross an ocean. *Figure 8* below shows the large amount of goods transported between countries in the Baltic Sea in 2009. The amounts transported per country all correspond to the size of the individual economies. Accordingly, the largest economy, Germany, accounts for the largest amount traded; 257 million tonnes in 2009.

Figure 8. Short Sea Shipping of EU countries and Norway in the Baltic Sea Area by country in 2009 (gross weight, millions of tonnes)



Including transports in to and out of Russian ports significantly increases the intensity of short sea shipping in the Baltic Sea Area. In 2008 three Russian ports ranked highest by total cargo volume; Primorsk, St. Petersburg, and Klaipeda, as demonstrated in *Table 3*, which lists the largest ports in the Baltic Sea.

Table 3. Largest ports in the Baltic Sea by total cargo volume in 2008 (million tonnes)

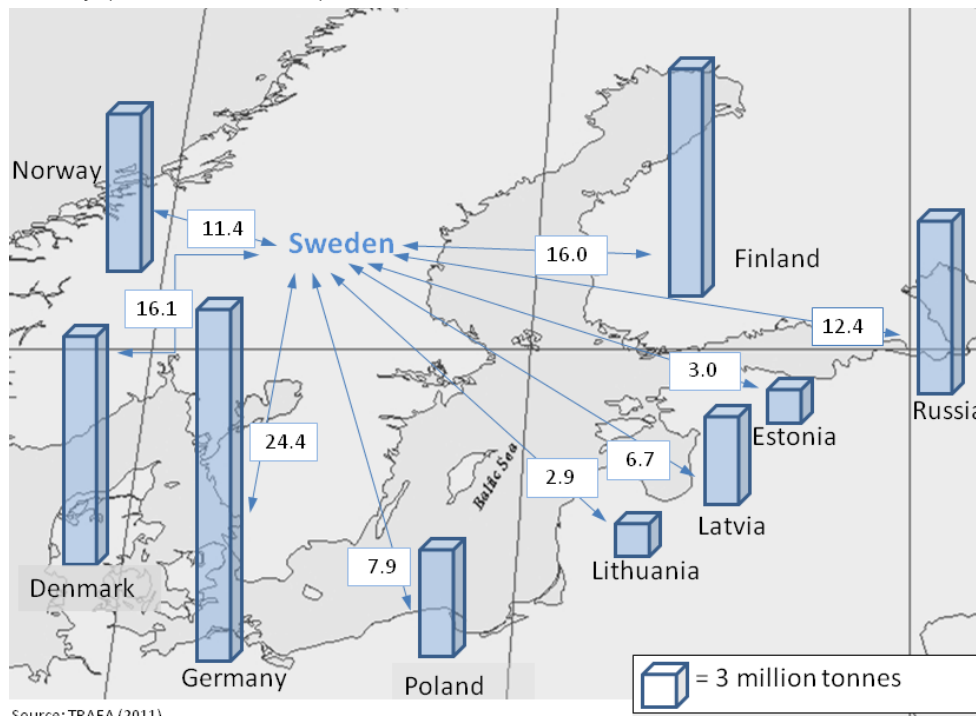
Primorsk	75.6
St. Petersburg	60.0
Klaipeda	29.9
Riga	29.6
Tallinn	29.0
Ventspils	28.6
Kilpilahti/Sköldvik	21.6*
Lübeck	21.3
Rostock	21.3

*) Only international

Sources: Baltic Maritime Transport Journal 12/2010

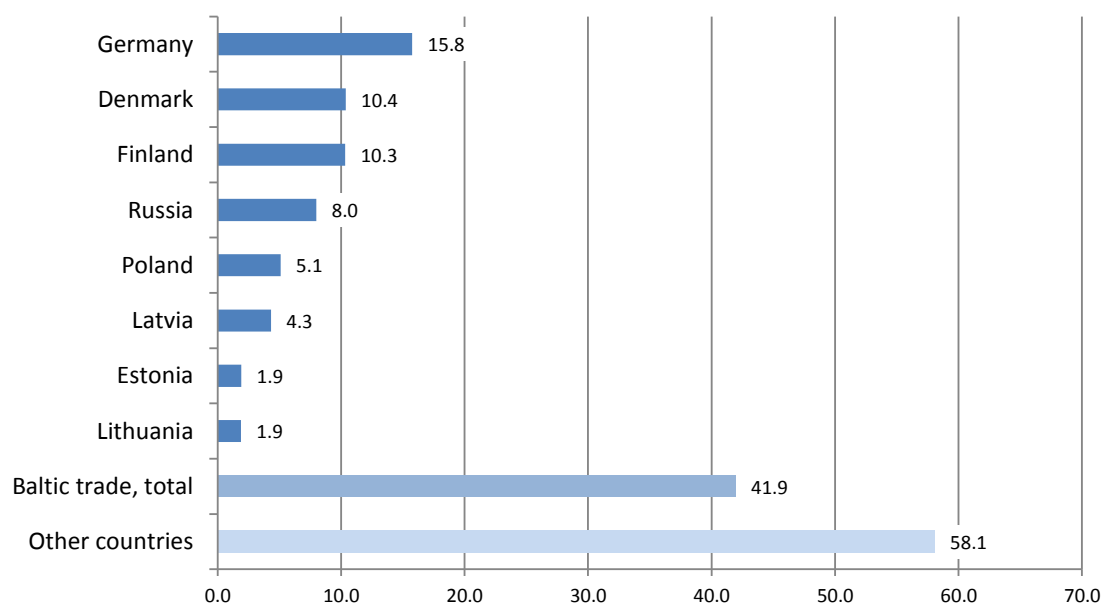
3.6 Sweden's seaborne trade

A large part of Sweden's international seaborne trade is with other countries in the Baltic Sea Area (*Figure 9*). Trade with Germany – Sweden's largest trading partner – amounted to 24.4 million tonnes, trade with Denmark to 16.1 tonnes and trade with Finland to 16.0 million tonnes in 2009.

Figure 9. Transport of goods in the Baltic Sea Area in to and out of Swedish ports, 2009 by country (millions of tonnes)


In 2010, 42 per cent of goods traded in and out of Swedish ports were traded with other countries in the Baltic Sea Area, and consequently 58 per cent was traded with other areas.

Table 4. Sweden's seaborne Baltic goods transports by country and region in 2010, (tonnes, percentage shares)



Source: TRAFRA 2011

Moreover, Sweden is highly integrated with the EU as regards maritime trade with goods. As *Table 5* reveals, EU countries accounted for almost three quarters of Sweden's seaborne goods trade (74.1 per cent).

Table 5. Shipping of goods between Sweden and foreign countries in 2010, according to dispatching country (1 000 tonnes and percentages of total)

	To Sweden		From Sweden		Total	
Total	84 372	100.0	70 624	100.0	154 995	100.0
Germany	11 068	13.1	13 366	18.9	24 434	15.8
Denmark	9 919	11.8	6 161	8.7	16 081	10.4
Finland	6 999	8.3	9 008	12.8	16 007	10.3
Latvia	6 370	7.6	331	0.5	6 702	4.3
Great Britain	4 721	5.6	8 926	12.6	13 647	8.8
Poland	4 315	5.1	3 606	5.1	7 921	5.1
Belgium	4 059	4.8	5 319	7.5	9 378	6.1
The Netherlands	3 626	4.3	4 843	6.9	8 469	5.5
Estonia	2 196	2.6	779	1.1	2 975	1.9
Lithuania	1 991	2.4	954	1.4	2 945	1.9
France	643	0.8	1 601	2.3	2 244	1.4
Spain	489	0.6	1 516	2.1	2 005	1.3
Portugal	323	0.4	241	0.3	564	0.4
Italy	305	0.4	227	0.3	532	0.3
Ireland	218	0.3	310	0.4	528	0.3
Greece	192	0.2	104	0.1	295	0.2
Other EU countries	17	0.0	144	0.2	160	0.1
EU	57 450	68.1	57 437	81.3	114 887	7.1
Russia	11 462	13.6	917	1.3	12 379	8.0
Norway	8 632	10.2	2 735	3.9	11 368	7.3
Island	25	0.0	80	0.1	105	0.1
Other, non-EU countries	6 802	8.1	9 454	13.4	16 256	10.5

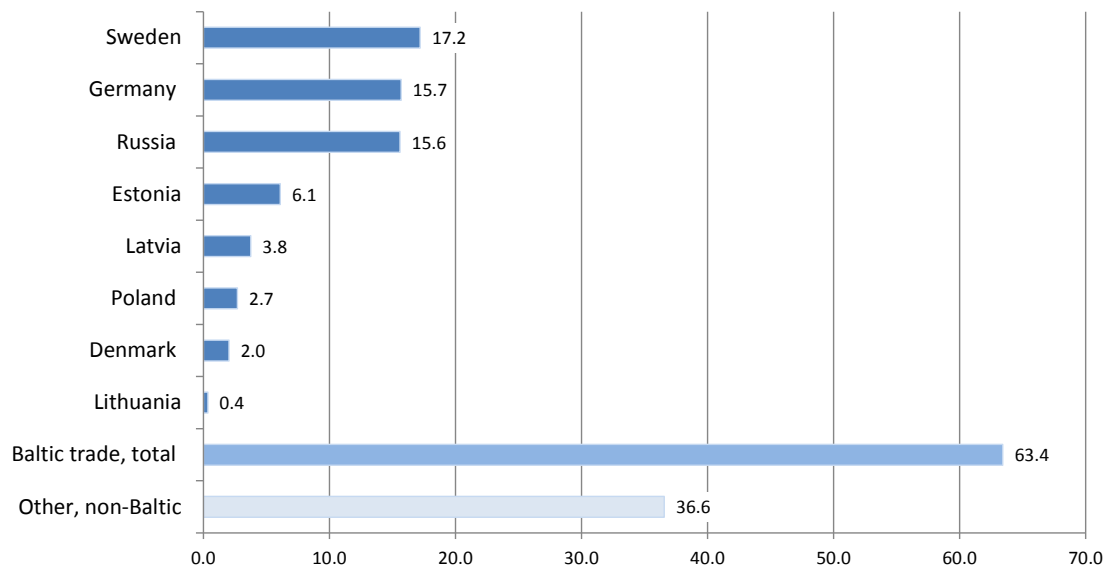
Source: TRAFRA (2011)

3.7 Finland's seaborne trade

Finland is even more closely integrated with the countries in the BSR than Sweden. As demonstrated in *Figure 10* Finland's international seaborne trade is highly concentrated to the Baltic. In 2010, almost two thirds (63.4 per cent) of the goods traded on Finnish ports were with the countries around the Baltic. Finland's trade in West-East, East-West direction (with Sweden and Russia) accounted for a third (32.8 per cent) of total Finnish intra-Baltic seaborne goods trade.

A significant share of goods traffic to and from Finnish ports is constituted by transit traffic, that is, goods reloaded from ships in Finnish harbours on to heavy lorries destined for Russia, and more importantly, the other way around; goods produced in Russia reloaded on to ships in Finnish harbours.

Figure 10. Finland's seaborne goods transports by country in 2010, (tonnes, percentage shares)



Source: Finnish Transport Infrastructure Agency. Authors' own calculations

Table 6 below shows total and transit trade in to and from Finnish ports in 2010. As we see, almost 13 per cent of exports were transit goods traffic. The same year, share of transit destined mainly for Russia in imports was 4 per cent.

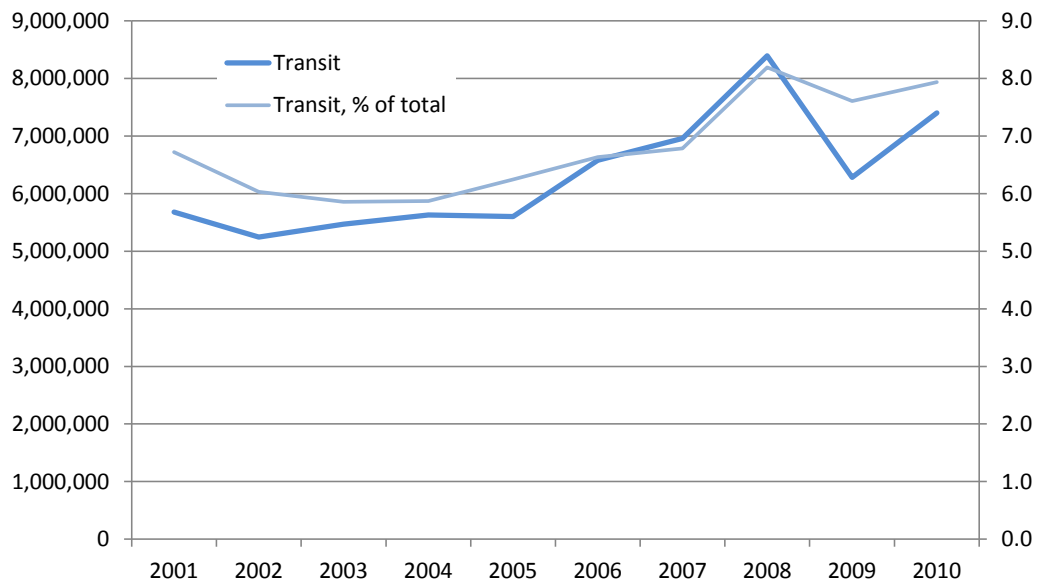
Table 6. Total and transit trade in to and from Finnish ports 2010

	Imports	Exports	Total trade
Total	51 487 514	41 786 412	93 273 926
Transit	2 053 256	5 349 530	7 402 786
<i>Transit, % of total</i>	<i>4.0</i>	<i>12.8</i>	<i>7.9</i>

Source: Finnish Transport Infrastructure Agency (2011). Author's own calculations

The share of total transit trade through Finnish ports has increased slightly during the last decade (see *Figure 11*).

Figure 11. Transit transportation of goods to and from Finnish ports, 2001-2010 (tonnes and share of total goods handled)



Source: Finnish Transport Infrastructure Agency (2011)

3.8 A tax-free sustained Baltic Triangle of transnational ferry traffic

Ever since the establishment of the first passenger ferry lines between Sweden, Åland and Finland in the late 1950s and early 1960s the ferry companies benefitted from selling duty-free alcohol and tobacco on board. This profitable arrangement was threatened when Finland was to join the European Union in 1995. However, the autonomous Åland Islands managed to negotiate a permanent exemption from the EU value added tax area for the archipelago. Hence, the ferry companies were able to continue the profitable tax free sales on board.

When Estonia joined the EU in May 2004, duty-free sales on direct routes from Sweden to Estonia and from Finland to Estonia were abolished. Instead, the exemption of Åland from the EU customs union provided a possibility to continue tax-free sales on board ferries calling at the ports of Mariehamn or Långnäs, when destined for Estonia, and thus continuing selling tax free on board.

Currently (2011) the main passenger route from Sweden to Estonia calls at the port of Mariehamn. The number of arrivals at the port of Tallinn from Stockholm were 437 602 in 2010 (*Figure 12*). These are, indeed, significant numbers in a comparative European perspective.

Table 7. Major intraregional tax-free and non-tax-free maritime passenger routes in the Central Baltic

<i>Tax-free</i>	Stockholm	↔	Mariehamn, Åland	↔	Helsinki
<i>Tax-free</i>	Stockholm	↔	Mariehamn	↔	Turku
<i>Tax-free</i>	Stockholm	↔	Långnäs, Åland	↔	Turku
<i>Tax-free</i>	Stockholm	↔	Mariehamn	↔	Tallinn
<i>Non-tax-free</i>				Helsinki ↔ Tallinn	

There is currently (October 2011) several regular tax-free routes to and from Åland (Table 7):

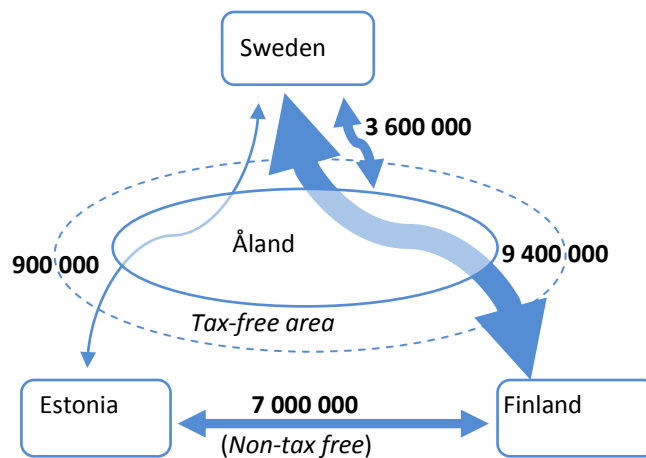
- Regular cruise lines between Stockholm and Mariehamn (Åland)
- A regular cruise/transport line between Grisslehamn (Sweden) and Berghamn, Eckerö (Åland)
- Regular cruise/transport lines between Stockholm, Mariehamn and Finland (Turku and Helsinki)
- A regular cruise/transport line between Stockholm, Mariehamn and Estonia (Tallinn)

Moreover, there is now a regular (weekly) cruise line between Stockholm, St. Petersburg, Helsinki, Mariehamn, and Tallinn.

Together, these routes with their logistic and commercial centre in Mariehamn, constitute what could be labelled a *Central Baltic Triangle* (CBT) of duty-free supported ferry routes between Sweden, Åland, Finland and Estonia. As we mentioned earlier, the third ‘leg’ of the original CBT, the one between Finland and Estonia, no longer has the privilege of selling tax free.

The tax-free routes continue to represent the backbone of seaborne transports between Sweden and Finland, transporting more than 9 million passengers a year between Stockholm and Turku and Helsinki (Figure 12).

Figure 12. Central Baltic Triangle: Major tax-free and non-tax-free links. Number of maritime passengers* in 2010

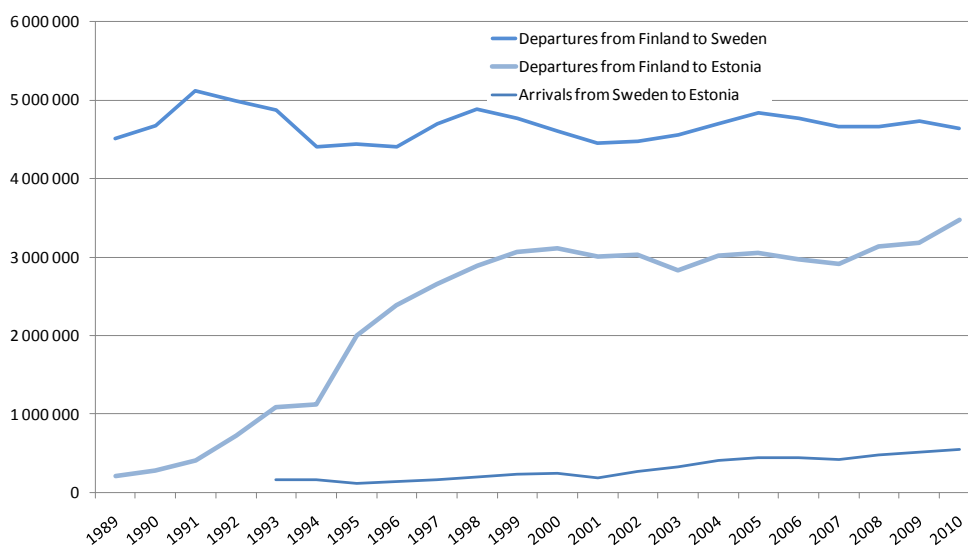


*) Arrivals and departures. Approximate figures

Source: Statistics Estonia, Statistics Finland, Statistics and Research Åland

Interestingly, the positive growth of the volume of passengers in the Central Baltic triangle during the last two decades can almost entirely be attributed to the non-tax-free route between Finland and Estonia (*Figure 13*). However, even in this case, the price differences in alcohol appear to be the main reason for this astonishing growth. Many of the passengers travelling from Finland to Estonia do day-trips to Tallinn in order to buy cheap Estonian alcohol.

Figure 13. Maritime transport of passengers between Finland, Sweden and Estonia 1989-2010



Source: Finnish Transport Agency (2011), Statistics Estonia

Obviously, the Åland tax-free area is still very important for the ferry and cruise companies, since their routes between Sweden, Finland and Estonia (the ‘Central Baltic Triangle’) all involve calling at one of the tax-free ports of Åland (Mariehamn, Eckerö or Långnäs). *Figure 14* shows the considerable size of the flows of passengers traveling to or through the tax-free area.

The population of Sweden, Finland and Estonia account for no more than 3.2 per cent of the population of EU27, yet inward regular seaborne passenger transports to these three countries amount to roughly 15 per cent of the corresponding EU27 total.³ Obviously these three countries account for a significant and disproportionate share of EU seaborne passenger traffic.

Figure 14. Central Baltic Triangle: Major tax-free and non-tax free maritime connections between Åland, Sweden, Finland and Estonia. Number of passengers (1 000) in 2010



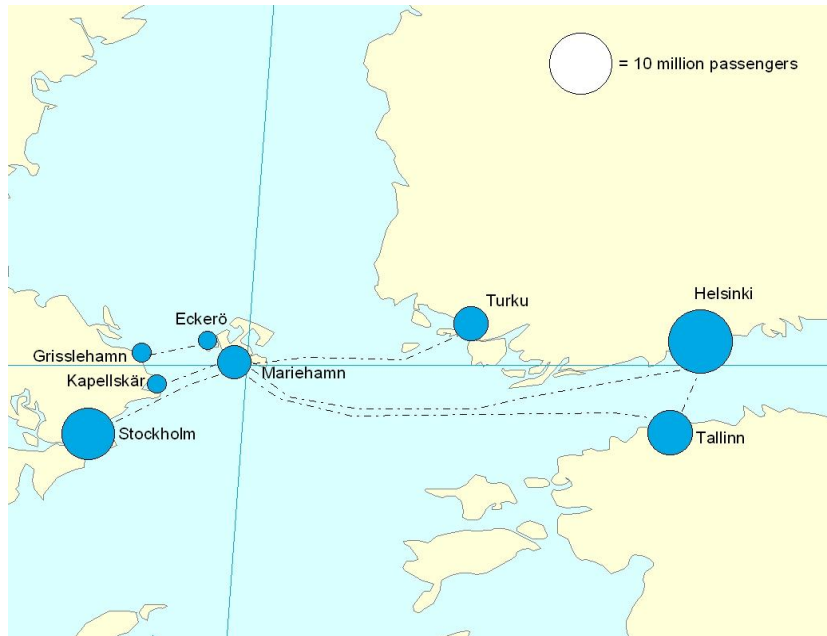
Source: Finnish Transport Infrastructure Agency (2011), Statistics Estonia, Statistics and Research Åland

Figure 14 summarizes the flows of maritime passenger traffic in the Central Baltic Triangle. Beginning from West to East we have the entirely tax-free routes between Sweden and Åland, which carried approximately 3.6 million passengers in 2010. Secondly, the major tax-free connections between Sweden and Finland carried approximately 9.4 million passengers the same year. The route between Sweden

³ Author's own calculations based on data from Eurostat

(Stockholm) and Estonia (Tallinn) carries approximately 0.9 million passengers annually. Finally, the non-tax free lines running between Finland and Estonia carry approximately 7.0 million passengers annually. All together the annual flow of passengers in the CBT exceeded 21 million in 2010, of which 15 million on tax free routes.

Figure 15. The largest passenger ports in the Central Baltic



Source: Finnish Transport Infrastructure Agency (2011), Statistics Estonia, Statistics and Research Åland, Swedish Passenger Ship Association (2011)

The flows of passengers and goods along the tax free routes in the CBT sustain a large part of the activity in the ports of the Stockholm area, in the Finnish south-western port of Turku and in Helsinki (See *Figure 15*).

Obviously Åland's exemption from the EU's VAT territory *is of great importance for the maritime passenger traffic in the area, primarily the traffic between Sweden, Åland and Finland*.

3.9 The significance of tax-free ferries in central Baltic cargo shipping

The major ferry companies in the CBT; Viking line and Tallink publish annual data on the number of 'cargo units' which are transported (*Table 8*). Moreover, Swedish TRAFPA publish data on the weight of goods shipped to and from Swedish ports, which provides us with the possibility of calculating the relative importance of goods transport on board tax-free ferries between Sweden and Finland.⁴

⁴ TRAFPA (2011)

Table 8. Number of cargo units on tax-free routes transported by Viking line and Tallink in 2010

	Sweden-Finland	Sweden-Estonia	Total
Viking Line	62 563	..	62 563
Tallink*	91 412	33 278	124 690

*) September 2009-December 2010. Figures include non-tax free supported transport of cargo vessel m/s Regal Star during summer months

Source: Viking Line and Tallink annual reports. Author's own calculations

Table 9 shows various shares of tax-free ferries in the CBSR in transport of goods to and from Sweden (percentages) 2010. Close to half of the goods transported from Finland to Sweden (48.5 per cent) on lorries/trucks, was on board the tax-free ferries travelling via Åland, slightly less the other way; from Sweden to Finland (47.6 per cent). The share of these ferries in total transports of goods on lorries/trucks on board ferries to Sweden was 6.0 per cent, and the proportion was the same for goods from Sweden. Finally, the share of tax-free ferries in total maritime transports of goods to Sweden was 1.4 per cent, and in goods shipped from Sweden 1.8 per cent.

Table 9. Various shares of tax-free ferries in seaborne transport of goods to and from Sweden (tonnes, percentages) 2010

In maritime transport of goods from Finland to Sweden on lorries/trucks	48.5
In total maritime transport of goods on lorries/trucks to Sweden	6.0
In total maritime transport of goods shipped to Sweden	1.4
In transport of goods from Finland	16.5
In transport of goods from Sweden to Finland on lorries/trucks	47.6
In total transport of goods on lorries/trucks from Sweden	6.0
In goods shipped from Sweden	1.8
In transport of goods to Finland	14.0

Source: TRAFKA (2011). Author's own calculations

Table 10 demonstrates the importance of the tax-free routes for Finnish transport logistics. The percentage share of tax-free ferries in transports to Sweden was 17.1. Here, we need to mention that the result based on calculations using Finnish data differ somewhat from our previous figure based on data from Swedish sources (16.5 per cent).

The share of tax-free ferries in total outgoing seaborne transports from Finland was 2.8 per cent. The share of these ferries in ingoing maritime transports to Finland was

somewhat lower; 13.5 for transports from Sweden (corresponding calculations based on Swedish data gave 14.0 per cent). Regarding the share in total ingoing maritime transports to Finland, the share of tax-free routes was 2.4 per cent.

Table 10. International sea transports of goods to and from Finland (total, to and from Sweden and on board tax-free ferries) 2010

	1 000 t and per cent
From Finland	41 786.4
To Sweden from Finland	6 745.0
To Sweden from Finland on board tax-free ferries	1 156.3
<i>Share of tax-free ferries in goods transports to Sweden (per cent)</i>	<i>17.1</i>
<i>Share of tax-free ferries in all goods shipped from Finland (per cent)</i>	<i>2.8</i>
To Finland	51 487.5
From Sweden to Finland	9 300.1
From Sweden to Finland on board tax-free ferries	1 260.1
<i>Share of tax-free ferries in transports from Sweden to Finland (per cent)</i>	<i>13.5</i>
<i>Share of tax-free ferries in total goods shipped to Finland (per cent)</i>	<i>2.4</i>

Source: TRAFA (2011), Finnish Transport Agency (2011). Authors' own calculations

Accordingly, we find that tax-free ferries play an even more important role in Finnish transport logistics than they do for Swedish.

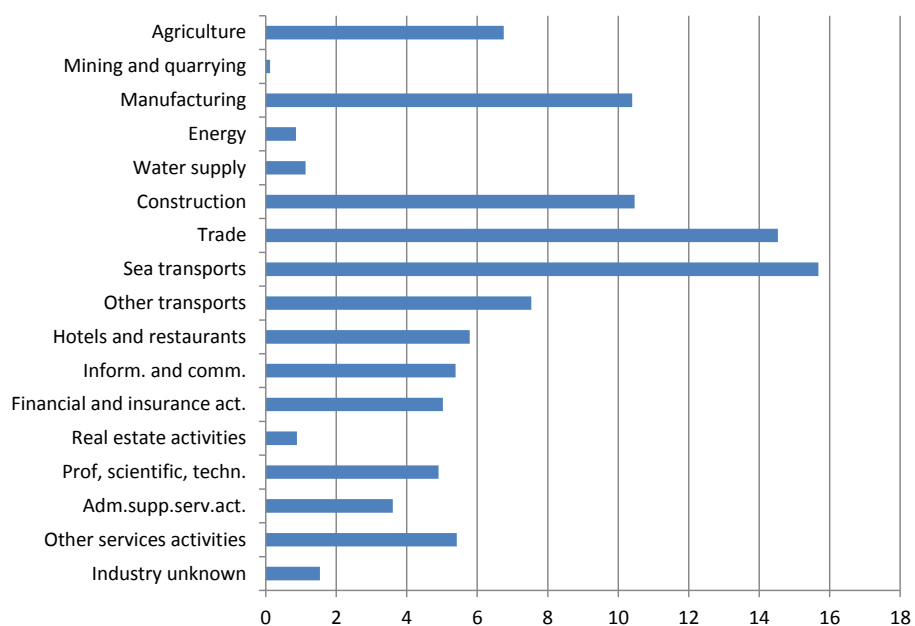
3.10 The significance of tax-free sales for Åland

The exemption from the EU tax area is of overriding and fundamental importance for the economic welfare of the autonomous Åland Islands. A recent report from Statistics and Research Åland showed that the largest cluster of maritime activity in the Central/Northern Baltic is located in Åland.⁵ Economic growth, population growth, employment, household income, basic comparative advantages etc., all depend on the continuance of the opportunity to sell tax-free goods on board the routes between Åland, Sweden, Finland and Estonia.

Approximately 16 per cent of employment on Åland is in the shipping sector, and it contributes around 25 per cent of GDP. *Figure 16* shows private sector employment. However, employment generated indirectly by shipping companies on Åland is significantly higher.

⁵ ÅSUB (2010)

Figure 16. Private sector employment by industry on Åland 2008 (Per cent)



To summarize, the account above tells us that *the transport of goods on board tax-free ferries between Sweden, Åland and Finland constitutes a significant part of the Nordic transport infrastructure.*

4 Tax-free Supported Transport and Logistics in the Central BSR

4.1 An actor-based method of data collection

In the previous chapter, we used official statistics to present a base line representation of the main logistical structure and seaborne transportation flows in the Baltic Sea Region (BSR). In the following two chapters, we have gathered empirical information by interviewing top executives from the five companies/groups that dominate shipping operations on the tax-free routes in the central Baltic Sea Region (CBSR). Furthermore, we have also conducted interviews with executives from two of the main ports in the area, and from the only freight transporter on rail on the tax-free route between Sweden and Finland. The interviews were conducted from June to September 2011.

The interviews with the top executives (see Appendix, p.69) have made it possible for us to obtain a strategic and practical understanding of how the main operators in the region evaluate the importance to their operations of on-board tax-free sales, how they assess the potential effects of a scenario where the duty-free exemption would be abolished, and how that would change the traffic, routes and transportation flows in the region.

4.2 The tax-free based business model

Today, ferry shipping in the CBSR is formed around four main business areas:

- Passenger/car transportation
- Short cruises
- Freight
- Conference/business meetings

These four areas of business complement each other in a model that provides an efficient and economically effective transport system for people, cars and cargo. The different business areas are closely connected, and thus level out fluctuations in demand for the different services offered by the cruise ferry companies. During the summer, passengers and cars are the main segments, whereas during autumn and winter, transportation of cargo is more important. This flexibility provides the means to sustain year-around traffic on the main sea routes in the CBSR, according to one of our interviewees.

This provides for a frequency and a time table that makes it possible for large volumes

of people and cargo to be transported throughout the year, both during high and low season. Historically, cheap transport with a high frequency of departures have structured the logistical system of the motorway of the sea in the CBR.

According to the ferry business, the tax-free supported passenger traffic is of vital importance for the current system of seaborne transportation in the northern and central BSR. As one of our interviewees puts it:

“The tax-free exemption could be seen as a market-driven subvention that provides an economic possibility to promote a transport system through low-fare travel.”

Figure 17 below shows the main maritime routes in the central BSR; both the tax-free supported and the none-tax-free supported ones (see also Figure 14, 15).

Figure 17. Major passenger ferry routes in the Central Baltic Area



4.3 The shipping companies on the main tax-free supported routes

Historically, there have been only a few companies operating simultaneously on the tax-free routes in the central Baltic Sea area. In recent years, mergers and acquisitions have consolidated the business into three dominating shipping companies; *Tallink-Silja*, *Viking Line* and the *Eckerö Line Group*. The latter two of these “top three” are both based on the Åland Islands. These three companies currently dominate ferry shipping on the main duty-free routes in the BSR.

There are, however, some other actors of interest operating on the central Baltic Sea

shipping routes, among them the large Finnish Ro-Ro group *Finnlines/Finnlink* and the Russian *St Peter Line*, a newcomer on the CBSR's ferry cruising market.

Tallink-Silja

The origin of the shipping company Tallink can be traced back to 1965 when ESCO – Estonian Shipping Company launched passenger traffic between Estonia/Tallinn and Finland/Helsinki. The company and brand of Tallink was launched in 1989 as a Finnish-Soviet joint venture, primarily intended to transport tourists between the capital cities Helsinki and Tallinn. Since Estonia gained independency in 1991, the company has developed rapidly through mergers and buyouts. In 2006, Tallink purchased Silja Line from Sea Container Line and became the largest cruise ferry company operating in the central Baltic Sea area, with 19 ships serving cruise passengers, transport of people and cars, and the cargo segment.

Today, the Estonia based Tallink Group operates on six shipping routes under the name of Tallink and Silja Line. In addition to the shipping business, Tallink operates four hotels in Tallinn (Estonia) and Riga (Latvia). For the 2010/2011 financial year (01.09.2010-31.08.2011) the group's unaudited revenue reached EUR 897 Million. On average the Group employed 7 135 people.⁶ During the same period Tallink-Silja transported 9.1 million passengers on the main routes in the central Baltic Sea region.⁷

Viking Line

The shipping company Viking Line was established in 1959 by local businessmen in the Åland Islands. During the following years, the shipping companies *Vikinglinjen Ab*, *Ålandsfärjan Ab* (SF Line Ltd) and *Rederi Ab Slite* established a joint marketing company called Ab Viking Line Ltd. When two of the owners of the joint company Viking Line ceased with their operations, and the marketing company merged with the remaining company SF Line Ltd, which in 2005 was renamed and became the corporation Viking Line.

Today, the Åland Islands-based Viking Line operates seven cruise ferry ships on five routes. The Viking Line Group also operates a hotel in Mariehamn, Åland Islands, a travel agency and a bus company. During the 2009/2010 financial year turnover amounted to 569.9 Million EUR. On average 3 087 people were employed. The same period Viking Line transported 7.3 million passengers on the main routes in the central Baltic Sea region.⁸

⁶ Tallink Group Quarterly Report 2011-10-17

⁷ *Ibid.*

⁸ Viking Line (2011)

The Eckerö Group

Rederiaktiebolaget Eckerö was established in 1961 and has operated the route between Eckerö on the Åland Islands and Grisslehamn on the Swedish east coast since the start. Gradually, the shipping company has grown and consolidated into different areas of business. Today, the Åland Islands based Eckerö Group entails five different units:

- *Eckerö Line*, which operates one passenger ferry and one RO-PAX cargo ferry on scheduled journeys between Helsinki and Tallinn
- *Eckerö Linjen*, which operates on the route between Eckerö on the Åland Islands and Grisslehamn in Sweden
- *Birka Cruises*, which operates one cruise ship between the capital of Sweden Stockholm and Mariehamn, Åland Islands
- *Birka Cargo*, which operates seven Ro-Ro vessels in the short sea transport segment
- Furthermore, the Eckerö Group contains a *bus company*

In 2010 turnover of the Eckerö Group amounted to 228.9 Million EUR, and the number of passengers transported during the year was 2.6 million.⁹ The number of employees amounted to 1 161, of which 855 on board the ships and 306 people on shore.

St. Peter Line

St. Peter Line is a newcomer in the cruise ferry business in the central Baltic Sea region. Established in 2010, the Russian based St. Peter Line so far operates only two vessels on three routes.

Finnlines/Finnlink

The four shipping companies which we have mentioned above, have all built their transport capacity (including Ro-Ro freight trucks and trailers) and traffic system around the possibility of tax-free sales on board. However, there is a fifth important player engaged in shipping along the routes between Sweden-Finland-Estonia-Russia: the Helsinki-based international Ro-Ro shipping Group Finnlines/Finnlink. In this case, however, the business' primary focus is on cargo, not passengers.

⁹ Eckerö Line Annual Report 2010

Finnlines is one of the leading companies in the Ro-Ro sector in the Baltic Sea, the North Sea and the Bay of Biscay. Finnlines Ro-Ro operations run under the Finnlines brand in the Baltic Sea and North Sea, under the FinnLink brand in their operation between Naantali and Kapellskär, under the name NordöLink between Malmö and Travemünde and under the TransRussia-Express name between Lübeck, Sassnitz, Ventspils and St. Petersburg.¹⁰

Finnlines offers passenger services on Helsinki-Travemünde, Helsinki-Rostock, Malmö-Travemünde, Naantali-Kapellskär, Lübeck-Ventspils-St.Petersburg, Gdynia-Helsinki and Gdynia-Rostock routes. Finnlines/FinnLink offer Ro-Ro services on the Naantali – Kapellskär route without duty-free sales on board. Finnlines' revenue in 2010 was 561.1 million EUR and the company had on average 2 096 people employed.¹¹

Table 11 below summarises key information on the dominating shipping companies on the tax free supported routes in the BSR.

Table 11. Shipping companies, vessels and routes

<i>Shipping Company</i>	<i>Type of vessel</i>	<i>Routes</i>
<i>Tax-free supported</i>		
Tallink: (including Silja Line and Seawind)	19 vessels: Cruise ferries, Fast ferries and Cargo vessels	Turku – Åland* - Stockholm, Turku – Kapellskär, Helsinki – Åland – Stockholm, Tallinn – Helsinki, Riga – Stockholm, Kapellskär - Paldiski
Viking Line	7 vessels: Cruise ferries, Cruise ship	Turku – Åland – Stockholm, Stockholm – Mariehamn, Helsinki – Åland – Stockholm, Helsinki – Tallinn
Eckerö Group (incl. Eckerö Linjen, Eckerö Line and Birka Cruises)	11 vessels: Cruise ferry, cruise ship, cargo ferry and Ro-Ro vessels	Eckerö – Grisslehamn, Stockholm – Mariehamn, Helsinki – Tallinn
St. Peter Line	2 vessels: Cruise ferries	Helsinki - St Petersburg, Stockholm - St. Petersburg– Helsinki - Åland – Stockholm, Stockholm – Tallinn St. Petersburg – Tallinn - Stockholm
<i>Non-tax-free supported</i>		
Finnlines/Finnlink	Finnlines 9 vessels: Ro-Ro and Ro-Ro/Passengers Finnlink 3 vessels: Ro-Ro/Passengers	Helsinki – Travemünde, Helsinki – Rostock, Gdynia – Helsinki, Rostock – Gdynia, Travemünde - Malmö Kapellskär – Naantali, Lübeck - Ventspils - St.Petersburg

*) Mariehamn and Långnäs

¹⁰ Finn Lines is part of the Italian based Grimaldi group

¹¹ http://www.finnlines.com/company/financial_information (26.9.2011)

4.4 The significance of tax-free sales in the ferry and cruise segment

Today, the concept of on-board sales is formed around two tax-exemptions (i) the Åland tax-exemption and (ii) the non-taxed consumption on board (i.e. restaurant services) in the traffic between EU-member states. According to one of our interviewees these two tax-free connected factors combined provide almost 70 per cent of the cruise ferry companies' revenues, all based on sales from the duty-free shops and consumption on board.

On-top of the tax-free related consumption on board and duty-free sales, operations are divided between the transport of people and cars, complemented by cargo on trucks. Roughly 15-20 per cent of the passengers, depending on the route, travel for transport reasons. The rest travel for pleasure and work-related reasons (on-board conferences etc.). Approximately 90 per cent of the car deck is occupied by cars and the rest is occupied by trucks and trailers.

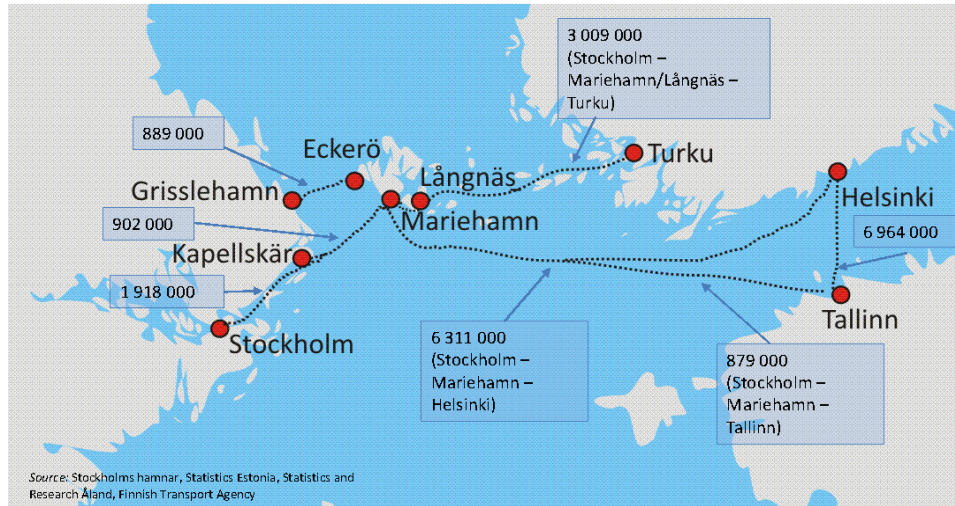
The cruise ferry concept provides a profitable mix of capacity for both passengers, cars and cargo, which complement each other and thus provide a lot of versatility. The cruise ferries provide a combination of Ro-Pax and cruise services that you don't find in many other places around the globe. This type of shipping supports the flow of goods between the countries, and is even more important for the transport of people and cars. It is also imperative for the external transport infrastructure and national economy of its driving logistical centre: the Åland Islands.

A tax-free supported logistical system provides high capacity, low fare traveling and frequent sailings. It constitutes a transport system that supplies cheap and flexible sea transports for people, cars and cargo between countries, regions and cities within the central Baltic Sea region. The total flow of passengers amounted to approximately 14 million on the tax-free supported routes in 2010.

Passenger transports *en route* between Helsinki and Tallinn amounted to almost seven million during the same year. This route between the two capitals provides no duty-free sales on board. However, the driving force behind this traffic is partly the same as for the tax-free routes, namely the significantly cheaper alcohol and tobacco in Estonia in comparison with neighbouring Finland. Furthermore, the Helsinki-Tallinn route is mainly operated by shipping companies which have been able to use their cruise capacity and knowhow that they have developed during previous years when sailing in the tax-free part of the sea borne transportation system within CBR.

Figure 18 illustrates the large volume of sea borne passenger travel in the CBSR:

Figure 18. Volume of passenger flows on the tax free routes in the CBSR 2010



The tax-free routes supply the major part of the capacity, operations and transport/cruise traffic between the countries in the central BSR. As already stated above, the tax-free supported ferries are also important carriers of trucks and trailers, thus playing an important role in the whole logistical system in the central Baltic Sea area.

Obviously the synergies of the combined handling of passengers, private cars and trucks are very important. According to unanimous voices in the shipping industry, traffic in the current form and volume could not be sustained without the possibility of duty-free sales on board. As stated by one interviewee:

“It is all connected. There is no business in keeping the traffic as it is today if the tax-free exemption would vanish, because duty-free sales, especially during the summer, provide the means to keep the traffic running throughout the year.”

The tax-free supported ferry traffic provides a unique market driven support system that enables ferry companies to offer services with high-frequency time tables and low fares. As much as 70 per cent of the earnings are yielded by duty free on-board sales, meaning that the price of the ticket is not as important a source of income as is the profits derived from getting people on board and buying duty-free products and services. Thus, tax-free sales could be perceived as a market driven mechanism that *de facto* renders traditional public financial support unnecessary. No doubt, one of our interviewees expressed, the

profitability of ferry shipping in the CBSR would vanish very quickly if the tax-free exemption would be abolished.

The importance of tax-free on board sales has not declined in recent years, rather the contrary. According to representatives of the Baltic cruise ferry business, a growing demand for better service and new products has increased the need for profitable on-board consumption in order to maintain the traffic. One of our interviewees explains the tight profit margins of the business:

“The request for better comfort, environmental friendliness, top class safety, higher wages and on top of this, higher price for the bunker oil, requires increasing income through duty-free sales and other consumption on board”

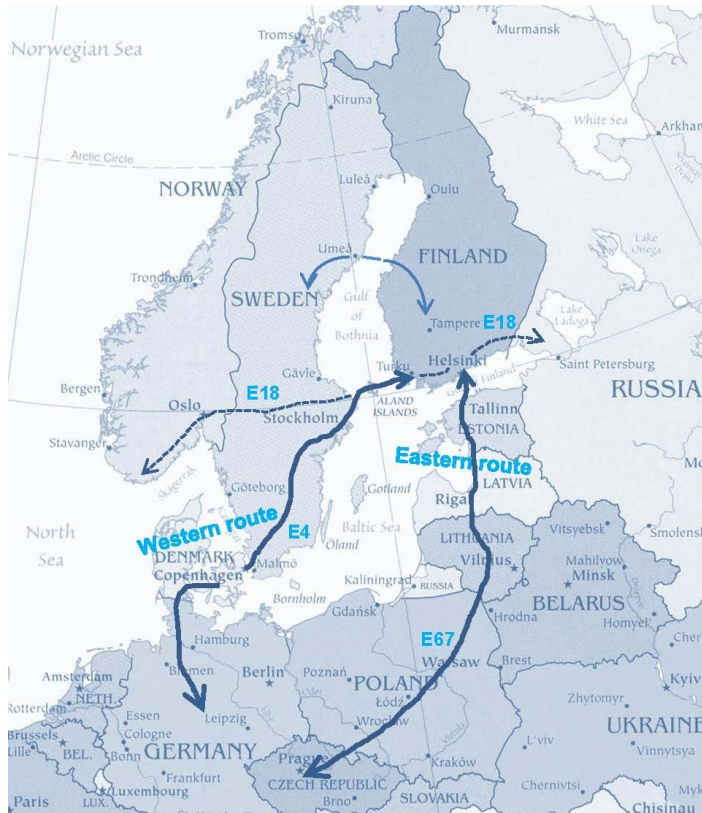
4.5 The significance of tax-free in the wider North European logistical system

The logistical system of the BSR is connected through roads, railway, sea- and airways. The seaways provide efficient infrastructure and logistics for the transport of people and goods within the BSR as well as between BSR and the rest of EU, and also to and from the western part of Russia.

According to the interviewed managers, there are two main routes for the flow of people and goods through roads, railways and seaways connecting continental Europe with BSR: The Western and Eastern route. These two transport corridors are strategically inter-connected through the tax-free sustained passenger and car ferry system in the north with its logistic and geographical centre in the Åland Islands. This inverted U-shaped multi-modal transport infrastructure also channels a multitude of secondary flows of people and goods from/to the rest of Scandinavia through road and rail, and also along the coasts and across the Gulf of Bothnia.

The geographical structure of the (non-airborne) Nordic-Baltic transportation system and its main connections with the European/international markets is shown in *Figure 19* below:

Figure 19. The main intermodal western and eastern transport routes to/from the BSR



The *Western route* runs through Germany, Denmark, Sweden and Finland with major terminal infrastructure in e.g. the Swedish cities of Helsingborg and Stockholm and Turku in Finland. Junctions provide major hubs and terminals for the multi-modal flow of cargo into and from the Nordic region along the Western route and the European highway E 4.

An influx of cargo is also provided through the “Nordic triangle” (see *Figure 20*) – connecting the capital cities of the Norway, Sweden and Finland. This part of the Scandinavian transportation system is prioritized in EU’s plans for infrastructural investments, i.e., the development of roads, bridges and rail systems of trans-European importance. The “Nordic triangle” is an important part of the European highway route E 18 running from Craigavon in the UK to St. Petersburg in Russia, passing through Norway, Sweden and Finland. The E 18 route also includes the tax-free supported ferry routes between Stockholm/Kapellskär in Sweden, Mariehamn in the Åland Islands and Turku/Naantali and Helsinki in Finland.

Currently, most of the Finnish cargo carried by trucks or trailers destined to/from the European or the international markets are shipped on tax-free supported ferries and non-

tax free Ro-Ro vessels via Sweden (Stockholm/Kapellskär) and the south west in Finland (Turku/Naantali). The geographical proximity between these two harbours and terminal areas provides an opportunity of maintaining high frequency time tables, currently about 60 departures per week.

According to one of our interviewees, close to 90 per cent of the cargo on trucks between Finland and Sweden is transported via this route. Accordingly, the sea route between Stockholm and Turku is of crucial importance for the flow of goods between the two countries, but also for the transit traffic within the central BSR and to and from Russia. The sea route between Umeå in Sweden and Vaasa in Finland was also part of the BSR tax-free transport system until 1999 when duty-free sales were abolished on the EU-internal routes. After that, the traffic has been cut and today there is just one Ro-Ro ship operating on this route.

The *eastern route*, also labelled *Via Baltica*, runs from the eastern part of the central BSR from Helsinki/Tallinn through the Baltic states to Warsaw and further via the European route 67 stretching all the way down to Prague (*Figure 19*). This route provides the main road infrastructure for the eastern logistical flows to and from the CBSR, including Russia/St Petersburg.

The sea route between Helsinki and Tallinn has become one of the main corridors for the flow of goods from the south and central EU to Finland and also between the Baltic States and Finland. Since the early 1990s, the traffic between the Estonia and Finland has been expanding continuously, and several shipping companies have established new operations in the area, providing the infrastructure and logistics services for the transport of goods and passengers between the countries. This busy sea lane has been in operation since the 1920s, with a stop during the first part of the Soviet era in the Baltic States. The service was back in operation in the 1960s. Ever since the Soviet era came to an end in 1991, both passenger and cargo traffic has continued to increase.

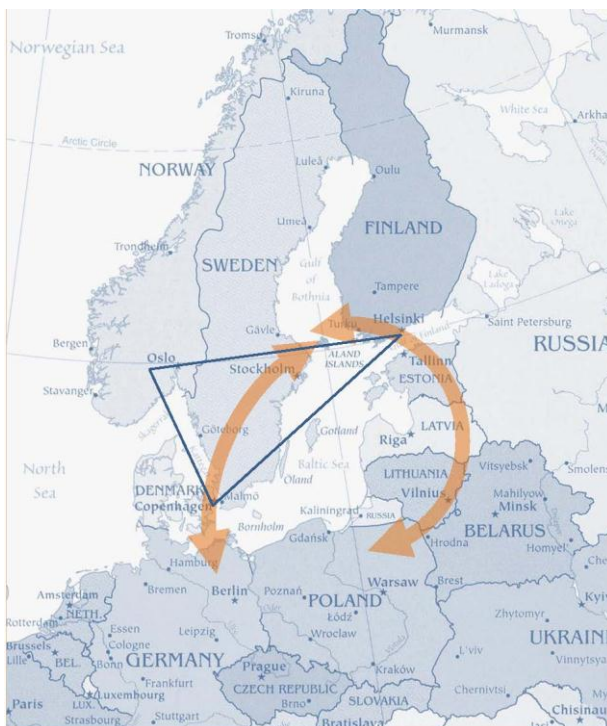
The Helsinki-Tallinn route enjoyed tax-free status until 2004, when Estonia joined the European Union. Today, the route is built around seaborne goods transportation and a passenger cruise concept adapted to differences in price levels in Finland and Estonia. Most of the ships on the route are engaged in a business formed around a combination of the two concepts. The difference in tax levels and thus the retail price on alcohol and tobacco between Finland (and the rest of the Scandinavian countries) and Estonia and the possibility to offer (un-taxed) consumption on board (i.e. restaurant services) has provided enough incitement for upholding the traffic.

According to one of our interviewees about 50 per cent of the passengers traveling

between the two capitals Helsinki and Tallinn are on a cruise. The main shipping companies operating on this route providing cruise ferry services are Tallink, Viking Line, and Eckerö Line. Other companies on the route are Linda Line and Nordic Jet Line providing fast transport with hydrofoils.

The overall transport structure of the BSR with its emphasis on the "Nordic Triangle" and the two main competing corridors to the European continent is graphically summarized in *Figure 20* below:

Figure 20. The Nordic Triangle and the Western and Eastern transport routes



The well-developed year-round traffic on the sea route between Sweden-Åland-Finland with vessels especially developed for integrated transport of passengers, private cars and trucks is *critically important as a connecting link between the flows in the Nordic Triangle and on the two main routes to the wider European and international markets.* This route also accounts for the bulk of seaborne trade between Sweden and Finland.

The capacity and flexibility in the traffic based on revenue from tax-free on-board sales are of central importance in maintaining the current broad range of transportation options on sea routes between the Northern Baltic region's western and eastern parts. *Thus, the tax-free supported links in the BSR form a vital part of the wider North European transportation and logistics structure.*

5 Effects of an abolishment of Åland's tax-free exemption

5.1 A non-tax free scenario for passenger and cruise shipping in the CBSR

In 1999, when duty-free sales between the EU-member states were abolished, an immediate threat to the tax-free subsidized ferry traffic system in the CBSR occurred. It had been the corner stone of the cruise ferry business in the area since the late 1950s providing enough surplus revenue to enable a development of, and further investments in the transport infrastructure in the central Baltic Sea for cargo, cars and passengers.

The insight of the potentially disastrous effects of an abolishment of the tax-free system on the economy of the Åland Islands engaged the government of Åland to seek an exemption from the new regulations prohibiting tax-free sales on all EU-internal routes.¹² As an effect, a special protocol on the Åland Islands (part of the treaty of Accession of Finland to the European Union) was negotiated, excluding the islands from the EU tax area, thus making it possible to continue selling tax-free on board passenger and car ferries to or from Åland.¹³

Currently (August/September 2011), none of the interviewed representatives of the maritime industry foresees a threat to this all-important Åland protocol, nor do they have any plans for establishing future traffic without the possibility of duty-free on-board sales. We cite one of our interviewees:

“As long as Åland is considered as a third country - the shipping companies will be able to practice tax-free sales on international and Åland water.”

On the other hand, one cannot completely rule out the possibility of a future EU-Treaty revision that abolishes Åland's status as a third country (in relation to the Union's tax territory). This chapter presents the assessments of top executives in the cruise ferry, Ro-Ro shipping and port authorities sector, on the probable long-term effects of a scenario without tax-free supported sea transports in the CBSR.

¹² Following the abolishment of tax-free sales on board ferries in EU in July 1999, the ferry market in the EU shrunk dramatically by 20 per cent in the second half of 1999. Ferry traffic across The Gulf of Bothnia was reduced by 84 per cent. See Andersson, L. (2005).

¹³ Protocol No 2 on the Åland Islands (articles 1-2), Treaty of Accession of Finland to the European Union 1994.

5.2 Effects on business models and logistical systems in the cruise ferry sector

All the interviewed top executives agree that today's passenger- and cruise ferry traffic would be seriously challenged by an abolishment of the possibility of tax-free sales on board vessels en route to and from Åland. The passenger market - boosted by the duty-free sales and on board services - has such a large share of the cruise ferry business revenue that such a drastic change in the operating environment would have a great impact on the organisation and functioning of the logistical system in the region. The running of current ferry/cruise operations demands a high service and competence level which will be impossible to sustain without the incomes from tax-free sales. Even though some ferries certainly would continue operations in the area, logistics would have to be adjusted in accordance to the new conditions.

The three most important outcomes of an abolishment of tax-free sales, stressed by all the interviewed shipping executives, were:

- Fewer departures
- Higher fares
- Introduction of public subsidies

They also pointed out earlier concrete examples of such developments in the Nordic and Baltic Sea area. One example is what happened to the traffic between Gothenburg and Rostock after Sweden joined the EU. Other examples include the non-tax-free - but heavily state subsidized - passenger shipping that serves the Swedish island of Gotland in the central Baltic and Danish island Bornholm in the southern Baltic. Other examples in the Nordic region are the "Hurtigrutten" in northern Norway which is subsidized by the Norwegian government, and also the ferry line between the Finnish city of Vaasa and Umeå in Sweden across the Gulf of Bothnia. In the rest of Europe, routes between Ireland and Wales, England and France, and Italy and Greece serve as examples of a possible development for the traffic in the central Baltic Sea region.

A scenario without tax-free on-board sales would therefore, according to the interviewed executives, provide very limited traffic during off season, and would also require higher ticket prices combined with various forms of public subsidies. A new competitive environment would emerge as a future non-tax-free shipping business would have to compete with air traffic and other business offering similar services on shore, i.e., spa and other hotel services.

The surviving shipping companies would have to change their operational model in such a way that they could compete with other types of products and services that would provide the new means for a profitable traffic. The most likely outcome is a change of

business strategy towards Ro-Ro/Pax traffic with focusing primarily on transport of cargo and cars. There would still be a market for car/passenger ferries, but they would offer less service and be more adapted to the demands of the cargo operators, according to our interviewees.

5.3 Effects on the cruise ferry routes in the CBSR

According to the interviewed executives the localisation of the scenario's future non-tax-free sea routes in the BSR would primarily depend on:

- The shortest journey between the destinations
- Differences in the level of excise tax on alcohol and tobacco in the CBSR
- Cities with large catchment areas
- Available harbours in third BSR-countries outside the EU tax/vat-area.

Without duty-free on board sales or a substantial difference in taxation levels between the departure and destination countries/regions, the future sea born leisure travel would be substantially down-sized. The number of ferry/cruise ships would be fewer, concentrating on transport of people and cars, and on a schedule that is more flexible and adjusted according to various demands.

However, the ferries left in operation would probably continue to sail along the existing sea routes and corridors in the CBSR. The most probable outcome is *a concentration of the remaining passenger and car ferry traffic to the two main routes between Sweden and Finland: Turku-Stockholm and Stockholm-Helsinki.*

Moreover, our interviewees expect that the current routing of most of the ferry traffic via Mariehamn and Långnäs in Åland would virtually cease. This also applies to direct sea links between Åland and Sweden, i.e., between Eckerö-Grisslehamn and Mariehamn-Kapellskär.

Other traffic options of interest for the traditional Swedish and Finnish cruise passenger market would be destinations where the excise tax is lower and therefore shopping would be cheaper than in their home countries (i.e., the Baltic states) and also where tax-free on board sales en route still are possible (i.e., Russia).

This implies an increase in ferry traffic to Tallinn, possibly also to Riga and other destinations where excise tax is considerably lower than in Sweden and Finland.

An interesting destination in this context is Russia. Since Russia is not a member of the EU, tax-free sales on all sea routes to and from this country are secured. *Russia, and*

especially St Petersburg, also represents a large potential market which offers the possibility of further exploitation by the cruise ferry companies. Today, passengers are shipped by bus and train to Turku and Helsinki to embark on their cruises. Incitements like on-board casinos could also provide opportunities and new concepts in the future. Casino and gambling is a globally growing market and could, therefore, further develop the services provided on the cruise ferries operating in the central BSR. As several of our interviewees express, in the future, the closeness to the Russian market will also create new possibilities for the operators and other service providers related to the cruise ferry segment.

The traffic area that would suffer the most is the autonomous Åland Islands and its capital city of Mariehamn. According to all of the interviewees the traffic to Åland would be reduced to a minimum. The remaining transports to and from Åland would be less focused on transportation of people and more on cargo – and with fewer departures, less capacity, and thus also better use of capacity. Accordingly, the Island would be placed outside the main logistical flows in the area. In the words of one of our interviewees:

“Without duty free sales on board to support it, most of the departures that we currently have during the summer would not be there anymore.”

5.4 Effects on cargo traffic in the CBSR

The transport of cargo has historically followed the same routes as today. Also, the main routes for the cruise and car ferry vessels in the area are along the traditional historical routes. The main positive impact on the cargo business of the tax-free ferry supported traffic is that it offers more options and a higher frequency of departures for the customers to choose from.

Furthermore, from an EU infrastructural policy point of view, combining transport of people and cargo is in line with the policy for development of a robust European transport system. If one part of this ‘two-legged’ traffic concept is abolished, the transport system would be more vulnerable. As a couple of our interviewees pointed out, the tax-free supported ferries on the routes in the CBSR are also important for the industry in the different countries in the region, but most of all, for the economy and for the transport of people and cars to the Åland Islands.

An abolishment of the on board duty-free sales would create *a need for new logistical solutions, which also would include some new routes.* Hence, one of the interviewees suggests that the port of the Finnish city of Hanko would be a possible alternative to

Helsinki on the route to the Swedish capital region ('*Mälardalen*') and its ports (including Nynäshamn, see also section 5.6, p. 59) due to a shorter journey. Hanko is already an important port of call in the traffic between i.e., Germany and Finland, primarily for transit cargo to Russia, but it could also be an option for traffic to Sweden according to one of our interviewees.

However, today's volume of cargo transported between Finland and Sweden by trucks, trailers and train wagons could probably be handled by as few as four modern Ro-Ro vessels on the Stockholm-Turku/Helsinki routes. As we learnt from our interviewees even in the case of tax-free supported passenger ferry dependent Åland, most of the cargo from Finland is currently carried on one single Ro-Ro ship, not included in the tax-free system.

Most of the freight shipping on the routes in the CBSR is controlled by providers of multi-modal logistic solutions for trucks, cargo wagons (train) and trailers in the central BSR, mainly through Ro-Ro ships without duty-free sales on board. In a future scenario without tax-free subsidized cruise ferry traffic, the vessels on the main routes in the CBSR would have to be much more adjusted to the demands for transport of cargo and offer less service for passengers. How and where the cargo would be transported would be a decision based on:

- The value of the cargo
- The time frame
- The most effective geographical routing available

Therefore, the logistical system would be built around the most cost effective way of transporting various types of goods. This would also be decisive for the type of ships operating in the Baltic Sea and the possibility for their commercial success.

Currently, most of the goods are transported either on a tax-free subsidized car ferry or a non-tax free Ro-Ro vessel. There is usually very little differentiation of the cargo according to the mode of transport. In a future without a tax-free subsidized transport system, *the logistic system would probably provide more differentiated services based on the type of goods, the time frame and the most efficient route for the cargo to reach its destination.*

5.5 Effects on cargo flows between BSR and the European markets

According to the interviews, the tax-free supported route system in the CBSR is an important link within the wider European Union's logistical transport network:

“Åland’s tax-free exemption is not just a question for the Baltic Sea region. It is much more important than that, since it concerns other regions and other infrastructural solutions in the EU as well.”

There have been shipping companies trying to open new cargo routes connecting to the CBSR corridor, but they have so far not been very successful. The main reason for this is that the routes have been located outside the core of the existing (tax-free supported) route system where the infrastructure of terminals, ports and other services are concentrated. And the favourable time table which well-developed and dense terminal infrastructure provides, will always be of critical importance for the cargo shipping business:

“People outside the business cannot understand the difficulties in selling for example a departure in the morning, since industries are, in most cases, not working through the night, which means that deliveries have not reached their destinations until late afternoon. Goods shipped the following morning will be too late for delivery the same day. This is why having the right time table is crucial /...../ It all comes down to lead time for the goods to be delivered.”

This implies that the flow of goods along the duty-free routes which are linked to the highly developed infrastructure in the Swedish part of the western transport corridor probably *will continue to run along this old and well established sea route between Finland and Sweden*, regardless of the future of tax-free on-board sales.

Furthermore, the completion of the new fixed *Fehmarnbelt* link between Denmark and Germany is likely to further strengthen the already well-developed and efficient infrastructure along the western main route of transport between the European markets and Scandinavia.

There are, however, some indications that parts of the Finnish goods flow and, above all, cargo bound for Russia, increasingly will use alternative routes. In addition to the reduced capacity on the west-bound route to Europe via South-West Finland and Sweden that a tax-free stop would imply, there are several other important factors that indicate *an increase in traffic along the main eastern route via the Baltic States, but also directly between the Russian ports and ports in Poland and Germany.*

The *Via Baltica*-corridor will probably attract increasing goods flows due to its low cost of operations. As long as the trucks and trailers used on the eastern route have the advantage of low-cost labour and cheap fuel, there are few incitements to re-route some of the Finnish/Russian goods flows via Sweden towards the main western corridor.

Moreover, the lack of terminal and harbour capacity along the Russian and Estonian coasts makes it difficult to open up alternative/competing sea routes along the eastern transport corridor with direct access to the European markets. This will, however, change as soon as the new Russian harbour and terminal infrastructure at Ust-Luga outside St Petersburg will be ready for large scale shipping operations. Thus, according to one of our informants:

“With the new harbour Ust-Luga, a possible scenario is that the Russian transit traffic will go directly there, and another incitement for that is that they can use whatever fuel they wish for their ships/...../ There is also a scenario where the transit traffic to Finland and Estonia goes to Russia and Ust-Luga and then on trucks to their destinations in Finland and Estonia.”

This option - a direct sea route between Russia and the European market (via ports in Poland and Germany) - will be further enhanced by the fact that Russia is not part of the EU environmental agreement that will set strict limits for the sulphate levels in the fuel of EU shipping.¹⁴ This new route will therefore gain a competitive advantage over other sea routes connecting the CBSR and the European markets since they are able to provide more cost effective transports due to cheaper fuel.

5.6 Effects on terminal areas and nodes in the logistical system

Through the years a transnational and interregional logistic system has been built around strategic points (harbours, terminals and concentrations of competitive logistics operators) on the main flow of goods and passengers; in this case the infrastructure of harbours, hubs and terminals in the CBSR:

“In Sweden, there is a system of hubs and terminals in strategic places like Helsingborg and Stockholm - feeding the logistics system in Sweden but also in extension, other countries along the route in the Central Baltic Sea Region.”

¹⁴ Ministry of Transport and Communication (2009)

As a result, close to 90 per cent of all seaborne goods on trucks using the Western route to/from the European market are shipped between Stockholm/Kapellskär and Turku/Naantali. The port in Nynäshamn south of Stockholm also holds the potential of becoming a more actively used part of the western corridor between CBSR and the European market. Its future position in the over-all logistics system will be further strengthened by current plans to invest in better connections to the E4 motor way, and thus also to the main western route leading down to the continent.

In the Stockholm region, traffic via the tax-free routes in the CBSR dominates the shipping that calls at its ports on regular basis. Other routes, for instance the one via the northern part of E 4 between Haparanda in Sweden and Torneå in Finland, account for but a fragment of the total volume transported. This is why the existing sea routes, ports and terminals are so important for the industries in the region, and this is also why it has become a prioritized route for the European Union.

The transport infrastructure running from South-western Finland and Åland via Stockholm down to southern Sweden and Denmark/Germany is so well developed that an abolishment of the tax-free on board sales on routes in the Northern Baltic Sea is *unlikely to lead to any dramatic change in the routing of the main cargo flows*. The resulting decline in the passenger-based ferry service would, however, be likely to reduce some of the congestion in the central ports of Stockholm, Turku and Helsinki. This would probably be offset by an increase of the traffic in the region's smaller but logistically better placed ports, such as Kapellskär and Nynäshamn in the Stockholm area and Hanko in South-west Finland. Once again, *the only really big loser would - not surprisingly – be the current centre of tax-free supported ferry and cruise traffic, that is, Mariehamn in Åland*.

An abolition of duty-free sales on the sea routes in the CBSR would probably not influence the use of the ports and terminal areas related to the eastern *Via Baltica* very much. Possibly, a decline in car ferry capacity on the route between Sweden and Finland would further *accelerate the already on-going expansion of the eastern route's terminals, ports and roads*.

6 Concluding analysis: winners and losers

6.1 The significance of tax-free supported sea transport in CBSR

The baseline study in the beginning of this report showed that, although sea transport in general in the European Union has lost ground during the last decade and a half, *maritime passenger transport continues to be a highly important part of the infrastructure in the Baltic Sea Area*. Specifically, passenger transport along tax-free routes remains highly important for Sweden and Finland. More than a third of Sweden's maritime passenger transport is along routes sustained by the profitability of tax-free sales and more than half of Finland's maritime passenger transports are duty-free supported.

Accordingly, an abolishment of the exemption from the VAT area of EU of the Åland Islands *would affect the larger part of the maritime passenger traffic in the central BSA, primarily the traffic between Sweden, Åland and Finland*. These routes are also used for shipping cargo on board the tax-free supported ferries. The share of tax-free supported transport of goods from Sweden to Finland is approximately one seventh, and the corresponding share of transport from Finland to Sweden is about one sixth. The tax-free supported routes and shipping thus play an important role in Finnish and Swedish – and especially Åland's – transport logistics.

The high frequency of departures of ferries along the tax free routes between Finland, Åland and Sweden function as a 'highway of the seas' connecting the eastern part of the BSR (Finland, Russia, and Estonia) with the central and western parts. *The 'Åland tax-free corridor' therefore functions as an integral link between today's two main transport routes connecting Scandinavia and the western part of Russia and the European continent* – i.e. the north/south bound corridors on the eastern and western side of the Baltic Sea.

A study carried out by Statistics and Research Åland a few years ago suggested that the exemption of the Åland Islands from the EU VAT area can be viewed as a provision of a semi-collective good, which is consistent with basic EU-principles of supporting regions, facilitating the flow of people and goods between member countries and providing an important link in over-all European transport logistics.¹⁵ Our conclusions in the present study seem to confirm this judgment.

¹⁵ ÅSUB (2004)

6.2 Tax-free abolished – the main losers

Inevitably, major changes not only create winners but unfortunately also some losers. This would most certainly apply to the effects of a possible future abolishment of the tax-free on board sales on the sea routes to and from Åland. *The obvious group of losers from such change is the firms and individuals that are currently the most closely connected to, and the ones benefitting the most from the specific economy and logistics that the tax-free supported shipping in the CBSR has created:*

- Companies that operate tax-free ferry business
- Suppliers and logistics firms specialized on CBSR tax-free shipping
- Cruise passengers and motorists using the tax-free ferries for transportation and leisure purposes
- Export and import firms using the tax-free supported ferries and their logistic infrastructure

The major losers are the shipping companies and employees with their core business in the tax-free segment. This also holds for the ports and terminal operators whose operations are dominated by these companies and their passengers. This group of companies, with related suppliers, currently represents the largest maritime cluster in the Northern and central Baltic Sea. The Åland-based shipping companies within the cluster alone, generate a demand in the regions along the tax-free routes of up to one billion euros and contribute - directly and indirectly - to over 10 000 jobs.¹⁶ These companies have very few alternatives to their current operations, and would therefore be very hard hit if the sale of duty-free products and services would be abolished.

The considerable number of individuals that have become accustomed to today's comprehensive range of cheap and convenient ferry connections between Sweden, Åland and Finland can also be considered to be among the main losers. Indisputably, an abolishment of the duty free on-board sales would lead to a sharp reduction in the number of departures, to higher fares and less and more expensive on-board service.

Another category that would suffer is the businesses which regularly use the ferries on the tax-free routes for their shipments. However, these would probably have the opportunity to use alternative modes of transport. In some cases, though, the high frequency of departures and the option of direct delivery to ports in the very centre of the region's metropolitan areas, is a competitive advantage that is difficult to achieve with the conventional freight shipping's less frequent schedules and with ports of calls located in the outskirts rather than in the central parts of the large consumer markets.

¹⁶ ÅSUB (2010)

Among the regions and cities located along the main tax-free sea corridor, Åland and Mariehamn would be the hardest hit. The Åland archipelago is the economic and logistical centre of today's tax-free supported sea transport in the Northern Baltic Sea. Two of the three shipping corporations that dominate the business have their head offices in Mariehamn. Approximately a quarter of Åland's GDP is generated in and by the tax-free based shipping segment, and a significant part of the shipping companies' employees live on the islands.

In addition, the Åland society as a whole is heavily dependent on the effective and inexpensive transportation capacity to and from the mainland of Sweden and Finland that the tax-free supported ferry shipping offers. Therefore it is beyond all doubt that the principal loser of a future 'tax-free stop' would be Åland and its economy and inhabitants. Nowhere else in or outside CBSR would you find such a geographic concentration of firms, households and people suffering the negative socioeconomic impact of such fundamental institutional change.

The negative effects of a withdrawal of Åland's tax-free exemption would not be limited to Åland alone. As stated above, there are companies and suppliers serving the firms within the 'tax-free cluster' located around the entire North and Central Baltic Sea region, and the overwhelming majority of individuals and businesses that use the duty-free subsidized transport are located outside Åland. Thus, the ports and terminal areas that would suffer are not only those located in Åland, but also the authorities, companies and terminal operators in the city centre ports throughout the CBSR traffic area; especially those in Stockholm, Helsinki and Turku.

6.3 Tax-free abolished – the main winners

The most obvious actors benefitting from a non-tax free CBSR-scenario are *companies specialized in Ro-Ro and Ro-Pax liner services and cruise ferry companies that can successfully compete on the remaining tax-free routes and the routes to destinations where on-shore prices are significantly lower than in Finland and Sweden.* Other winners are the logistics companies, port and terminal operators that would benefit from a transfer of transport capacity from the previous tax-free routes to new routes and ports.

The main groups of potential winners from an abolition of the Åland tax exemption are listed below:

- Cargo and Ro-Pax shipping companies and logistics operators in the CBSR
- Ports and terminal areas specialized in cargo shipping located close to the shortest sea routes between important hubs along the BSR's shores

- Cruise ferry companies that are able to expand their operations on the remaining tax-free routes
- Cruise ferry companies that can profit on differences in tax rates on alcoholic beverages and tobacco between the departing and arrival destinations

Unlike the concentration of potential ‘tax-free losers’ to Åland, and to some extent also to the centrally located metropolitan ports in Sweden and Finland, *the group of potential winners from an abolishment of tax-free sales would be much more geographically dispersed.* The sea routes that would benefit from an abolishment of tax-free on board sales are among others those with departures in Helsinki and the Baltic States; especially the two capitals of Tallinn (Estonia) and Riga (Latvia). Already today, these two destinations are among the main ports in the Baltic States for transport of cargo and people. Estonia and Latvia have lower tax levels on alcohol and tobacco than Sweden and Finland. Hence, they have become interesting destinations for cruise ferries, and also for other types of Ro-Ro and Ro-Pax ferries. Moreover, the two countries are an important part of the eastern *Via Baltica*-route.

An interesting shipping market in the outskirts of the main cruise ferry area is constituted by the routes between Helsinki, Tallinn, Riga and St. Petersburg. This easternmost part of the CBSR would provide an opportunity for the ferry operators to continue tax-free on-board sales after a future abolishment of Åland’s special tax status. Since Russia is not an EU-member it is considered a third country from an EU tax perspective. Another reason for the growing market potential in this part of the region is that Russia offers a large cruise passenger market which is still not fully exploited. Thus, the main ports in the Baltic States in general and Russian St Petersburg in particular, would probably all be winners in the context of this scenario.

Turning our attention to the western transport corridor, the main change in the traffic would be on the route between Turku and Stockholm, where traffic would be redirected to bypass Åland. The direct route between Naantali (Turku) and Kapellskär/Nynäshamn (Stockholm) is the fastest sea transport option between the two countries. These sea lanes also connect the western route to the eastern route and the Russian and Baltic markets. Hence, the winners would be those ports in South-western Finland and in the Stockholm region that are in the best position to handle the growing Ro-Ro and Ro-Pax traffic that would result from the abolition of the tax-free supported ferry traffic. And as stated above, we are here mainly referring to the ports and terminal areas in the vicinity of Turku and Stockholm: Naantali and Nynäshamn.

The port of Hanko, strategically located on the south-westernmost tip of mainland Finland, can probably also be included in this group of winners. Moreover, this port has

the potential to function as the northern hub of an expanding direct sea route leading down to Germany, which can be seen as an alternative to the land-based transports via the Eastern or Western route between the CBR and the continent.

6.4 Overall impact on regions and transport logistics in the Baltic Sea region

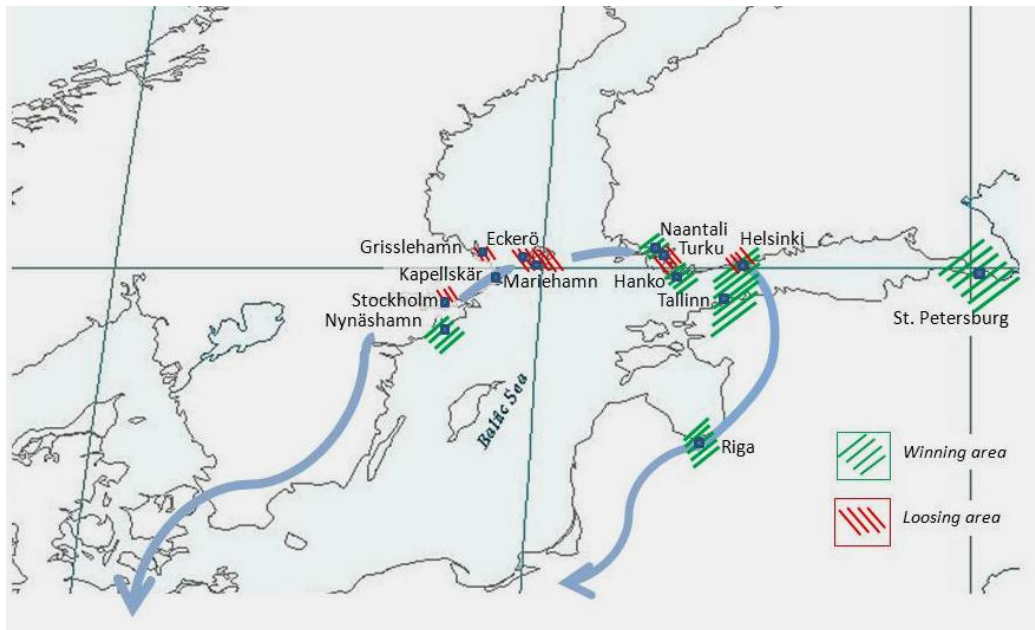
The strongest impact of the abolition of duty-free sales on the sea routes via the Åland Islands is thus located to the ferry traffic area along the Sweden-Åland-Finland route connecting the two main transnational transport corridors between Scandinavia, western Russia, the Baltics and the European continent. If tax-free sales were to terminate the ferry traffic volume would be significantly reduced and the remaining ferry transport would become more expensive for the users. The first and most obvious effect of this would be a substantial reduction in the volume of passenger transport between Sweden, Åland and Finland as well as a decline in the supply of seaborne transport capacity for certain types of freight.

These profound changes within the 'Åland tax-free corridor' would affect the flows of freight, goods and passengers to and from the ports and terminal areas along the two main corridors between CBR and the European continent, and thus the overall transport logistics in the entire Baltic Sea region. *The general picture is that we would see a strengthening of the regions and cities in the eastern part of the area, with a special focus on Helsinki, Tallinn and St. Petersburg, and the hubs, harbours and terminal areas along the Via Baltica-route further down to the European continent.*

The western corridor, with its highly developed infrastructure and large traffic volumes would probably retain most of its current traffic volume. The route might lose some of the shipments to/from the eastern parts of the CBR, which now use the tax-free subsidized ferry service on the sea lanes between Sweden and Finland.

Figure 21 summarizes graphically the overall picture of the traffic and terminal areas, ports and regions that would suffer most from a deterioration of their transport logistics due to abolition of Åland's tax exemption - and those that could gain from such a future development.

Figure 21. Winning and losing areas in the CBSA



As shown in the figure above, the losers are mainly located to the east/west bound link between the main western and eastern corridors to the European and international markets. The most obvious loser in this part of the BSR sea transport system, the Åland Islands, would completely lose its current role as the financial and logistic centre for ferry traffic between Sweden and Finland.

According to one of the interviewees, we have to go all the way back to the 1940s to realize what sort of down-sized transport logistics Åland would have to face in the event of an abolishment of tax-free sales on board the sea routes to and from the islands.

The principal winners are the major passenger- and cruise destinations in the northern parts of the Via Baltica corridor (i.e. St. Petersburg, Tallinn, Riga). Some of the specialized Ro-Ro ports and terminals outside the Finnish and Swedish capital region's central areas would probably also belong to those gaining some traffic and economic activities as a result of an abolishment of tax-free sales.

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Appendix

Interviewees

Christer Backman, MD/Senior Adviser Finnlink/FinnLines

Mikael Backman, MD Viking Line Abp

Björn Blomqvist, MD Eckerö Group

Igor Glukhow, President and CEO/St. Peter Line

Andres Hunt, Member of Management Board/Tallink Group

Christian Ramberg MD/Port of Turku Finland

Krister Sigfrids, MD SeaRail Ltd.

Henrik Wideståhl, Dep. MD/Ports of Stockholm

Swedish summary – Svensk sammanfattning

Bakgrund

Den skattefria ombordförsäljningen på de EU-interna sjö- och flygrutterna avskaffades 1999. Detta gällde dock inte trafiken via Åland i norra Östersjön eftersom den självstyrda ögruppen i samband med sitt EU-medlemskap 1995 erhöll ett särskilt skatteundantag som möjliggjorde fortsatt skattefri ombordförsäljning på fartyg som anlöper sina hamnar.

Åland var redan före EU-medlemskapet en central aktör inom rederinäringen i norra Östersjön, och har genom skatteundantaget ytterligare kunnat förstärka positionen som logistiskt och ekonomiskt centrum för färje- och kryssningstrafiken i de norra och centrala delarna av Östersjöregionen.

Det finns idag inget som tyder på att den åländska särställningen inom EU och de möjligheter till skattefri ombordförsäljning i trafiken via åländska hamnar som detta ger, skulle vara ifrågasatt eller hotad. Den väl utbyggda, turtäta och prismässigt förmånliga färjetrafiken på rutterna mellan Sverige, Åland och Finland kommer därför med största sannolikhet fortsättningsvis att vara ett viktigt inslag i Östersjöregionens sjöburna transportinfrastruktur.

Studiens syfte

Syftet med studien är att mer i detalj analysera betydelsen av den här trafiken, och vilka konsekvenser det skulle få om möjligheten till skattefri ombordförsäljning på rutterna via Åland försvann. Vad skulle bli kvar av dagens omfattande färje- och kryssningstrafik? Vilka nya transportsätt och rutter skulle tas i bruk? Hur skulle sjötrafiken till och från de idag använda hamnarna och terminalområdena påverkas? Vilka kan förväntas vinna och vilka blir de mest sannolika förlorarna? Hur skulle transporterna mellan Östersjöområdet och den europeiska kontinenten påverkas?

Den tax-free baserade transportmodellen

Den på skattefri ombordförsäljning baserade färjetrafiken är uppbyggd kring fyra olika affärsområden: (1) transport av passagerare och personbilar, (2) kortkryssningar, (3) lastbils- och trailerburna godstransporter samt (4) konferens- och affärsresor/möten. De fyra verksamhetsområdena har betydande ekonomiska och logistiska synergieffekter, något som kunnat utnyttjas för att bygga upp dagens väl fungerande system för kombinerad sjöfrakt av resenärer, privatfordon och frakt.

Den viktigaste transportlänken mellan Sverige och Finland

Färjetrafiken över Ålands hav, i norra Östersjön och i Finska viken är en viktig länk i det övergripande transportsystem som idag binder samman länder, regioner och städer inom Östersjöområdet – men också mellan Östersjöregionen och den europeiska kontinenten.

Detta gäller särskilt den sjöburna passagerartrafiken mellan Sverige och Finland. Mer än en tredjedel av Sveriges sjöburna passagerartransporter sker idag ombord på färjor som bygger sin ekonomi på skattefri ombordförsäljning, och drygt hälften av motsvarande finska persontransporter sker på samma färjor. Den med skattefri ombordförsäljning stödda färjetrafiken används också för kommersiella varutransporter. Cirka 14 procent av den totala sjöburna godsvolymen från Sverige till Finland transporteras på dessa färjor, och motsvarande andel av varuexporten från Finland till Sverige uppgår till dryga 16 procent.

Ålands livsnerv

Bland de aktörer och regioner som drar nytta av den sjötrafik som möjligheten till skattefri ombordförsäljning ger, står Åland och den åländska ekonomin i en klass för sig. Ålands läge i tax-free ruttens huvudled mellan Sverige och Finland ger det åländska samhället unikt välutbyggda, billiga och tur-täta året runt förbindelser med omvärlden (se Figurerna 12,14 och 15 i rapportens engelska huvudtext). Kravet på invikning till åländsk hamn för att kunna sälja skattefria produkter ombord har också medfört att huvuddelen av färjetrafiken mellan Sverige och Estland går via Åland.

Den åländska ekonomin är till stora delar uppbyggd kring den tax-free baserade rederinäring som i dag utgör kärnan i norra Östersjöområdets största maritima kluster. BNP per capita, den ekonomiska tillväxten, befolkningsutvecklingen, sysselsättningen och hushållen samlade inkomster är idag starkt beroende av den ekonomi och den sysselsättning som trafiken på de skattefria sjörutterna mellan Sverige, Åland, Finland och Estland genererar.

De ekonomiska fördelarna av trafiken begränsas dock på inte sätt enbart till Åland. Huvuddelen av rederiernas underleverantörer och ombordanställda finns utanför Åland, inte minst i Sydvästra Finland och Stockholmsregionen. Av de dryga 10 000 direkt och indirekt anställda som det åländska rederiklustret genererar bor sålunda omkring tre fjärdedelar utanför Åland, huvudsakligen i sydvästra Finland och Stockholmsregionen.

Viktig länk i Östersjöområdets övergripande transportsystem

Den tax-free baserade färjetrafiken via Åland spelar även en viktig roll som integrerande länk mellan de två huvudsakliga rutterna för transporterna mellan

Östersjöområdets norra delar (inkl. västra Ryssland) och den europeiska kontinenten. Den fram till idag mest trafikerade av dessa går från Stockholms- och Mälardalsområdet ner till kontinenten via Sydsverige, Danmark och norra Tyskland. Den konkurrerande, och idag av växande betydelse, andra huvudrouten går från Helsingfors-St. Petersburgsområdet via Tallinn, Baltikum och Polen ner till Centraleuropa ("Via Baltica"). Den tax-free baserade färjetrafiken mellan Sverige, Finland och Estland fungerar som en "sjöburen motortrafikled" som knyter samman dessa två för Östersjöregionen så kritiskt viktiga transnationella korridorer ner till de europeiska och internationella marknaderna (se Figurerna 19 och 20 i rapportens engelska huvudtext).

De viktigaste förlorarna vid ett tax-free stopp

Om möjligheten till skattefri ombordförsäljning på rutterna via Åland helt försvann skulle de företag, myndigheter och privatpersoner som drar ekonomisk och transportmässig nytta av nuvarande trafikkoncept självfallet också bli de största förlorarna. Till dessa hör framför allt:

- De rederier och deras anställda vars inkomster i huvudsak kommer från fartyg med skattefri ombordförsäljning på rutterna via Åland
- De underleverantörer och logistikföretag och deras anställda som är beroende av efterfrågan inom den tax-free baserade sjöfarten i norra Östersjön
- Den omfattande grupp av bilburna och övriga privatpersoner som utnyttjar tax-free trafikens billiga och bekväma trafikutbud för sina resor
- De export- och importfirmor som regelbundet använder färjornas bildäck för sina transporter
- De hamnmyndigheter och terminaloperatörer vars inkomster och sysselsättning i betydande utsträckning är beroende av den tax-free baserade färjetrafiken

Potentiella vinnare

De mest sannolika vinnarna i ett hypotetiskt framtidsscenario där Åland skattestatus inom EU ändrades så att möjligheten till tax-free ombordförsäljning försvinner, är de rederier och logistikföretag som är specialiserade på godstransporter mellan Sverige och Finland. Men även en del andra aktörer inom sjötransportsektorn hör till den potentiella vinnargrupp vars huvudsakliga innehåll sammanfattas nedan:

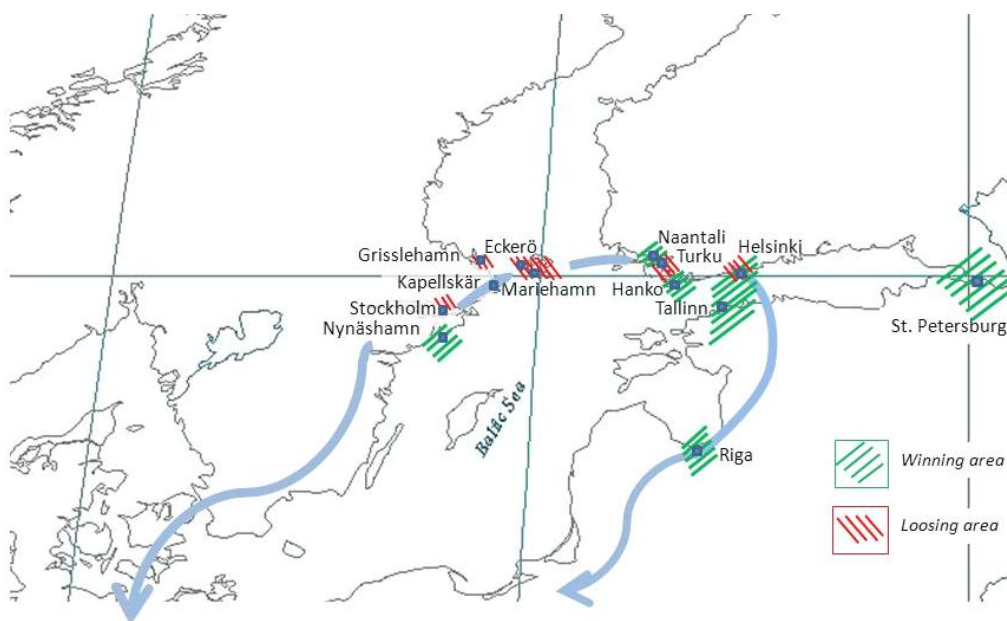
- Ro-Ro och Ro-Pax rederier och relaterade logistik företag i det berörda ruttområdet

- Hamnar och terminalområden med god lokalisering i förhållande till de snabbaste sjörutterna mellan länderna i de centrala och norra delarna av Östersjöregionen
- De kryssnings- och passagerarfärjerederier som kan expandera sin verksamhet på de rutter där tax-free ombordförsäljning kan fortsätta (St. Petersburg-trafiken)
- Passagerarfärjerederier som trafikerar rutter där skillnaderna i priserna på alkohol och tobaksprodukter i land är så stora att de lockar till "shoppingresor" (Sverige/Finland-Estland/Lettland)

Regionala effekter

En övergripande – indikativ – bild av lokaliseringen av de trafikområden, regioner och hamnar som sannolikt skulle ha mest att förlora respektive vinna på ett framtida stopp för den skattefria ombordförsäljningen på rutterna via Åland återges i kartan nedan:

Vinnande och förlorande områden vid ett "tax-free-stopp"



Eftersom den tax-free baserade sjötransportinfrastrukturen är avgränsad till rutterna mellan Sverige, Finland och Estland, så drabbar de negativa effekterna i första hand de regioner, hamnar och terminalområden som ligger längs dessa rutter. Den absolut största förloraren är Åland som helt skulle gå miste om sin nuvarande roll som trafikens ekonomiska och logistiska centrum.

Sett i ett bredare logistiskt perspektiv skulle detta innebära en betydande försvagning av den nordliga länken mellan de två huvudtransportkorridorerna mellan norra Östersjöområdet och den europeiska kontinenten. De viktigaste vinnarna finns i trafikområdets nordöstra delar, och då inte minst hos de kryssnings- och färjedestinationer i Finland, Baltikum och Ryssland som kan dra nytta av fortsatt tax-free trafik (St. Petersburg) och/eller den ”shoppingtrafik” som bygger på stora landprisprisdifferenser (Helsingfors, Tallinn, Riga). Till vinnarområdena hör sannolikt också vissa specialiserade frakthamnar (Ro-Ro) i utkanterna de svenska och finska huvudstadsregionerna (gäller främst Hangö och Nynäshamn).

ÅLANDS STATISTIK OCH UTREDNINGSGSBYRÅ

Ålands statistik- och utredningsbyrå, ÅSUB, är en fristående enhet vars huvuduppgift är att verka som Ålands officiella statistikmyndighet och bedriva kvalificerad utrednings- och forskningsverksamhet.

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Tfn +358 (0)18 25490
Fax +358 (0)18 19495
info@asub.ax
www.asub.ax

Ålandsvägen 26
PB 1187
AX-22 111 MARIEHAMN