Dear Sirs

Discussion paper on options for supporting English regional airports from the impact of Air Passenger Duty (APD) devolution

We comment on the discussion paper concerning options to support English airports from the perceived impact of the devolution of APD to Scotland and, possibly, Wales (we note that devolution - or part devolution - of APD to Northern Ireland should have little or no impact on English airports).

Our interest

As an organisation, we do not usually concern ourselves with tax rates so we make no comment on the impact of rates per se other than to recognise that reduced rates of APD should feed into the price of airline tickets; and that consumers, ie passengers, generally seek cheaper alternatives, provided the lower cost is not at the expense of other perceived needs, eg time and convenience.

In fact, in the context of APD devolution, we question whether the latter requirements of typical consumers/passengers, ie time and convenience, would be outweighed by the reductions in APD that might be practicable. We discuss this further below.

We also note that, contrary to many people’s view, APD was not conceived as an environmental tax; its purpose was and remains to raise revenue (as paragraph A3 of the APD background note acknowledges). We agree, therefore, that in principle those to whom APD is devolved will have to bear the cost by way of reduced support grants. This, however, is a very important point in terms of the fiscal impact on devolvees, which we also discuss further below.
Relevant tax principles

We expect stakeholders such as airlines, airports, travel agents, tour operators and public authorities can provide evidence of practical issues. It is likely that environmental groups will also argue that APD has a role as an environmental tax. Given Government policy that APD is a revenue raising measure, we make no comment on its appropriateness as a fiscal instrument driving environmental change.

This paper looks primarily at fundamental tax principles and in particular –

- Certainty
- Ease of administration

We also discuss the issue of tax transparency and the economic impact on consumers, ie airline passengers.

The principle of certainty

It is generally accepted that legal certainty is a fundamental requirement of a good tax system. The impact of lack of certainty has been well-illustrated by the problems posed by the exemption from Aggregates Levy in Northern Ireland, which took 13 years of litigation and legislation to resolve¹.

The discussion paper recognises the problems that face the devolution of a tax such as APD; it must be EU and international law compliant. If it is not compliant then financial consequences follow, eg if the reduction of APD were seen as an illegal subsidy under the state aid rules, then it would have to be repaid by those benefiting, presumably the airlines, which is unlikely to be popular.

Ensuring compliance may be easier said than done; in the case of Aggregates Levy, the UK Government sought approval from the European Commission before the tax was introduced but there were issues with the approval process. One of the consequences of the protracted litigation in regard to Aggregates Levy was to delay its devolution to Scotland.

Accordingly, it is important that there should be a comprehensive programme of consultation on the detail of any APD devolution to ensure that all legislation is fully compliant; this should involve all stakeholders including airlines, local authorities and the devolved governments. Given that international travel may be involved, it may be that there will be overseas stakeholders as well.

Ease of administration

APD is not without its complexity but is arguably a fairly simple tax by comparison with other taxes. However, it must be obvious that devolving APD to different authorities will lead to several consequential compliance issues including the following.

- **Number of different APD administrations** - Within England, there could be in excess of 20 additional tax authorities² to whom airlines would have to declare and


² Based on the number of airports in different counties reported in Wikipedia (which may not be wholly accurate) that have scheduled air travel. Of the current main ‘budget airlines’ serving English airports, RFlyBE operate out of 18 different English airports, EasyJet 12 and Ryanair 11; even a very small niche airline, Skybus with just three routes serving the Isles of Scilly,
pay APD – thus some airlines that currently have a single APD regime to deal with, making a single Return to HMRC to declare their full APD liability on all tickets sold regardless of the departure airports, could, under devolution, have to deal with up to 20 different APD-levying local authorities.

- **Increased compliance costs** - While it would be potentially possible to create a system similar to the Mini-One-Stop-Shop to facilitate the submission of Returns and make payments to each responsible local authority, this would only work with substantial agreement of all affected local authorities and there may be IT costs and challenges to overcome. Alternatively, it would be possible to use HMRC or an independent cost sharing body to administer the taxes. With multiple jurisdictions though, costs will almost inevitably rise because there would be less economy of scale. And different tax rates of course complicate the financial accounting.

- **Dispute resolution** - While APD has not been the subject of substantial litigation, it would inevitably be necessary to make provision for a dispute resolution process, including possibly a local tribunal if the UK tribunals were not used, e.g. because they were too expensive.

- **Whose APD is it?** - If the devolved authorities, including those to whom APD is devolved in England, have full control over the tax, issues may arise as to how to deal with connecting flights. For example, under current rules, a flight from Edinburgh to London and then on to South Africa is treated as a long haul flight subject to UK APD on the initial departure from Edinburgh only. When Scotland has devolved power over APD, will it set the rate for the whole flight on its initial departure from Edinburgh as now? Is it fair that Scotland retains the full APD when the international leg leaves from say Heathrow (and will the Heathrow APD regional administration agree?). What if the Scottish international APD rate is different from the Heathrow APD regional administration such that the same flight from Heathrow to South Africa requires different APD rates to different APD administrations? This seems hugely complex and difficult and costly for airlines and their IT systems providers to code and administer.

**Economic impact**

Recognising that APD is a revenue-raising measure not an environmental tax, devolution to local authorities in England will have to be revenue neutral, meaning some hypothetical quantum for APD will have to be assumed and that sum somehow ‘clawed back’ from affected local authorities’ Government funding. Thus, any discounting (or abolition) of APD locally will have to be met fully from the local authority’s own resources. Realistically, in the present fiscal climate, it is difficult to see how any local authority could justify this. There also seems scope for potential conflict over the actual reduction in APD and the precise value of any UK government clawback.

**Tax Transparency**

All in all, before legislation is drafted, it would seem sensible to set out the precise basis upon which APD would be devolved both to Scotland and Wales and within
England. Otherwise English regional airports will not have the power to counter perceived competition from airports in Scotland and, if it accepts devolution, Wales.

The proposals also raise an important issue over identifying the appropriate local authority to which APD should be devolved. Simplicity suggests devolution should be to the local authority within whose geographic area an airport is situated. But it is rare for English regional airports to serve just one local authority’s area, their economic impact generally being on a significantly broader ‘hinterland’.

For example, East Midlands Airport is situated with Leicestershire County Council’s geographic area (actually within the area of North-West Leicestershire District Council at ‘second tier level’). But the Airport is at the extreme north-west edge of Leicestershire (and is nearer to Derby and Nottingham than Leicester) serving - as the name suggests - not just Leicestershire but much of Derbyshire and Nottinghamshire, ie the East Midlands.

By way of another example, Bristol Airport is not even in Bristol but is located within the area of North Somerset Council, though clearly serving not only Bristol (and North Somerset) but also the rest of the former Avon County plus Gloucestershire and Wiltshire.

Furthermore, to which authority would responsibility for APD be devolved for London’s airports? Indeed, might Heathrow, Gatwick and London City be regarded as ‘special cases’ subject to ‘nationally imposed’ APD rather than it being devolved? Or might APD be devolved to Transport for London in these cases (even though Gatwick is outside Greater London)? And who would be granted APD devolution in respect of Stansted, Luton and Southend, each of which are designated as ‘London Airports’?

**Non-tax issues**

In addition to tax issues, there are of course other considerations, eg as a matter of policy do the UK and devolved governments wish to see changes in behaviour driven by APD, such as people getting in cars to drive to airports miles away to save APD? We recommend these other impacts should be evaluated and costed.

However, on this we do note that the proposals cite the background of devolution of APD to Scotland and possibly Wales, the implication being that if Scotland and/or Wales reduce APD rates, that could have a competitive distorting impact on certain English regional airports; that being so, allowing those affected English regional airports to respond with commensurately reduced APD rates must inevitably have an equivalent impact on other English regional airports, so what must be considered is not simply the consequence on English airports of APD being devolved to Scotland and/or Wales but also the impact of further devolution of APD in England between ‘competing’ English airports.

For example, if Bristol is allowed to reduce APD to ‘compete’ with Cardiff, it seems logical that, say, Bournemouth and Exeter should equally be allowed to reduce APD to ‘compete’ with Bristol. It is not clear to us, in the absence of any economic study, how elastic supply and demand is between different airports and how much competition might exist. We think that such a study should be undertaken given the potential adverse impact on regional airports should such elasticity exist. We would note that the potential price differential for long haul and especially for premium seats will be significantly higher and thus the risk of airport APD price wars may be more likely to arise.
In terms of ‘competition’, we also make a further observation that, rather than a ‘need’ arising to discount APD rates to ‘compete’ with other airports, airlines - especially ‘budget airlines’ - may perceive this as a means of driving down ticket prices from English regional airports (or indeed retaining more income themselves by having to declare less APD) and so might put pressure on the airport and thus the responsible local authority, with the threat of moving their flights to other ‘more co-operative’ airports. Where impacted local authorities are unwilling or unable to reduce APD rates in response to such demands, the consequence for consumers, ie airline passengers, may well be the loss of convenience of locally departing flights, which is clearly counter-productive.

If you want us to elaborate or explain any matter considered herein, please contact our technical team at indirecttax@ciot.org.uk.

Yours sincerely

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