

# HM Treasury discussion paper on options for supporting English regional airports from the impacts of Air Passenger Duty devolution

September 2015

## Introduction

The British Air Transport Association (BATA) welcomes the opportunity to submit our views and evidence to HM Treasury's discussion paper on options for supporting English regional airports from the impacts of Air Passenger Duty (APD) devolution.

BATA is the trade body for UK-registered airlines. Our members – British Airways, DHL, easyJet, Flybe, Jet2.com, Monarch, RVL Group, Thomas Cook, Thomson Airways, Titan Airways and Virgin Atlantic – employ over 74,000 people and served 138 million passengers and carried one million tonnes of cargo in 2014.

It is airlines, not airports, that serve passengers and destinations, and understand how passenger demand, affected by high taxation, will impact on existing routes, and route development.

## Summary of our position

- UK APD is the highest tax of its type in Europe and one of the highest taxes on flying in the world. Most countries do not tax air travel, and countries such as Ireland, the Netherlands and Belgium have abolished their equivalent tax.
- Following the decisions in the last Parliament to simplify the banding system and to abolish APD for children, the Government should now finish the job and abolish APD for all other passengers during this Parliament to transform the UK's international competitiveness, boost trade, increase productivity, encourage inbound tourism and support the travelling public.
- In line with this objective, the Government should abandon its policy of inflation linked annual increases to APD rates. The few other equivalent taxes in Europe do not tend to be increased annually, so each year the UK becomes gradually but steadily less competitive.
- The devolution of APD to Scotland and Wales raises significant concerns about market distortions and unfairness to passengers living in different parts of the UK. The Scottish Government are committed to reducing Scottish APD by 50% from 2018, and abolishing it entirely when public finances allow.<sup>1</sup> The UK Government should take a lead and eliminate these concerns by abolishing APD during this Parliament.
- None of the three options presented in the discussion paper should or can realistically be taken forward as they do not meet commonly accepted principles of good taxation.
- The discussion paper should have considered the widest possible range of policy options, including abolition and significant reductions of UK APD.

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<sup>1</sup> The Scottish Government's Programme for Scotland, 2015-16, <http://www.gov.scot/Resource/0048/00484439.pdf>

## Context

The Conservative general election manifesto identified a number of challenges that a Conservative Government would tackle:

- how to increase trade with emerging economies because the UK remains too reliant on slow-growing EU markets;
- how to increase business investment because it remains lower than other countries;
- how to increase productivity; and
- how to support tourism further – an industry that already supports three million jobs and is one of the nation’s leading export earners.

By increasing the cost of an air ticket from between £13-£142 per journey (depending on class of travel and destination), APD currently acts as a barrier to making progress on these issues. It is a significant tax on inbound tourism and business travel alike that has increased significantly since its introduction in the mid-1990s.

The last majority Conservative Government raised £356m per year from APD in 1996/97. Ten years later the tax rates had been increased such that the total revenue raised was £971m (2006/07).<sup>2</sup> Another ten years later and the revenue for APD is forecast to be £3.2bn in 2016/17.<sup>3</sup>

Passenger numbers have grown, but tax receipt growth has outstripped passenger growth because the tax rates have been increased significantly.

	<b>APD chargeable passengers (m)</b>	<b>APD receipts (£m)</b>
1996/97	53.8	356
2006/07	106.1	971
2013/14	101.8	3,013

Source: HMRC/ONS APD Bulletin, June 2015, Table 5  
<https://www.uktradeinfo.com/Statistics/Pages/TaxAndDutybulletins.aspx>

Despite the recent positive reforms to exempt children and abolish the two furthest long-haul bands, APD remains the highest tax on flying in Europe, and one of the highest in the world.

In May, the World Economic Forum published its latest biennial Travel and Tourism Competitiveness Report. The UK is ranked 137<sup>th</sup> out of 138 countries in their global Travel & Tourism Competitiveness Index for air ticket taxes and airport charges.<sup>4</sup>

The UK is one of just a handful of European countries to levy an air passenger duty, and in recent years many countries have abolished their equivalent taxes in order to become more competitive.

- Ireland abolished their air travel tax in 2014 to stimulate their economy;
- the Netherlands abolished their air passenger ticket tax in July 2009 in response to a significant drain of passengers to airports in Germany and Belgium<sup>5</sup>;

<sup>2</sup> HMRC/ONS APD Bulletin, June 2015, Table 5 <https://www.uktradeinfo.com/Statistics/Pages/TaxAndDutybulletins.aspx>

<sup>3</sup> [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/443232/50325\\_Summer\\_Budget\\_15\\_Web\\_Accessible.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/443232/50325_Summer_Budget_15_Web_Accessible.pdf) p.108

<sup>4</sup> [http://www3.weforum.org/docs/TT15/WEF\\_Global\\_Travel&Tourism\\_Report\\_2015.pdf](http://www3.weforum.org/docs/TT15/WEF_Global_Travel&Tourism_Report_2015.pdf), p.434

- Belgium abolished its air travel tax in 2008; and
- Denmark phased out its air passenger tax in 2006-07.

The limited number of EU countries that do levy an equivalent tax (such as Germany, France, Austria and Italy) have much lower rates and raise significantly less revenue than APD. For example, Germany has the second highest air passenger tax in Europe, but it raises £2.4 billion less than APD.

Tax revenue raised in 2014	£ bn	€ bn
UK – Air Passenger Duty <sup>6</sup>	3.14	4.20
Germany – Aviation Tax <sup>7</sup>	0.75	0.99

	UK rates (£)	German rates (in £)
Within EU	13	5.70
Medium-haul	71	17.70
Long-haul	71	32.10

Furthermore, the gap between UK APD and the German tax is forecast to increase over the next five years, partly because UK rates continue to increase by inflation each year, whereas German rates are not updated each year (they were, in contrast, reduced in 2012).

Tax revenue forecasts	£ bn	€ bn
UK – Air Passenger Duty – for 2019/2020 <sup>8</sup>	3.80	5.09
Germany – Aviation Tax – for 2019 <sup>9</sup>	0.77	1.03

## Abolition of APD

There is a strong economic and political case for abolishing APD. Independent evidence suggests it would stimulate additional business travel that would lead to higher productivity, increased trade and greater investment. The UK would become a more attractive and internationally competitive tourist destination. Britain's families would find it cheaper to go on holiday and visit friends and relatives across the country and overseas.

PWC published a report on the impact on the economy and Government tax revenues if APD were abolished in 2013.<sup>10</sup> PwC's robust and detailed economic assessment was underpinned by a Computable General Equilibrium model; similar to the ones used by HM Treasury. The report found

<sup>5</sup> A report by the KiM Netherlands Institute for Transport Policy Analysis found that: "A conservative estimate of the air passenger tax's effects during that period is that the tax accounted for nearly two million fewer passengers from Amsterdam Airport Schiphol." It estimates that of these potential air passengers: 50% did not fly (either did not travel or used an alternative mode) and 50% used foreign airports – mostly Dusseldorf, Germany; Brussels, Belgium and Weeze, Germany (Source: KiM Netherlands Institute for Transport Policy Analysis report, p9)

<sup>6</sup> <https://www.uktradeinfo.com/statistics/pages/taxanddutybulletins.aspx>

<sup>7</sup>

[http://www.bundesfinanzministerium.de/Content/EN/Standardartikel/Press\\_Room/Publications/Monthly\\_Report/Abstract/2015-01-english-version.html](http://www.bundesfinanzministerium.de/Content/EN/Standardartikel/Press_Room/Publications/Monthly_Report/Abstract/2015-01-english-version.html).

<sup>8</sup> [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/382327/44695\\_Accessible.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/382327/44695_Accessible.pdf), p.100

<sup>9</sup>

[http://www.bundesfinanzministerium.de/Content/DE/Standardartikel/Themen/Steuern/Steuerschaetzungen\\_und\\_Steuer\\_einnahmen/Steuerschaetzung/2014-11-11-ergebnisse-145-sitzung-steuerschaetzung-dl.pdf?\\_\\_blob=publicationFile&v=2](http://www.bundesfinanzministerium.de/Content/DE/Standardartikel/Themen/Steuern/Steuerschaetzungen_und_Steuer_einnahmen/Steuerschaetzung/2014-11-11-ergebnisse-145-sitzung-steuerschaetzung-dl.pdf?__blob=publicationFile&v=2),

Table 5

<sup>10</sup> <http://www.bata.uk.com/wp-content/uploads/2013/09/APD-study-Abridged.pdf>

that abolition would boost GDP, leading to thousands of new jobs and higher tax receipts such that abolition would be self-funding.

In May 2015 BATA published a further study by PwC that updated their 2013 report, with new analysis taking into account APD policy changes since 2013 and recent economic studies by government and PwC's own work for the Airports Commission.<sup>11</sup> Their study for the Airports Commission looked at the relationship between the aviation sector and GDP and found a stronger link than the evidence used in the 2013 APD study. This suggested that the benefits of abolition had been underestimated and are even greater than previously thought. Their economic model has been updated to reflect this new evidence and has produced a revised set of results suggesting that:

- APD abolition could boost UK GDP by 0.46% in the first year, with continuing positive benefits up to 2020;
- the economy could be 1.7% bigger by 2020 than would be the case if APD were to remain unchanged;
- the increased economic output associated with abolition could lead to the creation of 61,000 jobs by 2020 – 1,000 more than the 2013 report found despite recent policy changes; and
- more tax revenue would be raised from other taxes than is lost from abolition, with a net 570m in extra tax receipts in the first fiscal year, and positive benefits in total compared with status quo.

In short, the evidence suggests that abolition would boost growth, help to create jobs, and would more than pay for itself through increased revenue from other taxes. The modelling suggests that the boost to GDP from abolition would come from three main sources:

- airline investment to offer new routes and maximise existing capacity to meet an estimated 10% increase in the demand for flights;
- higher productivity, international trade and investment from increased business and leisure travel; and
- a 7% net increase in foreign inbound tourism passengers by 2020 – equating to approximately 200,000 extra inbound tourist arrivals in the UK.

## Overall response to the discussion paper

The Government is right to recognise that APD devolution will have impacts in England, but wrong to see this as an issue affecting just a handful of regional airports closest to Scotland or Wales. We agree with the Prime Minister who said during the recent election campaign that implications would be felt across the whole country:<sup>12</sup>

*“The SNP government in Scotland is committed to using its new powers to cut and eventually abolish air passenger duty for flights from Scottish airports. That could distort competition and see business drawn north of the border with a huge impact on airports in the rest of our country so we’re reviewing the way air passenger duty works to make sure other cities don’t lose out”.*

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<sup>11</sup> <http://www.bata.uk.com/wp-content/uploads/2015/06/The-economic-impact-of-APD-analytical-update-PwC-May-2015.pdf>

<sup>12</sup> <http://www.itv.com/news/update/2015-04-20/cameron-snp-plan-to-abolish-passenger-duty-could-harm-uk-airports/>

We are very concerned that the scope of the discussion paper is too narrowly focused. The three options included in the paper have significant flaws and are not supported by UK airlines.

Other policy responses, including the abolition of APD and significant reductions to match changes in Scotland and/or Wales and make the UK more competitive in Europe should be considered. These options deserve serious analysis, including detailed dynamic modelling of their likely economic impact.

Rather than conducting a rather insular debate looking at different nations and regions within the UK and seeking to somehow mitigate the impact of devolution, the Government should take a broader, international perspective, and consider the more fundamental problems with Air Passenger Duty. It should ask why the Scottish Government wants to halve and abolish APD, and consider whether the UK as a whole would benefit from a similar approach. A review of APD should not just focus upon questions and impacts arising from the North East competing with Scotland or even London and the South East, or the South West competing with Wales or the West Midlands. A review of APD should instead consider whether the tax allows the UK to be internationally competitive.

Devolution presents a perfect opportunity to set out a new course on APD. Abolishing APD during this Parliament would make concerns about market distortions and unfairness for passengers caused by devolution redundant, and, even more importantly, would deliver significant economic benefits to the country.

### **Responses to the 3 options contained within the discussion paper**

**We have assessed the three options in the discussion paper on how they each meet commonly accepted principles of good taxation** (such as those identified by the Treasury Select Committee<sup>13</sup>), **including stability, certainty, practicality and coherence**. We have also taken into account a requirement for basic fairness and the stated aims of the Government's productivity plan, as published by Treasury and BIS in July 2015<sup>14</sup>, which states:

*"The tax system can support productivity by providing incentives, stability and certainty for long-term investment and innovation, avoiding distorting economic choices, and minimising the administrative burden of paying taxes."*

*"The government will continue making tax easier and simpler"* and also that the *"government believes in lower taxes"*.

**Option 1: Devolving APD within England** (either fully or partially) to local authorities or Combined Authorities (including mayoral city-regions) within England.

*Full devolution* would entail UK APD being "switched off" in an area, and local authorities given power to raise their own APD on passengers departing from airports within their geographic boundaries. *Partial devolution* would entail UK APD continuing to apply with a local authority's boundaries, but with the authority being given the power over one or more rates of APD. One option for the partial devolution of APD would be to devolve power over long haul rates only, as is the case in Northern Ireland.

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<sup>13</sup> <http://www.publications.parliament.uk/pa/cm201011/cmselect/cmtreasy/753/753.pdf>

<sup>14</sup> [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/443898/Productivity\\_Plan\\_web.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/443898/Productivity_Plan_web.pdf)  
pp. 17-18

We do not believe this option meets the commonly accepted principles of good taxation as set out above and therefore we do not support it.

This option would allow the creation of a patchwork of different rates (and even potentially different systems) which would simply add **confusion, complexity and cost** for government, passengers and airlines.

Furthermore, it may be worth considering whether there would be a **conflict of interest** where the rate setting authority could comprise those with an ownership stake in an airport. Of the current Combined Authorities<sup>15</sup>, two have ownership interests in airports<sup>16</sup>:

Greater Manchester Combined Authority	Manchester Airport (also other MAG airports – Stansted, Bournemouth and East Midlands)
North East Combined Authority	Newcastle Airport and Durham Tees Valley
Sheffield City Regional Combined Authority	
West Yorkshire Combined Authority	
Liverpool City Region Combined Authority	

In addition, work is well underway on forming another Combined Authority, members of which would also be involved in ownership of an airport:

West Midlands Combined Authority	Birmingham Airport
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The airports in the other existing Combined Authorities (Robin Hood Doncaster Sheffield, Leeds Bradford and Liverpool John Lennon) are privately owned with no public sector stake.

We understand that there are also currently proposals for Combined Authorities in Nottinghamshire, Derbyshire and Leicestershire (which would include East Midlands Airport) and Tees Valley (which could cover Durham Tees Valley Airport).

Newquay, Humberside and Norwich airports also have varying degrees of public sector ownership, in the form of stakes by local authorities.

We question whether there would be any significant improvement to **domestic connectivity** from adoption of this proposal – for example, if the North East reduces the Band A rate (including UK domestic services) but London retains the UK rate, then a return flight from Newcastle to London would still incur the UK rate on the return leg.

There is also the obvious prospect of a **‘domino effect’** up, down and across English regions, as they are each in turn affected by neighbouring areas which reduce the APD charged on flights from their airports. As the discussion paper acknowledges, a land border does have an effect on APD:

*“In response to the uniquely challenging situation faced by Northern Ireland, the only part of the UK to share a land border with another EU member state, the government took the decision, in line with the wishes of the Northern Ireland Executive, to devolve powers over APD rates for long haul flights to the Northern Ireland Assembly (NIA).”*

<sup>15</sup> <http://researchbriefings.parliament.uk/ResearchBriefing/Summary/SN06649>

<sup>16</sup> <http://researchbriefings.parliament.uk/ResearchBriefing/Summary/SN00323>

If APD was devolved within England, there would be the prospect of a multitude of such 'land borders' between regions and authorities, resulting in a constant change of rates for competitive reasons and a significant additional administrative burden and cost for airlines. This proposal would create a tax system lacking in stability, certainty, practicality and coherence. Such a system would pose problems for airlines in being able to plan routes and make investment decisions.

There may be an assumption that devolving APD will result in rates reducing, but there is the possibility, given the local authority funding challenges, that regions and authorities may actually seek to increase their rates. This may mean the UK becoming even more uncompetitive, with higher tax rates.

The **Airports Commission considered devolving and varying APD** in their Interim Report<sup>17</sup> and found that:

*“Devolving APD would do little to incentivise better use of existing capacity at regional airports in England, and could potentially distort competition between proximate airports on either side of a border such as Bristol and Cardiff, or Newcastle and Edinburgh. Regional variations in APD could potentially give rise to perverse incentives, for example, not to use spare capacity in London and the South East, as currently exists at Stansted and Luton.”*

Finally, we are concerned that local authorities would either need to develop and invest in the necessary expertise, resources and capacity to **administer a devolved system of APD** themselves or contract and pay HMRC to fulfil this role. This does not appear to be a cost-effective or efficient use of taxpayer's money and presents the possibility of varied, complex and expensive administrative systems operating across the country.

**Option 2: Varying APD rates within England.** Central government would retain powers over APD, apart from where these have been devolved to Scotland, Wales and Northern Ireland. The rates of UK APD would be varied according to specific criteria, resulting in different rates in different parts of the country.

We do not believe this option meets the commonly accepted principles of good taxation as set out above and therefore we do not support it. This option, as presented in the discussion paper, lacks sufficient clarity and detail to allow a comprehensive response.

We note this that option has already been considered and dismissed by the Airports Commission. Congested airports are already priced differently in the highly competitive, global market in which the airline industry operates.

Furthermore, we feel that there is an issue of basic fairness at stake when UK residents face paying different levels of tax to fly simply because they live in different parts of the country.

The discussion paper is correct in assessing that varying APD rates regionally would lead to a more complicated tax collection environment, which would increase administrative burdens on both airlines and HMRC.

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<sup>17</sup> [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/271231/airports-commission-interim-report.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/271231/airports-commission-interim-report.pdf) p.119

We also note the question over the legality of this option in relation to EU law and that the discussion paper itself concludes that, *“it is unclear if this option would be effective in supporting those airports most likely to be affected by lower APD rates in Scotland and Wales”*.

**Option 3: Providing aid to regional airports within England.** The provision of aid to those airports or regions particularly affected by the devolution of APD.

Fundamentally, this approach would do nothing to address the competitive impact of the halving of APD in Scotland for existing routes in England.

While all English airports would be affected by devolution of APD to Scotland and Wales, the discussion paper is correct in assessing that, due to the EU State Aid Guidelines, many of the airports likely to be particularly affected are too large to be eligible for aid, as is shown below.

CAA 2014 Airport Passenger Data<sup>18</sup>

**More than 5 million passengers – highly unlikely to be eligible for aid**

Manchester	21,989,682
Birmingham	9,705,955
Bristol	6,339,805

**3-5 million passengers – possible that may be eligible, but would need to meet very strict and demanding criteria**

Newcastle	4,516,739
East Midlands	4,510,544
Liverpool	3,986,654
Leeds Bradford	3,274,474

**Upto 3 million passengers – the most likely to be eligible for aid**

Exeter	767,404
Humberside	239,173
Newquay	221,047
Durham Tees Valley	142,379
Gloucestershire	15,172

The combination of the restrictions of the EU State Aid Guidelines together with the ineffectualness of the proposal in alleviating the core problems created by devolution of APD, mean that we cannot support it.

## Conclusion

As the House of Commons Transport Select Committee so eloquently summarised in their recent report on smaller airports<sup>19</sup>:

*“If APD were scrapped in Scotland, airports in England would be subject to a similar competitive disadvantage to that currently experienced in Northern Ireland. The further devolution of APD to, for example, north-east England or Wales would ultimately serve to extend a patchwork of APD-derived*

<sup>18</sup> [http://www.caa.co.uk/docs/80/airport\\_data/2014Annual/Table\\_09\\_Terminal\\_and\\_Transit\\_Pax\\_2014.pdf](http://www.caa.co.uk/docs/80/airport_data/2014Annual/Table_09_Terminal_and_Transit_Pax_2014.pdf)

<sup>19</sup> <http://www.publications.parliament.uk/pa/cm201415/cmselect/cmtran/713/713.pdf> p.10

*market distortions across the UK and drive a race to the bottom on regional APD rates. We would prefer the Government to act strategically and in the national interest to address APD.”*

*“The way in which APD is double-charged on domestic return flights is damaging to UK smaller airports. In effect, it incentivises airlines and passengers to fly from airports located in other EU member states. It cannot be revised to allow UK airports to compete on a level playing field in the European marketplace because of the operation of EU competition law. The proposed devolution of APD to Scotland threatens to create further market distortions which could severely disadvantage airports in England.”*

None of the three options in the discussion paper should or can realistically be taken forward. Instead, Government should focus on introducing a sensible, simple and clear policy to abolish APD as soon as possible.

BATA  
September 2015