

Meeting: Stansted Airport Advisory Panel **Date:** 19th May 2021
Title: Government consultation on aviation tax reform
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Summary

1. The Government committed to consult on aviation tax reform in the 2020 Budget and, in particular, the case for amending the Air Passenger Duty (APD) treatment of domestic flights and for increasing the number of international distance bands.
2. This consultation sets out the Government's current approach to levying APD. It then seeks views on the Government's initial policy position that in order to support Union and domestic connectivity, the effective rate of APD on domestic flights should be reduced and the potential options through which this could be achieved. It also seeks views on a potential increase to the number of distance bands, in order to align the tax on international flights more closely with UK environmental objectives.
3. The consultation also sets out the Government's initial position on a potential Frequent Flyer Levy (FFL).

Recommendation

4. That the Panel:
 - i) considers the officers' response to the consultation and advises of any changes it would like made, and
 - ii) endorses the final response which will then be put to Cabinet for ratification

Financial Implications

5. None.

Background Papers

6. None.

Impact

- 7.

Communication/Consultation	The consultation runs from 23 rd March to 15 th June 2021.
Community Safety	To be carried out by the Government.
Equalities	To be carried out by the Government.
Health and Safety	To be carried out by the Government.
Human Rights/Legal Implications	To be carried out by the Government.
Sustainability	To be carried out by the Government.
Ward-specific impacts	Districtwide – passengers and those affected by airport activity.
Workforce/Workplace	Officer and member time in considering the Council’s response.

Situation

8. This consultation is available on gov.uk, a link to which is given here: <https://www.gov.uk/government/consultations/consultation-on-aviation-tax-reform>
9. The consultation is an industry-wide one and contains 25 questions in total. It is not expected that consultees will respond to every question. Many of the questions are directed towards the aviation industry and, in particular, those who collect APD. Responses are requested by email.
10. It is not intended to go through each question individually in this report, but rather to concentrate on the main principles behind the imposition and levying of APD. Once the response has been agreed, it is suggested that officers complete the detailed reply via the online questions as set out in Appendix A. In the remainder of this report, officers’ comments are in **bold** to distinguish them from the explanatory text. Much of the explanatory text is taken from the wording of the consultation document.

Current operation of APD

11. APD is the UK’s principal aviation tax as tickets are VAT free and there is no aviation fuel duty. APD raised £3.6bn in 2019-2020. Due to the pandemic, from April to September 2020 APD receipts were down 86.9% compared to the equivalent period the previous year. APD is paid by airlines on a per-passenger basis on all flights departing UK airports. The rates differ according to class of travel, distance and, to a degree, aircraft weight and specification.

International arriving passengers do not pay APD.

12. There are two APD distance bands, 0-2,000 miles (Band A) and 2,000 miles + (Band B) as measured from capital city to capital city. From 1st April this year, the amount of APD paid per flight varies from £13 to £541. Band A includes all domestic flights.
13. The Government's objectives are that aviation tax:
 - supports Union and international connectivity;
 - aligns with environmental objectives, particularly the commitment to net zero emissions by 2050; and
 - ensures the aviation sector makes a fair contribution to public finances.
14. **The Climate Change Committee's (CCC) December 2020 report on the Sixth Carbon Budget mentions APD once in its aviation sector summary. It says:**

“The particular policies that might be utilised to manage demand could have different impacts on ticket prices (e.g. carbon pricing, frequent flier levy, VAT, fuel duty, APD reform, airport capacity management). CCC analysis has focused on the outcomes (demand, fuel and emissions), rather than prescribing or modelling the policy method for achieving the demand levels required”.
15. **The CCC does not therefore express an opinion on what future rates of APD should be or whether it should be retained or abolished.**

Domestic air connectivity

16. The Government cites domestic air connectivity as vital to UK integration and social cohesion, particularly travel between Great Britain and Northern Ireland as well as connections from the Scottish Highlands and Islands to the mainland. Also, regional airports in all UK nations play a crucial role, acting as hubs for growth by serving local businesses and aiding tourism. Finally, domestic air connectivity into international hubs (such as Heathrow) can foster greater global connectivity.
17. The Government currently supports UK air connectivity via Public Service Obligations (PSOs). A PSO is a domestic air route that is deemed essential for connectivity but is commercially unviable, and therefore benefits from a direct subsidy and an APD exemption. There are currently 22 such routes in the UK, which connect Anglesey to Cardiff; Dundee, Derry and Newquay to London;

and 18 further routes connecting Scottish airports.

- 18. In 2019, according to CAA data, Stansted handled about 1.55 million domestic passengers mostly to Edinburgh, Belfast International and Glasgow. Other destinations included Derry, Guernsey and Dundee. Domestic passengers made up about 5.5% of the airport total for that year. 2020 date will be unrepresentative due to the pandemic, and the extent of recovery to former levels is not known.**
19. The Government has received several representations from the aviation sector, including in response to Sir Peter Hendy CBE's Union Connectivity Review, that a reduction in the rate of APD on domestic flights could provide a further boost to Union air connectivity, by supporting the economic viability of domestic air routes, potentially leading to the introduction of new domestic air routes or increased frequency on existing routes. Previously, the Prime Minister has remarked on the apparent unfairness of a return passenger from Belfast to London being liable to twice the rate of APD compared to a Dublin to London passenger.
- 20. In the Aviation 2050 (the future of aviation) consultation, in the section on supporting regional growth and connectivity, the Government stated that without APD, aviation would be relatively under-taxed compared to other sectors. It also said that the economic competitiveness of the UK's regions and nations remained a priority, recognising the benefits that new air routes can bring, both in terms of better connecting UK regions to each other and providing connections to the rest of the world.**
21. The Government's initial policy position is that the effective rate of APD on domestic flights should be reduced, in order to support Union and regional connectivity. Such a proposed reduction would apply to all flights departing from a UK airport to a destination within the UK. There are two potential policy options that could achieve this outcome, namely: (1) the introduction of an APD exemption for the return leg of domestic return flights; or (2) the introduction of a new band for domestic flights. Option 1 could effectively halve the rate of domestic APD in certain circumstances – the effect of Option 2 would depend upon the amount of the levy.

Policy Option 1: return leg exemption

22. Domestic flights would continue to be treated within the lowest APD band, but airlines would not be liable to pay APD for passengers travelling on the return leg of a domestic flight. The exemption could operate as follows:
- evidence required that a passenger was travelling on a return ticket, i.e. that both legs of the journey were purchased at the same time, although there would be no time limit on when the return leg took place:

- APD would still be due on the outbound leg:
- exemptions would only apply to passengers travelling between the same UK airports:
- both the outbound and return service would need to be provided by the same carrier; and
- the exemption would apply across all classes of travel including business jets.

23. The Government's view is that a return leg exemption could be administratively complex for both Her Majesty's Revenue and Customs (HMRC) and airlines and would not benefit domestic travellers on a single ticket. Modern ticketing practices may make it less likely for passengers to purchase a return ticket.

24. When APD was first introduced in 1994 it did include a return leg exemption. This was removed in 2001 in response to concerns from the European Commission.

Policy Option 2: a new APD band for domestic flights

25. The Government is considering introducing a new, separate domestic band within APD for routes between UK airports, which would be set at a lower rate than the shortest international band.

26. The introduction of a new domestic band would ensure that all domestic flights benefited from a lower rate of APD, including single leg journeys. The Government considers that such an approach would be simpler for HMRC and airlines to administer than a proposed return leg exemption, because it would apply to all domestic flights, not just those on a return ticket.

27. The Government's position is that the introduction of a new domestic band is favoured above a return leg exemption.

28. In its response, the Council should refer to the climate and ecological emergency that it declared in 2019 (along with many other local authorities) with an aim to achieving net-zero carbon status by 2030. Whilst domestic aviation only contributed 1.4MtCO₂e in 2019 (3.6% of the UK's total 2019 aviation emissions), APD reform should not result in a total tax burden on domestic passengers that is lower than before the reform took place. It is not clear how a tax policy that would encourage more domestic flights is a sustainable one in either the short or longer term.

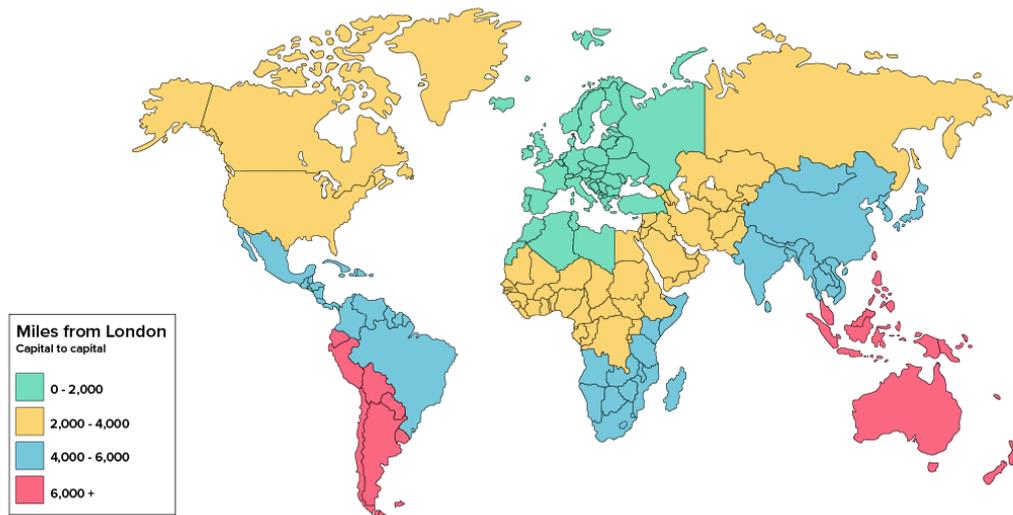
29. **Of the two options being proposed, Option 2 seems the easiest to impose because it would be per passenger per flight, as now. The main problem with Option 1 is that the rationale behind it is not obvious – why, for instance, should passengers benefit from an exemption for booking a return flight rather than two singles. However, neither option would incentivise the use of more sustainable domestic travel modes if others were possible.**
30. **Through the Council’s membership of the Strategic Aviation Special Interest Group (SASIG) of the Local Government Association, it is clear that many member authorities (particularly in the south west and north) attach considerable importance to domestic air connectivity for economic and social wellbeing. APD exemptions should continue to apply to PSO routes, and it is noted that this consultation is not proposing the removal of this exemption.**

International distance bands

31. The Government states that aviation is currently responsible for 8% of the UK’s Greenhouse Gas emissions. Emissions from international aviation are responsible for the majority of the sector’s environmental impact, contributing 37MtCO₂e in 2019, and have more than doubled since 1990. The majority of the increase came in the 1990s and early 2000s, however emissions have also been increasing since 2012. UK domestic aviation contributed 1.4 MtCO₂e in 2019, representing less than 1% of UK Greenhouse Gas emissions. The aviation sector’s proportion of UK emissions is forecast to increase nearer to 2050, as other sectors decarbonise more quickly. The sector also contributes to Nitrogen Oxide (NO_x) and noise pollution amongst others.
32. The Government’s position is that the number of international distance bands should be increased to align APD more closely with environmental objectives, including the “polluter pays” principle. This means that those who travel furthest internationally, and consequently have the greatest impact on the environment, pay the most APD. Increasing international APD revenue could also make up any shortfall from decreasing the domestic levy, but if the new post-pandemic baseline is less international flying that might not be the case.

Policy Option A; revert to the 2008 distance band structure

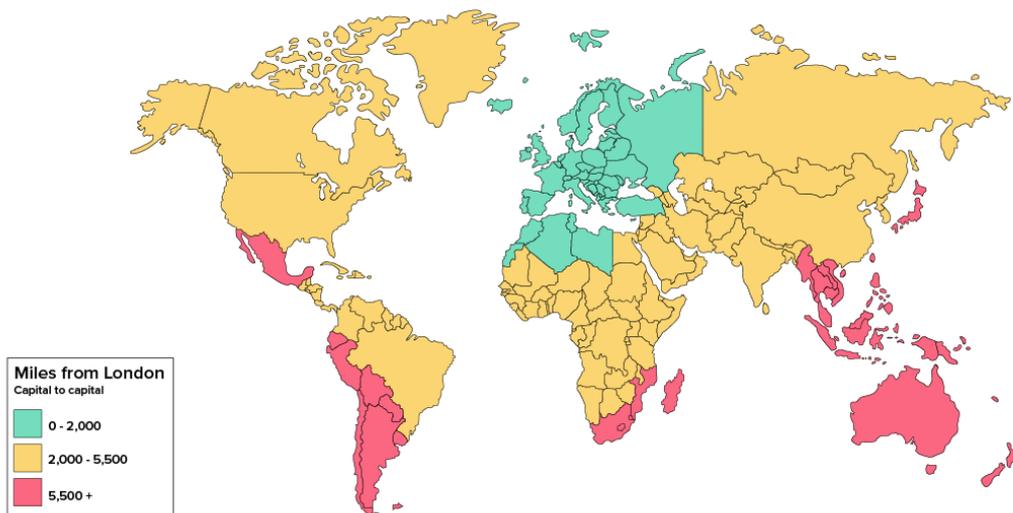
33. Under this option, the 2008 band structure could be reintroduced as shown in the chart below, which is taken from the consultation document. This reversion should be relatively simple for airlines.



34. However, there were some practical issues, notably between Bands B (yellow) and C (blue). The whole of the USA was in Band B whereas the Caribbean was in Band C because of the distances between the respective capital cities. For this reason, the current two-band structure has been used since 2014 (see paragraph 12).

Policy Option B: design a new distance band structure

35. Under this option, there would be three distance bands as shown in the chart below, which is also taken from the consultation document.



36. As with Option A, this would strengthen the “polluter pays” principle, but it would reduce the number of destinations that were subject to differential APD

treatment.

- 37. International APD should be reformed so that it increases the tax burden on those who fly more frequently and furthest. This would be consistent with the bringing of Carbon Budget 6 into law, including international aviation and shipping emissions for the first time rather than the existing “headroom” provision. Option B would seem to overcome the tax calculation anomalies that would occur with Option A, although any banding system is likely to throw up some inconsistencies.**

Frequent flyer levy

38. The Committee on Climate Change and several environmental stakeholders have suggested that the Government should introduce an FFL, in order to tackle the environmental impacts of flying in an equitable way. An FFL would seek to constrain overall demand for flights, by increasing the amount of tax liability due, according to the number of flights a passenger had previously taken. Unlike APD, FFL would be levied on the individual, rather than the airline.
39. The Government considers that an FFL would be significantly more complex to administer than APD, for both airlines and HMRC, on the basis that it could require the collection and storage of personal information on each passenger. The Government would have to be able to record and identify every flight an individual took from a UK airport for the purposes of calculating how many flights they had taken within a given period. This would not only increase complexity (because of the significant increase in taxpayers) but may also pose concerns around data processing, handling and privacy. There may be additional compliance issues, particularly with passengers who were able to travel under multiple passports. It may also pose challenges for individuals who have an essential need to fly frequently.
40. The Government points out that airlines ordinarily pass on the cost of APD to passengers, so those who fly more will already pay more under the APD structure. The Government says it is minded to retain APD as the principal tax on the aviation sector and not introduce an FFL.
- 41. Imposing an FFL would seem to be administratively difficult, as the Government acknowledges and should not be preferred to retaining and reforming APD. APD, by the way it is levied, already picks up the more frequent flyers and international distance band reform would enhance the “polluter pays” principle.**

Risk Analysis

42.

Risk	Likelihood	Impact	Mitigating actions
The Government is not able to take the Council's views into account as part of the consultation process.	1 The consultation process is designed to allow all views to be considered.	2 Aviation taxation is a national issue, but aviation is one of the most difficult industries to decarbonise, so treatment of taxation is an important factor to consider.	Respond to the consultation.

1 = Little or no risk or impact

2 = Some risk or impact – action may be necessary.

3 = Significant risk or impact – action required

4 = Near certainty of risk occurring, catastrophic effect or failure of project.