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Bob Harper

Legislative Consent Motion: UK Finance (No. 4) Bill 2012 Air Passenger Duty

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This Paper provides background on the forthcoming legislative consent motion that is to be put forward by the Department of Finance and Personnel. The motion concerns the devolution of Air Passenger Duty (APD) to Northern Ireland, as proposed by the UK Government's *Finance (No. 4) Bill 2012*, which is currently under consideration in Westminster. Details surrounding the general APD debate are outlined, as well as potential issues for consideration.

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Executive Summary

The UK *Finance (No. 4) Bill 2012*, currently at Committee Stage in Westminster, makes provision for the devolution of aspects of power over rates of Air Passenger Duty (APD) to the Northern Ireland Assembly. Under section 4(3) in the *Northern Ireland Act 1998*, and Standing Order 42(A), a legislative consent motion (LCM) will be moved by the Minister of Finance and Personnel seeking the Assembly's agreement that this matter be devolved.

Under clause 189 and schedule 23 to the *Finance (No. 4) Bill*, the Northern Ireland Assembly will be able to:

- Set the rate of Air Passenger Duty on direct long haul flights departing from airports in Northern Ireland.

The Assembly will not have the power to set the rate of APD on short haul 'Band A' flights. APD, in the more general sense of its structure, remains an excepted matter as it is a UK-wide duty.

At this time, the rate of APD on direct long haul flights from NI is held at a reduced level equal to the short haul rate of duty. This measure, in effect from 1 November 2011, was made by the UK Government in response to a risk that the sole direct long haul flight from Northern Ireland would be withdrawn.

Since its introduction in 1994, APD has undergone many changes, increases in rate and attempted reform. Currently, four destination 'bands' (A, B, C and D, increasing in distance from the UK and payable rate), together with higher rates on first class travel, determine the cost of the duty to passengers. The duty was brought in as a revenue raising measure; though some argue that it has environmental side benefits, this remains its primary function.

Attempted reforms and Treasury consultations in recent years, coupled with regular increases in the rate, have highlighted the arguments for the modification or abolition of APD. The UK is one of only a few countries with a tax on air travel, and it is regularly mentioned that UK passengers pay the highest rate worldwide.

Critics argue that APD harms the travel and tourism sectors, business and investment, all of which is damaging to the wider economy. They insist that its removal would bring greater benefits to economic growth than raising revenue can provide. Additionally, as an indirect taxation, critics argue that increases are socially regressive and harm poorer travellers the most. Furthermore, a greater burden of the tax is paid by travellers on the longest flights; while those who travel domestically within the UK pay the tax twice on a return flight.

Calls for a per plane charge to replace the current structure have been made on environmental arguments. While the UK Government has sought to make this change, international conventions on air travel have legally blocked this option. Other critics argue that APD should be offset by the recent introduction of the EU Emission Trading Scheme (ETS), which will further increase the cost of air travel.

Specifically to Northern Ireland, the land border with the Republic of Ireland, and relatively

short travel distance to Dublin Airport, presents the greatest challenge. NI's position within the UK is unique, as it is the only region sharing a border with a low air tax regime. RoI currently charges a €3 Air Travel Tax (ATT), with the possibility of future abolition. Generally, ticket prices for direct air travel to NI will be more expensive than for travel to RoI airports, especially when long haul rates of duty are taken into account. This sets NI at a distinct disadvantage when it comes to competing for airline routes, with the extra harm to business, tourism and the local economy that this brings.

Furthermore, as NI is peripheral to the UK, separated by the Irish Sea, domestic travel options are limited, and dependence on airplanes for short haul travel is high. Critics within NI argue that APD causes an inherent unfairness and financial disadvantage upon NI consumers.

The process of devolving aspects of APD to NI was started by a HM Treasury consultation on potential reform of APD. The Northern Ireland Affairs Committee (NIAC) in Westminster held a short inquiry into the implications of APD for NI before the current proposals for devolution were made. NIAC recommended a zero-rate of APD on *all* flights from, *and to*, NI airports, with the devolution of the power to set and vary APD to the Assembly in future.

Many witnesses and written submissions to the Committee for Finance and Personnel's inquiry reiterated a desire that short haul rates of duty be devolved and set to a zero-rate. This creates a contrast with the current proposals for devolution in the *Finance Bill,* as short haul flights are not included, nor are flights to NI from other UK airports. An important statistic to note is that 98.5% of all flights from NI airports are in the short haul 'Band A' category; 75% of which are domestic (within the UK).

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1. Introduction

Under Standing Order 42A[1] the Minister of Finance and Personnel has tabled a legislative consent motion relating to the *Finance (No. 4) Bill 2012:*

> *"That this Assembly agrees that the provisions in clause 189 of, and Schedule 23 to, the Finance (No. 4) Bill, as introduced in the House of Commons on 26 March 2012, dealing with the devolution of Northern Ireland long haul rates of air passenger duty should be considered by the UK Parliament."*

In effect, this motion, if approved by the Assembly, gives consent to the provisions contained within the *Finance (No. 4) Bill* (discussed in detail in Section 3) and allows the House of Commons to proceed with its consideration and potential enactment of the Bill.

This briefing paper is prepared for Members of the Committee for Finance and Personnel in the Assembly, to facilitate their consideration of the *Finance (No. 4) Bill* and related legislative consent motion. APD is of particular interest to Members, as the manner in which it is devolved may help to inform, to a lesser or greater extent, how further fiscal devolution – if any – will occur.

The paper is divided into 8 sections:

- Section 2 examines the background of APD and the changes it has undergone since its formation;
- Section 3 examines the provisions in the Finance Bill for devolving some APD powers to the Northern Ireland Assembly;
- Section 4 outlines some of the general arguments in favour of the reform or removal of APD across the UK;
- Section 5 considers the process through which the current proposals have been reached and the arguments for devolving APD to NI;
- Section 6 provides a comparison with Scotland and Wales given their similar consideration of this issue;
- Section 7 provides further comparative information, outlining similar taxes in other countries, with particular reference to the Republic of Ireland; and
- Section 8 concludes with potential key issues for consideration.

2. Background

This section details the history of Air Passenger Duty (APD), from its introduction in 1994 to the most recent alterations which the duty has received.

[1] *Northern Ireland Assembly*, Standing Order 42A

2.1. Introduction of Air Passenger Duty and subsequent changes

Air Passenger Duty was introduced in the United Kingdom in 1994 by the then Chancellor, Mr Kenneth Clarke MP. Subsequent changes have been made to the structure of APD and the rates themselves through various Finance Acts. The primary legislation on APD can be found in the *Finance Act 1994* (sections 28 to 44 and schedules 5A and 6).[2]

APD is a revenue raising tax with some environmental benefits. The duty is levied on passengers flying from a UK airport on planes which have a weight of at least ten tonnes or at least 20 passenger seats (planes which do not meet either of these criteria are exempt from APD). However, the duty is not payable when a UK airport is used as a stopover on an international flight for less than 24 hours. VAT is not paid on airplane tickets; and commercial aviation fuel is exempt from taxation.

2.1.1. When introduced

Originally, when APD was introduced in 1994 two 'bands' were created: the closest foreign destinations and UK internal travel carried a levy of £5; while further afield destinations carried a levy of £10.[3]

2.1.2. Subsequent APD changes

Subsequently, two new 'bands' were created by the *Finance Act 2000:* concerning destination and, for the first time, class of travel. European (EEA) destinations were charged the least (£5 in standard, or economy, class and £10 in other classes) and other destinations charged at higher rates (£20 in standard, or economy, class and £40 in other classes).[4] These rates were later doubled by the *Finance Act 2007*.[5]

In 2009 the duty was restructured by Mr Alistair Darling MP, under the *Finance Act 2009*.[6] There were now four geographical 'bands'; with two different rates for standard and other classes of travel within each band. The 2009 Act also introduced substantially higher rates of APD for each degree of travel. This was in response to a pre-budget consultation which had attempted to bring in a per plane tax to replace APD for environmental reasons. However, this plan was abandoned after concerns that it would harm the aviation industry.[7]

The June Budget 2010 launched a consultation exercise, which again looked at switching from a per-passenger to a per plane duty. This approach was abandoned, however, due to legality and feasibility arguments surrounding the UK's obligation under Air Service Agreements with 150 other countries and its commitment to the 1944 *Chicago Convention on International Civil Aviation*.[8] However, in *Budget 2011,* the Government announced a longer-

[2] Finance Act 1994: ss 28 -44, sch 5A and sch 6
[3] *Finance Act 1994* (original, as enacted): s 30 (The rate of duty)
[4] *Finance Act 2000*: ss 18-19
[5] *Finance Act 2007*: s 12
[6] *Finance Act 2009*: s 17
[7] HC Deb, 24 November 2008, vol 483, col 499
[8] International Civil Aviation Authority, *Chigaco convention on International Civil Aviation*, 1944. Note: the Chicago convention was signed by 52 states in 1944. Article 24 exempts aircraft themselves from custom duty.

term commitment to work with international partners in moving to a per plane duty.[9]

2.1.3. Imminent APD changes

In the March Budget 2011 the Chancellor launched a consultation on improving the efficiency and fairness of APD.[10] Issues raised related to changing the banding structure, the possible devolution of APD to Scotland, Northern Ireland and Wales, and geographical anomalies present in the current system. For example, as the current banding system uses the capital cities of destination countries to assign bands, flights to Caribbean destinations are subject to a higher band (Band C) of duty than flights to California and even Hawaii (Band B).[11] The Government's response was that the current banding structure would be retained as a revenue neutral system change would incur greater charges on flights within the UK and to European destinations. The Government also decided that private business jets should no longer be exempt from APD due to their small size of less than 10 tonnes.[12]

In the same Budget, it was announced that APD rates would be frozen for the 2011-12 financial year and the proposed Retail Price Index (RPI) increase deferred until April 2012 (increased detailed below).[13] As a result of the one-year deferment this would be a large "double inflation" increase.

3. The Finance (No. 4) Bill 2012

As well as the increases in the current rates of Air Passenger Duty and changes to the definition of chargeable aircraft, the *Finance Bill 2012* provides for the devolution of long haul rates of APD to Northern Ireland. The Bill provides for amendments to the *Finance Act 1994*, as this is the primary legislation to which Air Passenger Duty is given effect.[14]

The First Reading of the Bill was made on 26 March 2012 and the second on 16 April 2012. The Bill is a 'Money Bill', meaning that the House of Lords has no power to amend it or fail to pass it.

Clause 189 of the Bill gives effect to the devolution of rates of Air Passenger Duty on direct-long haul flights from Northern Ireland:

> *"Schedule 23 amends, and makes amendments connected with, Chapter 4 of Part 1 of FA 1994 (air passenger duty)."*[15]

The provisions of the Bill are explained below, in accordance with the parts stated in schedule 23 of the Bill.[16] As this part of the Bill is quite detailed and contains some

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[9] HM Treasury, *Budget 2011,* p 39 and House of Commons, *Official Report (Hansard) 23 March 2011 (Budget speech),* Col 963

[10] http://www.hm-treasury.gov.uk/2011budget_airpassenger.htm (accessed 24 April 2012)

[11] Under the *Finance Act 2009*: sch 5A, Aruba, Jamaica, etc. (Part 3) are further away than the USA (Part 2), under which Hawaiian destinations are considered. This results in Caribbean destination flights having a higher rate of duty payable.

[12] HM Treasury, *Reform of APD consultation response document*, December 2011

[13] HM Treasury, *Budget 2011,* p 39

[14] *Finance Act 1994:* ss 28-44, sch 5A and sch 6 (N.B.: amendments to the 1994 Act are still to be updated in this version; the online version still shows the pre-2009 structure to APD).

[15] *Finance Bill 2012,* cl 189

[16] *Finance Bill 2012,* sch 23

consequential clauses only the most important aspects of the schedule are discussed in order to give a meaningful overview.

3.1. Part 1: Northern Ireland long haul rates of duty from 1 November 2011 to 31 March 2012 (paragraphs 1-3)

Paragraphs 1 to 3 of schedule 23 give statutory effect to the rate reduction, which had been applied to long haul flights departing from Northern Ireland between 1 November 2011 and 31 March 2012. These are the same flights for which the responsibility for setting the rate of APD will be devolved to the Northern Ireland Assembly. Effectively, the rates of ‘Band B’, ‘C’ and ‘D’ flights are held at the same rate as for ‘Band A’: £12 on standard (economy) tickets and £24 on all other classes of travel.

3.2. Part 2: Rates of duty from 1 April 2012 (paragraphs 4-6)

Paragraphs 4-6 of schedule 23 provide for the increases in APD by amending section 30 of the *Finance Act 1994*. The proposed 2011 increases had been deferred for a year; therefore, the increases seen here are quite large and are as presented in Table 1, below. The increases range from £1 (for the shortest economy seat tickets) to £14 (for premium seat tickets on the longest flights).

The *Finance (No. 4) Bill 2012* contains the increases for each band, as detailed below:

Destination Bands and distance from London*	**Standard (economy) rate†**		**Other rates of travel**	
	Current rate	Rate from 1 April 2012	Current rate	Rate from 1 April 2012
Band A (0-2000 miles)	£12	£13	£24	£26
Band B (2001-4000 miles)	£60	£65	£120	£130
Band C (4001-6000 miles)	£75	£81	£150	£162
Band D (over 6000 miles)	£85	£92	£170	£184

†For the purposes of the *Finance Act 1994*, “standard” class is the class available if there is only one class on board a flight, or the lowest class available on other flights with multiple classes of carriage.

***Countries of destination appear in various “bands”, depending in which band the capital of the destination country is from London. The various countries are listed in schedule 5A of the *Finance Act 1994*, Part I relate to Band A, Part 2 relate to Band B and Part 3 relate to Band C. Any country not listed in Schedule 5A is treated as Band D.**

Table 1: Increase in rates from 1 April 2012 as contained in the *Finance (No. 4) Bill 2012*

Paragraph 4(6) inserts new subsections (4B) to 4(D) into the *Finance Act 1994* section 30, extending the holding of long haul rates from Northern Ireland at the new 'Band A' level from 1 April 2012, until the power to set rates is devolved to the Assembly. Therefore, all flights departing from Northern Ireland, no matter their destination, will be charged the new APD of £13 in economy class and £26 on other classes. In effect, the situation between 1 November 2011 and 31 March 2012 is extended for the foreseeable future.

3.3. Part 3: Devolution of Northern Ireland long haul rates of duty (paragraphs 7-15)

Paragraphs 7-15 of schedule 23 devolve direct long haul flight rates of APD to Northern Ireland.

First, as stated by paragraph 8, the subsections inserted by paragraph 4(6) (as detailed above) will be omitted. As stated by paragraph 9, these will be replaced by a new section 30A (Northern Ireland long haul rates of duty), the subsections of which are explained in the following:

- As defined by new subsection (1), this section will apply to flights originating in Northern Ireland as long as they are not to a 'Band A' destination (as defined by Part 1 of Schedule 5A of the *Finance Act 1994*), and as long as they are not followed by a connecting flight within the United Kingdom or 'Band A' territories (this stops passengers from using Northern Ireland airports as a starting point to avoid the higher rates of duty payable in the rest of the UK).

- New subsections (3), (4) and (5) hold Northern Ireland to the current "banding" structure of Air Passenger Duty: there is scope only to lower the rate of APD paid on these flights, and each band/class of travel may be set at separate rates if the Assembly so wishes. Under subsection (6) Northern Ireland is permitted to set a zero rate (£0), in effect, long haul flights could pay less duty than 'Band A' flights, which are held to the rate set by Westminster.

- New subsection (11) states that schedules 2 and 3 of the *Northern Ireland Act 1998* do not apply in respect of the provisions which may be made by Act of the Northern Ireland Assembly in relation to this part of the *Finance Act*. Schedules 2 and 3 detail the excepted and reserved matters which are retained by Westminster; as these include "*taxes or duties under any law applying to the United Kingdom as a whole*".[17] This is discussed in more detail in section 5.6 of this paper.

- New subsections (12) to (14) set out the detail of how the Assembly will set rates. The rates of duty must be detailed in a Bill brought to the Assembly by the Minister of Finance and Personnel (or signified on the Minister's behalf). The Bill then has to be passed into statue with cross-community support, as defined in section 4(5) of the *Northern Ireland Act 1998*.[18]

[17] *Northern Ireland Act 1998*, sch 2 s 9(a)
[18] *Northern Ireland Act 1998*, s 4(5)

- New subsection (15) provides that any duty collected on these devolved rates will be paid into the Consolidated Fund of Northern Ireland. Obviously, if all long haul rates are all set at zero there will be no payment into the Fund.
- These changes will take effect on the 'relevant day' that a commencement order stipulates, as specified by paragraph 9(9). Therefore, the current situation (long haul rates held at the short haul rate of duty) will continue until this order is made.

Secondly, paragraph 10 deals with section 33 of the *Finance Act 1994*, which deals with the register of aircraft operators, the responsibility for which lays with HM Revenue and Customs (the Commissioners). Paragraph 11 specifies that HMRC may keep a separate register of aircraft operators flying from Northern Ireland, and requires such operators to notify the HMRC of their liability to pay the devolved rates (while passengers pay the duty the responsibility for collected and payment lies with the airline).

Paragraph 13 inserts a new section 41A into the *Finance Act 1994* providing for HMRC to disclose information relating to devolved rates of duty (e.g. their collection, revenue raised, etc.) to the Secretary of State, Treasury or Department of Finance and Personnel. This information will assist with the setting of rates and calculation of the Northern Ireland budget. This new section also prohibits further disclosure without consent.

3.4. Part 4: Other provisions (paragraphs 16-23)

Paragraphs 16-23 of schedule 23 provide for the extension of APD to smaller aircraft.[19]

- The Chancellor's *Autumn Statement 2011* confirmed the intention to extend APD to small business jets, which are currently exempt due to the restrictions on weight and size.[20] This extension is to be effected through the *Finance Bill 2012*, and will result in most business jet passengers will be subject to the same rates of duty as commercial aircraft passengers.
- As has been mentioned, aircraft weighing less than ten tonnes or with fewer than 20 passenger seats are not chargeable in the case of APD. Under the tabled changes only aircraft under 5.7 tonnes or fuelled by something other than kerosene will be exempt from charge (regardless of seat numbers) in future. In fact, if the aircraft is above 20 tonnes but with fewer than 18 seats passengers will be charged at twice the higher class travel rate of APD.
- Under section 43 of the *Finance Act 1994* passengers who had travelled with a provider other than an airline are exempt from APD (for example, a private jet owned by a large business). The amended subsection (2) alters the interpretation of "passenger" to include all passengers (save for flight and cabin crew) and "arrangements for carriage" to include "informal agreements or arrangements between, for example, members of a family or friends".

[19] *Finance Bill 2012:* sch 23, pt 4. Note: aircraft with a weight of 5.7 tonnes or more will now be chargeable regardless of the number of seats for passengers.

[20] HM Treasury, *Autumn Statement 2011*, p 42

- The new section 29A exempts police, rescue and military aircraft etc. from these new provisions.
- Under paragraph 21 the above provisions are applied to Northern Ireland also, but the rates are set in accordance with the rates set by Act of the Northern Ireland Assembly.
- The logic behind these provisions is to close the gap which exempted business jet passengers from liability for APD, either because the aircraft was small enough to exempt it or they did not buy a ticket in the usual manner.
- Furthermore, aircraft above 20 tonnes but with fewer than 18 passenger seats (i.e. luxury private airlines – as there is no ready definition weight and seat number is used) will pay double the higher rate of APD, rather than the exemption they benefitted from beforehand.
- **Issue for consideration: if an Act of the Northern Ireland Assembly sets direct long haul non-standard rates of duty to £0, luxury private aircraft flying from Northern Ireland will be liable for a zero-rate of APD. This would create an anomaly as opposed to the situation in the rest of the UK after these proposed changes take effect.**

4. UK arguments for reform and removal of APD

Section 4 sets out some of the general arguments in favour of the reform or complete abolition of Air Passenger Duty in the UK, on the lines of environmental, economic and regional arguments. These cases are examined in relation to Northern Ireland in Section 5, of this paper.

4.1. Environmental arguments

Though APD was initially levied in order to raise revenue, the reasoning and interpretation of the tax has changed to one of environmental rationale: aiming for the reduction of carbon emissions. This approach has its critics: from those who oppose the duty as a form of unfair and economically damaging taxation; to those who criticise its appropriateness and effectiveness as an environmental instrument. The UK Government maintains, however, that APD is primarily a revenue raising tax with some environmental benefits.

After reforming the structure of APD in 2009, the Environmental Audit Committee made a recommendation that:

> *The Treasury must clear up the confusion as to whether Air Passenger Duty is an environmental tax.*[21]

To which the UK Government responded:

> *The Budget consultation and the subsequent Government Response made clear*

[21] Sixth Report of the Environmental Audit Committee, *Budget 2011 and Environmental Taxes* (HC 2010-12, 878), para 53

> *that the Government regards the core objective of Air Passenger Duty (APD) to be raising revenues for the Exchequer in a simple, fair and efficient manner.*
>
> *Moreover, evidence shows that changes in the structure of APD have only a negligible effect on CO2. Reductions in emissions from aviation can best be delivered through market-based mechanisms, agreed with our international partners.*[22]

One argument for reform questions the fact that the duty is imposed on passengers themselves – rather than on the plane – and does not account for the efficiency, size and occupancy of the aircraft. It is argued that a per plane duty will encourage aircraft operators to fill planes to capacity, therefore making a significant beneficial impact on the amount of emissions produced by having less planes in the sky. Another argument makes a case that the current banding system (which uses the distance of the destinations national capital city from London to designate bands) is illogical from an environmental perspective, resulting in Caribbean destinations incurring a larger duty than California.

As mentioned above, the 2010 consultation exercise looked at the issue of a per plane duty (ostensibly to replace the per passenger duty), but did not result in an effective commitment due to the presence of international treaties and the *Chicago Convention*. In *Budget 2011* Mr Osborne announced that the Government would seek to work with its international partners to resolve this situation.[23]

The Coalition manifestos both commit to reforming APD along environmental arguments. The Conservative Manifesto for 2010 stated that they would "*reform Air Passenger Duty to encourage a switch to fuller and cleaner planes"* and the Liberal Democrats sought a change to per plane duty with a higher rate charged on domestic flights where alternative less polluting travel was realistically possible.[24]

4.1.1. Emissions Trading Scheme

The EU Emissions Trading Scheme (ETS) was introduced in the UK in January 2012. As ETS is a cap-and-trade mechanism airlines will face extra costs depending on the efficiency of their aircraft, miles flown and load carried.

The Association of British Travel Agents (ABTA) estimate that passengers may be subject to increases of £4 on return flights within the EU, and £16 on return flights outside the EU area, possibly rising to £10 and £60 respectively by 2020.[25] The revenue raised is expected to be used by Member States to tackle climate change; however, the UK Government has made no commitment to do so. ABTA argue that with the introduction of ETS – a more practical method to tax aviation pollution costs – APD should be scrapped, (or at least offset against

[22] Sixth Special Report of the Environmental Audit Committee, *Budget 2011 and Environmental Taxes: Government Response to the Committee's Sixth Report* (HC 2010-12, 1527), paras 31-32

[23] HC Deb, 23 March 2011, vol 525, col 963

[24] House of Commons Library, *Air passenger duty: recent debates & reform*, 6 May 2011

[25] ABTA, *Emissions Trading*, (accessed 18 April 2012)

ETS) as it is a duplication of taxation.[26]

4.2. Economic arguments

Critics of APD argue that the duty is harmful to business and tourism as it imposes undue costs on travellers. They argue that British passengers pay the highest tax on travel in the World; and that the drop in passenger numbers from 2008 has been due to travellers being no longer able to afford to fly, mainly due to increases in APD coupled with global economic factors.[27]

4.2.1. Aviation

A low number of flights has a direct impact on jobs in the aviation industry. The industry directly employs over 141,000 people in the UK, and supports 93,000 extra jobs through the supply chain. Aviation employees are generally more productive in the economy, generating £62,000 added value, as opposed to £46,000 nationally.[28] Air transport directly contributes around £5bn-£6bn to the UK economy per annum through its business areas, so it is seen as a key industry.[29]

4.2.2. Tourism

On a wider scale, it is argued that the existence of a tax on air travel, or high rates of tax, discourages tourists from visiting the UK (as they will have to pay high rates of duty on their return tickets), therefore damaging airline operators and the potential to grow the economy through tourism. Similarly, the tax is also damaging to other countries which rely heavily on tourism, which includes visitors travelling from the UK.

4.2.3. Business

It is argued that the duty also harms business travel while increasing costs on businesses which have staff that have to travel by air, say the British Chambers of Commerce.[30] This leads to less spending within the national economy, both for domestic and foreign businesses. This consequentially harms inward investment and economic growth, again, both domestically and through foreign direct investment (FDI).[31]

4.2.4. Economy

The cumulative effect of the negative APD impact on the tourism, aviation and business sectors has an overall knock-on effect on the wider economy. This cost is much larger than the revenue raised through the duty, as represented through the opportunity cost of lost growth and the loss of job opportunities provided in each of the sectors.

[26] *Ibid*
[27] For details of passenger numbers at UK airports, see Civil Aviation Authority (CAA), *Aviation Trends,* (accessed 2 April 2012)
[28] Oxera, *What is the contribution of aviation to the UK economy?*, November 2009
[29] Office for National Statistics, *Annual Business Survey 2009, Regional Data: Division by Region*, (see GVA of SIC 51)
[30] British Chamber of Commerce, *Chancellor could have done more to support business confidence and growth*, 21 March 2012
[31] Federation of Small Businesses, written submission to the Committee for Finance and Personnel, April 2012

The International Air Transport Association (IATA) commented that if the Government merely reformed APD so that, while revenue neutral, the proportion of duty paid amongst the different bands was redistributed:

> *The GVA of the air transport sector would be improved and increased activity would have positive multiplier effects through the UK economy, boosting GDP by £66-123 million, jobs by up to 2,200, and raising non-APD tax revenues by £24-45 million.*[32]

A study by economic consultants, Oxera, found that a move from APD as it stands to a per plane tax would result in a large loss of jobs and damage to economic growth, especially if the change were to be revenue increasing. Regional economies would be more adversely affected, especially as they would lose air services as a result of a per plane tax.[33]

4.2.5. Equity

There is also the impact of indirect excise duty on the poorest travellers. Though passengers travelling in economy class pay a lower rate of duty, ABTA argues that:

> *tax rises are socially regressive and will impact most upon those who can least afford it and lead to families being priced out of taking flights. This is especially acute for lower socio-economic groups and ethnic minorities visiting friends and relatives abroad.*[34]

The 'Fair Tax on Flying' campaign is backed by 30 companies from the travel and air operator industry. Though they accept the need for air travel to pay its environmental cost, ABTA believe that the tax charged to consumers more than reflects this cost. They argue for a switch to a per plane tax at a level that will not be damaging to business.

The IATA also finds that APD penalises long haul travellers, who pay a higher proportion of duty in order to cross-subsidise short haul travellers. A study carried out by Oxford Economics finds that Band B-D passengers pay an average of 6% more in APD than Band A passengers as a percentage of the overall air fare, with Band C in particular paying 22% more for duty.[35]

Flybe, in its submission to the Treasury consultation, argued that there is an inherent unfairness in the APD structure which results in domestic passengers paying APD twice on return flights within the UK, while foreign travellers pay APD only once, due to the fact that the duty is payable on departing flights only. For instance, travelling from Belfast to Glasgow and back will be charged £26 total in APD (£13x2), while a return flight to any European destination (including Dalaman in Turkey, 4,352 miles round trip) would incur only £13 in duty.[36]

[32] IATA, *Economic Impact Of HM Treasury Proposals On UK Air Passenger Duty*, 15 June 2011
[33] Oxera, *Per plane or per passenger tax?*, September 2010
[34] ABTA, *Air Passenger Duty/'A Fair Tax on Flying' campaign*, (accessed 2 April 2012)
[35] IATA, *Economic Impact Of HM Treasury Proposals On UK Air Passenger Duty*, 15 June 2011
[36] Flybe, written submission to the Committee for Finance and Personnel, 19 April 2012

4.2.6. Revenue

The Treasury received £2.7bn in receipts from APD in 2011-12, which is expected to rise to £2.9bn 2012-13, £3bn 2013-14, £3.3bn 2014-15 and up to £3.9bn in 2016-17.[37] Recently, a correspondent commented that APD was "the most marvellous tax ever invented" as it cost very little for the government to administer, was largely paid for by foreign travellers who didn't vote in the UK and didn't seem to deter travel to a large extent.[38]

4.3. Regional arguments

In June 2011 Manchester Airports Group launched the 'Give us a break' campaign, whereby they encouraged passengers to sign petitions against any APD increases and to keep the rate lower for regional airports outside London. The Group argued that:

> *Passengers at regional airports tend to be more price sensitive than at the London airports, which can make regional airports less attractive to airlines. The Manchester Airports Group (MAG) has had a concern that additional price rises might discourage airlines from developing new routes from regional airports that businesses in the North require.*[39]

A number of regional airports (such as Manchester, Birmingham, Liverpool and Newcastle) signed an open letter to Mr Obsorne in response to the reform on APD consultation. They called for an abandonment of the current "one-size-fits-all" approach, which they say disproportionately affects airports outside London, as they are less able to attract new flights and keep existing routes. They also believe that the Government's commitment to constraining the growth of flight numbers from Heathrow and Gatwick can be better served by instating a regional policy on APD, while ensuring the retention of regional air services.[40]

An economic modelling study by Oxera Consulting commissioned by the Airport Operators' Association and Flybe found that a hypothetical zero-level of APD across all flights would lead to an estimated 16.3% increase in the aviation sector's contribution to the Northern Ireland economy (Gross Value Added). This was the most significant of the increases of all the regions identified. A similar modelling performed with a 20% decrease in APD at all regional airports (i.e. apart from London) found that each region would benefit, with Northern Ireland experiencing an estimated 2.09% change in the GVA contribution of the aviation sector.[41]

The March 2011 HM Treasury consultation document *'Reform of Air Passenger Duty'* noted:

> *Continuous improvement in air transport services at the UK's regional airports is […] vital for ensuring more balanced growth across all parts of the country. In this respect, the relatively low levels of congestion at the UK's regional airports, together with the excellent quality of the existing facilities and services on offer,*

[37] Office for Budget Responsibility, *Economic and Fiscal Outlook*, March 2012, p 101, Table 4.7
[38] BBC News, *Simon Calder: Air Passenger Duty is "impossible to avoid" (video)*, 1 April 2012
[39] Manchester Airport, *News release on 'Give us a break campaign'*, 13 June 2011 (accessed 29 March 2012)
[40] *Joint Open Letter to George Osborne*, 15 June 2011 (accessed 3 April 2012)
[41] Flybe, *op. cit*

> *should present opportunities for the future.*[42]

A means to ensure that regional airports receive increased investment in services is therefore essential to the UK Government's regional economic policy, and a reform of APD could provide a solution to this issue.

5. Devolution of Air Passenger Duty to Northern Ireland

Section 5 examines the course through which the proposed devolution of long haul rates of APD on direct flights from Northern Ireland has come about. Drawing on the HM Treasury consultation, the Northern Ireland Affairs Committee inquiry and the Committee for Finance and Personnel consultation, outlined below are some key issues surrounding the impact of APD and its proposed devolution. There is also an initial examination of the scope of powers to be devolved and the possibility of extending these powers.

5.1. Key UK Governmental developments

This subsection outlines key UK Governmental developments concerning the devolution of Air Passenger Duty in recent months:

- **23 March 2011**: During the Budget speech, the Chancellor announced that HM Treasury would be holding a consultation on the *Reform of APD*;
- **17 June 2011**: The consultation on *Reform of Air Passenger Duty* closes;
- **8 July 2011**: The Northern Ireland Affairs Committee's publishes its report on its short inquiry into *APD: Implications for Northern Ireland*;
- **27 September 2011**: The Chancellor announces that NI will have all direct long haul rates of APD held to the existing 'Band A' rate of duty;
- At the same time the Government announces its intention to devolve responsibility for the setting of direct long haul APD rates to Northern Ireland;
- **6 December 2011**: The UK Government publishes its response to the HM Treasury consultation;
- **21 February 2012**: A Written Ministerial Statement announces that the power of the Assembly to set direct long haul rates of APD will be included in the *Finance Bill 2012*;
- **26 March 2012**: The UK *Finance (No. 4) Bill* is introduced to Parliament with provisions for the continued deferment of NI long haul rates and for the devolution of the responsibility for the setting of these rates to Northern Ireland.

[42] HM Treasury, *Reform of APD consultation document*, March 2011, para 5.9

5.2. The HM Treasury consultation

The HM Treasury consultation, opened by the March 2011 Budget, sought views and comments on a proposed reform of Air Passenger Duty.[43]

The consultation document itself outlines the important of aviation to the growth of the UK economy, the environmental challenge of air transport, and the fair contribution of air travel towards public finances.[44] The document specifically outlines options for the reform and simplification of APD, while meeting the objectives of growth, fairness and environmental responsibility. Specifically, a two-band and a three-band regime are proposed to replace the current four-band regime (still with two separate classes of travel).[45]

The document also invited views on the case for devolving APD, mainly in response to the Calman Commission's recommendations of the devolution of fiscal powers to Scotland.[46]

The consultation was open until 17 June 2011. The December 2011 consultation response document referred to approximately 100 stakeholder responses made on the issue of devolution. Those arguing for devolution to Northern Ireland had highlighted the issue of the shared border with the Republic of Ireland, which had a lower air tax regime, threatening the direct long haul route between Belfast and New York. By this stage, however, the UK Government had already announced the deferment of long haul rates on flights from Northern Ireland and the launching of a process to "*devolve aspects of APD to the Northern Ireland Assembly […] as soon as possible*".[47]

5.3. APD Inquiry: The Northern Ireland Affairs Committee Report

The Northern Ireland Affairs Committee's *Second Report of Session 2010-12 (Air Passenger Duty: implications for Northern Ireland)*[48] looks at the effects of APD on Northern Ireland and makes a number of recommendations on this issue, including the devolution of APD to the Northern Ireland Assembly.

The Committee recognised the significance of APD for Northern Ireland, as it is geographically isolated from the UK mainland and is therefore heavily dependent on air (and ferry) transport links with no alternative options such as road and rail to GB and the Continent. Second, Northern Ireland shares a land border with the Republic of Ireland, where Air Travel Tax (ATT) is a comparatively insignificant rate of €3 (all flights) and is set to be abolished completely, making it hard for NI to compete for cheaper fares.

Evidence given to the Committee by Conor McAuliffe (Managing Director, Europe and Industry Affairs) and Bob Schumacher (Managing Director, Sales, UK and Ireland) from Continental Airlines[49] expressed the difficulties which the airline had with APD, specifically on

[43] http://www.hm-treasury.gov.uk/2011budget_airpassenger.htm (accessed 24 April 2012)
[44] HM Treasury, *Reform of air passenger duty: a consultation*, 23 March 2011
[45] *Ibid,* pp 21-22
[46] *Ibid,* p 24
[47] HM Treasury, *Reform of air passenger duty: responses to consultation*, December 2011, p 12
[48] Second Report of the Northern Ireland Affairs Committee, *Air passenger duty: implications for Northern Ireland* (HC 2010-12 1227), Annex
[49] Continental Airlines merged with, and changed its name to, United Airlines in November 2011

the Belfast to Newark route. As a result Continental was forced to absorb APD in Belfast in order to keep customers from switching to Dublin and keep the route open. Mr Schumacher commented that this was equal to “approximately seven weeks’ worth of revenue on that service” and that this was harmful to the long-term viability of a route that carries around 100,000 passengers annually. The Committee heard that the route was then being run at a loss, with Continental Airlines effectively subsuming the cost of APD (around £3.2 million) in the hope of future cyclical turnaround in profitability.[50]

The Committee, in its *First Report of Session 2010-12 (Corporation Tax in Northern Ireland)* commented that APD puts Northern Ireland at an economic disadvantage in retaining and attracting flight routes (especially international and cargo flight routes).[51] As a result of the disadvantage Northern Ireland faces in retaining air routes, there may be economic repercussions, the Committee heard: undermining of the aviation industry in NI; negatively affecting the number of visitors and the tourism sector; adversely impacting business travel and investment in the local economy.

5.3.1. Recommendations

In the *Second Report,* the Committee stated that it believed the option of devolving the power to set the rate of APD to the Northern Ireland Assembly would be a “*long, drawn-out legislative process, and a short-term solution is required*”. The Committee instead recommended a short-term solution and local measures to mitigate the effects of the tax in Northern Ireland. In the long-term, they recommended that a zero-rate of ADP apply to all flights departing Northern Ireland, and on direct flights to NI from Great Britain – essentially abolishing APD on all flights operating to and from NI.[52] The *Report* also linked the devolution of APD powers with the Committee’s previous recommendation (in the *First Report)* that the power to set the rate of Corporation Tax should be devolved.[53]

On 23 April 2012 the Northern Ireland Affairs Committee held a witness evidence session on the Air Transport Strategy for Northern Ireland in the Senate Chamber at Stormont. The value of the aviation to Northern Ireland was noted, as was the proposal to devolve the setting of APD rates on long-haul flights. The Chief Executives of Northern Ireland’s three main airports (Mr John Doran, MD of Belfast International; Mr Brian Ambrose, CE of George Best Belfast City Airport and Mr Albert Harrison, non-executive director of City of Derry Airport) each commented that APD should be fully scrapped, going beyond the proposals to devolve and lower the Band ‘B’, ‘C’ and ‘D’ rates.[54]

5.4. Committee for Finance and Personnel consultation

The Committee for Finance and Personnel has received many written submissions from stakeholders in relation to the legislative consent motion on the UK *Finance (No. 4) Bill*

[50] Second Report of the Northern Ireland Affairs Committee 2010-12, *Oral Evidence, 29 June 2011* (Q 153)
[51] First Report of the Northern Ireland Affairs Committee, *Corporation Tax in Northern Ireland* (HC 2010-12 558-I), para 128
[52] Second Report, paras 14, 17 and 26
[53] Second Report, para 15
[54] Belfast Telegraph, *Airport chiefs urge Stormont to fund air route and scrap levy on short-haul flights*, 24 April 2012

2012.[55] Nearly all stakeholders make the case for devolving APD, and support the proposal to devolve direct long haul rates of duty on flights from Northern Ireland. Some go further and make the case for devolving short haul rates of duty, and for scrapping APD altogether (this is outside the competence of the legislative consent motion).

Section 5.3 presents the arguments for devolving APD to Northern Ireland. Arguments in favour of the devolution of APD are made largely on an economic basis, but they also relate to fairness and to consumer choice and convenience. Some of these arguments fit in to the wider debate across the UK about the appropriateness of APD.

5.4.1. Fairness

As Northern Ireland is separated from the rest of the UK by sea, there is little choice for residents to travel to the mainland except by air, which for many outweighs the alternative ferry option in price and by convenience of proximity to final destination and shorter travelling times (e.g. it would take far longer to travel to London by overnight ferry to Liverpool with an onward rail or car journey, which would also be more expensive). Furthermore, there is no direct rail link to the European continental mainline such as the Channel Tunnel. An argument for the reduction or elimination of APD on the grounds of fairness to Northern Ireland passengers, who are effectively obliged to fly in order to go outside the country, can therefore be made.

For example, as there are much fewer options for NI air passengers to take a direct long haul flights out of NI, they must first fly to a hub airport, such as London Heathrow, before boarding a second flight. This incurs an extra charge of the lowest rate of APD (£13) on top of an air ticket, whereas passengers living on the GB mainland would be able to travel by car or train to Heathrow.

98.5% of flights from Northern Ireland are within Band ‘A’.[56] Civil Aviation Authority passenger statistics show that, on average, 17% of all UK departing flights are on domestic services within the UK. In comparison, 75% of NI passenger movements are on UK domestic services, demonstrating a much higher dependence on air travel.[57]

The Consumer Council argue that, given NI consumers’ high dependence on air travel:

> *APD, in its current structure, is unfair as it financially disadvantages NI consumers in comparison to their GB counterparts.*[58]

As the Consumer Council pointed out, England is to benefit from a £32.2 billion investment in a high-speed rail (HS2 Y) network, reducing dependence on domestic air transport, with wider economic benefits. Northern Ireland will not have access to this network, and will receive a limited benefit from this substantial investment of government money. The Consumer Council believes that exemption from all APD rates on flights to and from NI would

[55] Northern Ireland Assembly Committee for Finance and Personnel, *Devolution of Air Passenger Duty* (accessed 24 April 2012)
[56] Northern Ireland Assembly Official Report, *Committee for Finance and Personnel, 25 April 2011*
[57] Civil Aviation Authority passenger statistics, given in the Consumer Council, *written submission to the Committee for Finance and Personnel*, March 2012
[58] Consumer Council, *written submission to the Committee for Finance and Personnel*, March 2012

ensure equality of access for NI consumers.

5.4.2. Competition with the Republic of Ireland

The Association of British Travel Agents (ABTA) responded to the 2011 HM Treasury consultation, urging that Northern Ireland be treated as a “special case” due to the shared land border with the Republic of Ireland.[59] This had also been noted in the NI Affairs Committee *Second Report: Implications of APD for Northern Ireland.*[60]

The existence of a cheaper APD equivalent in the Republic of Ireland (Air Travel Tax, which is currently set at €3 and due to be abolished) has an economic impact on air services in Northern Ireland, due mainly to the shared land border and relatively short distances between Dublin Airport and Northern Ireland.

As an example, a flight to Newark airport (serving New York; the USA is a ‘Band B’ destination) from Belfast International would pay £65 in APD for a standard ticket, and £130 for a business or first class ticket, while the same destination from Dublin Airport would incur only €3 Air Travel Tax. On flights to destinations further away (in Bands ‘C’ and ‘D’) this difference would be even greater. The disparity in cost could be considered enough to encourage a journey by car or bus to Dublin Airport from Belfast, a situation which is magnified when multiple tickets (such as for a family of five) are being purchased, even when on short haul flights (e.g. five standard tickets to Spain would incur £13x5=£50 in APD).

In its written submission to the Committee for Finance and Personnel Belfast International Airport said (referring to the Chancellor’s decision to hold the Band ‘B’ rate of APD to the Band ‘A’ equivalent in Northern Ireland):

> *“Whilst the [recent APD] reduction safeguards the Belfast-New York service with United Airlines, it still leaves airline operators at a distinct disadvantage to their Dublin counterparts where the APD equivalent is 3 euro per passenger. This figure was reduced from 10 euro because the Republic of Ireland Government said it harmed tourism and hampered business. This enables pricing to be more keenly set in Dublin with the result that business is lost to the Northern Ireland economy.”*[61]

The Northern Ireland air and tourist industry is therefore at an effective competitive disadvantage due to the existence of higher rates of APD. The resultant decrease in demand at NI airports leads to a lower number of air travel routes, reducing consumer choice and convenience, regardless of the other economic consequences.[62]

5.4.3. Economic consequences

In 2009 the ‘Air Transport’ sector contributed Gross Value Added (GVA) of around £127m to

[59] ABTA, *written submission to the Committee for Finance and Personnel*, 16 April 2012
[60] Second Report of the Northern Ireland Affairs Committee 2010-12, para 25
[61] Belfast International Airport, *written submission to the Committee for Finance and Personnel*, 13 April 2012
[62] Consumer Council, *op. cit*.

the Northern Ireland economy[63] along with directly supporting 704 jobs and an additional 914 jobs down the production line.[64] This is a sizeable contribution and the new business attracted through a locally decided lowering of APD rates would very likely have a positive impact on all of these figures.

APD also has further economic consequences which reach beyond the direct impact on the business of airports and airline operators. First, as discussed above, APD puts Northern Ireland at a competitive disadvantage in establishing and retaining direct routes beyond the rest of the United Kingdom. Second, APD increases the cost of travel on return flights to Northern Ireland, no matter which route is taken. This has the impact of reducing the total number of flights taken here, which adversely impacts the tourism industry as well as the level of foreign direct investment. As the cost of travel to Northern Ireland is held at an artificially high level alongside the diminished number of flights options this has a severe consequence for the local economy due to the increased costs facing both businesses and pleasure travellers. This decreases the level of foreign money available to invest in Northern Ireland and affects its attractiveness as a tourist and commercial destination.

Belfast International Airport commented that the benefit to the NI economy of the flight to and from New York has been worth in excess of £100 million over 7 years. Compared to the predicted £5 million cost of APD devolution the economic benefit argument still remains. Furthermore, if a zero-rate of APD brings more long haul operations to Northern Ireland this benefit could be multiplied many times.

5.4.4. Tourism

According to the Deloitte report *The Economic Contribution of the Visitor Economy: UK and the Nations* (provided by ABTA) 30,000 jobs in Northern Ireland depend on the tourism industry, relative to around 3% of all employment. Approximately 20% of all business units in Northern Ireland are part of the “visitor economy”. Both of these rates are lower relative to each of the other UK nations, demonstrating that there is perhaps spare capacity and opportunity for growing the visitor economy in Northern Ireland. This is given further validation by the recent strong growth in the tourism economy, as evidenced in the same report. NI has had strong compound growth in staying visits of 3.3%, and average spend per visit of 2.8% over the last decade, higher than any other nation.[65] On Northern Ireland, the report concludes:

> *“The Visitor Economy reached £1.5 billion in 2009, equating to 4.9 per cent of Northern Ireland’s GDP. In total the Visitor Economy in Northern Ireland supported 4.7 per cent of total employment [in 2009].”*[66]

This figure of 4.9% GDP compares to 8.6% GDP in England, 10.4% GDP in Scotland and 13.3% GDP in Wales. Northern Ireland is clearly deficient on the proportion of the economy which is supported by tourism.

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[63] Office for National Statistics, *Annual Business Survey 2009, Regional Data: Division by Region*, (see GVA of SIC 51 for NI)
[64] Department of Enterprise, Trade and Investment, *NI Census of Employment 2009: Employee Jobs*, (see SICs 51 & 5223)
[65] Deloitte (and Oxford Economics), *Economic Contribution of the Visitor Economy*, June 2010, pp 18-19, 25-26, 30-31
[66] *Ibid,* p 45

The Federation of Small Businesses (FSB) point out that tourists rarely travel more than 100km beyond their point of arrival. As there are few opportunities for foreign travellers to fly directly to Northern Ireland (including a lack of any flights from Scandinavia, Germany and countries outside Europe), most visitors to Ireland will fly to Dublin Airport, and may decide against travelling north of the border into Northern Ireland. This shows a clear disadvantage to the potential of the tourism sector in NI.[67] The FSB argue that, though devolution of APD at any level would lead to an equivalent cut in the block grant, this would be immediately balanced by the economic benefits.[68]

Furthermore, the Deloitte report noted that "*constraints on the development of aviation infrastructure*" was a particular threat to Northern Ireland.[69]

5.4.5. Revenue

When conducting its short inquiry into the implications of APD for NI, the Northern Ireland Affairs Committee heard that Continental/United Airlines pay around £3.2 million to the Treasury in revenue from APD every year.[70]

HMRC estimate that the devolution of APD will result in between approximately 37,500-75,000 passengers flying in Bands 'B', 'C' and 'D' departing Northern Ireland in 2012-13.[71] To this end, a maximum figure of £5 million has been given as the forfeit from the NI block grant in order to devolve direct long haul rates of APD.[72]

According to Ms Justine Greening (Economic Secretary to the Treasury) Northern Ireland flights will contribute £60 million to the exchequer across all bands of APD.[73] This amounts to 0.021% of the £2.9bn UK-wide total.[74] Ms Greening mentioned that 'State Aid' issues may arise, meaning that this figure will need to be deduced from the NI block grant.[75] In order to fully devolve APD powers, the cost to the Northern Ireland Executive budget may be around £60 million.[76]

Issue for consideration: if the Committee wishes to pursue the devolution of powers over the short haul rate of duty in future, it will need to consider the potential reduction of £60 million in the NI block grant.

5.5. The Department of Finance and Personnel's position

DFP's position is outlined in their submission to the HM Treasury consultation *Reform of Air*

[67] Northern Ireland Assembly Official Report, *Committee for Finance and Personnel, 25 April 2011*
[68] Federation of Small Businesses, *written submission to the Committee for Finance and Personnel*, April 2012
[69] Deloitte (2010), p 101 (Annex, Northern Ireland dashboard)
[70] Second Report of the Northern Ireland Affairs Committee 2010-12, *Oral Evidence, 29 June 2011* (Q 172)
[71] HMRC, *APD: Devolution of rates to Northern Ireland*, 21 February 2012. "Of an estimated 3.75 million passengers departing NI, between 1 and 2 per cent will travel in bands 'B', 'C' and 'D'"
[72] Two classes of travel of either £65 and £130: the lowest end figure is £2,437,500; the highest end figure £9,750,000
[73] Second Report of the Northern Ireland Affairs Committee 2010-12, *Oral Evidence, 29 June 2011* (Q 277)
[74] HM Treasury, *Budget 2012*, Table D.3, p 106 gives £2.9bn as the forecast receipt from APD in 2012-13
[75] Second Report of the Northern Ireland Affairs Committee 2010-12, *Oral Evidence, 29 June 2011* (Q 281)
[76] The Irish News, *End to air duty 'may cost £60m'*, 24 April 2012

Passenger Duty.[77] In it they outline the importance of direct long haul routes to Northern Ireland to the local aviation, tourism and wider local economy, in addition to the particular significance of attracting foreign direct investment.

They highlight the current importance of the New York-Belfast route, which many Invest NI FDI clients, including the New York Stock Exchange (NYSE), "*expressly stated that their presence in NI was only possible of the basis of*". Attracting a greater volume of FDI and resultant economic growth, DFP say, can be possible through greater travel links with business and capital locations.

DFP also comment that the current UK rates of APD "*are now prohibitively high relative to similar taxes in other EU countries*", placing NI at a unique disadvantage when competing with the Republic of Ireland's very low (and soon to be zero) rate of air tax.

The conclusions of the DFP's submission sum their position:

- All business sectors in NI are adversely affected by APD, in particular tourism and the ability to attract foreign direct investment;
- It is an unfair tax as it is particularly severe in NI given the lack of alternative travel options to the rest of the UK;
- Lower tax arrangements in the Republic of Ireland put NI at a particular disadvantage in attracting tourism and business and in keeping air travel routes;
- APD damages and constrains the Executive's desire to rebalance the NI economy;
- If APD is to be kept it should have a single rate for all flights which should be equal to, or lower than, the current 'Band A' rate;
- DFP would wish to consider the proposal to devolve APD responsibility.

5.6. The scope of the devolved powers

This subsection examines the extent to which the Northern Ireland Assembly will have power to vary APD, i.e. what the Assembly can and cannot do as regards the duty. It also discusses key issues surrounding devolution in relation to legislative changes, and the potential for extending APD powers.

5.6.1. What the Bill does and does not allow

Schedule 23 of the *Finance (No. 4) Bill 2012* (as discussed in Section 3 of this paper) limits the scope of the devolved powers in two main aspects:

- The Northern Ireland Assembly will have the power to set the rates of 'Band B', 'Band C' and 'Band D' flights from Northern Ireland, though it may set these to zero for either class of travel. The Assembly will not have the power to alter the structure of Air Passenger Duty and must keep to the current banding structure as outline in

[77] Department for Finance and Personnel, *Response to HM Treasury Reform of APD Consultation*, 16 June 2011

the *Finance Act 1994*.

- The Northern Ireland Assembly will not have the power to set the rate of the shortest flights, i.e. 'Band A', in either class. Direct flights from Northern Ireland to these destinations will pay the same rates as those set by the UK Government.
- Flights to Northern Ireland from other UK airports will pay the same rate of duty as any other UK flight. The Assembly will not have power over rates on these flights.

5.6.2. Legislative competence

Paragraph 9 of Schedule 23 to the *Finance Bill 2012* inserts a new Section 30A into the 1994 Act. Draft subparagraph (11) effectively disapplies part of the *Northern Ireland Act 1998*:

> *"None of the following applies to any matter in respect of which this section authorises provision to be made by an Act of the Northern Ireland Assembly—*
>
> *(a) any paragraph of Schedule 2 or 3 to the Northern Ireland Act 1998 (excepted and reserved matters);*
>
> *(b) section 63 of that Act (financial acts of the Assembly)."*[78]

This means that for the purposes of direct long haul flights from NI, setting APD rates on direct long haul flights is neither a reserved nor an excepted matter.[79] In turn this means that the NIA will be competent to legislate for that specific purpose.

Section 63 of the *Northern Ireland Act 1998* relates to how financial acts of the Assembly are passed, i.e. they are made by the Minister of Finance and Personnel and passed by cross-community support. Though section 63 is disapplied in the case of APD, the provisions under schedule 23, paragraph 9(12-14) of the *Finance (No. 4) Bill* reinsert almost identical criteria in relation to the future setting of APD rates by the Assembly. Though this has a nil effect it is unclear why section 63 has been disapplied. The reason may be entirely technical.

Issue for consideration: is there a reason why section 63 of the North*ern Ireland Act 1998* will not apply in the setting of rates of APD, once devolved to the NI Assembly?

5.6.3. Extending the powers: The Northern Ireland Act 1998

The possibility still exists for consideration of whether to further extend the devolved powers to include setting the rates of Band 'A' flights departing Northern Ireland, as they apply to the other bands, though this is not legislated for under the *Finance Bill*.

In response to a question about the widening of the scope of the powers to include Band 'A', an official from the Department of Finance and Personnel's strategic policy division, commented:

> *"To devolve greater powers, it was considered that we may need to have an*

[78] *Finance Bill 2012*, sch 23, para 9, subpara (11)
[79] *Northern Ireland Act 1998*, s 63, sch 2, sch 3

> *amendment to the Northern Ireland Act 1998 rather than be able to deliver a reduction solely through the Finance Bill 2012. No parliamentary time for an amendment to the Northern Ireland Act has been scheduled before the end of 2013. Ministers consider that period too long to take the action that we want to take on direct long-haul flights.'*[80]

This raises the issue of how the current legislative proposal, contained in the *Finance Bill,* can be devolved *without* amending the *NI Act 1998*, when the proposal devolves limited rate-setting powers?

DFP confirmed that HM Treasury had taken legal advice, but by convention legal advice is not shared.[81] DFP has also sought legal advice – but it similarly is not shared. However DFP stated that, in effect, a *significant* change to devolution arrangements would have to be made through amendment to the *NI Act 1998,* by a constitutional bill in Westminster rather than a finance bill. The current proposal, therefore, is not considered to be a significant change to devolution arrangements.

Issue for consideration: as the proposed devolution does not include the power to alter the structure of Air Passenger Duty, and instead devolves the power to alter the rates of Bands 'B', 'C' and 'D', why can the power to alter Band 'A' rates not simply be extended? Does this amount to a significant change necessitating amendment to the *NI Act 1998*, and if so, why? The Committee may wish to seek legal advice on this issue, as well as the issue of amending the *NI Act 1998*.

5.6.4. Exemption vs. devolution

The PricewaterhouseCooper (PwC) report *Devolving Air Passenger Duty* makes the recommendation of either:

- "*Scrapping APD completely as is the case in the Scottish Highlands and Islands, based on the peripheral nature of the region and the discriminatory nature of a largely unavoidable tax on necessary travel; or*
- *Devolving the powers to vary (or scrap entirely) APD to the Northern Ireland Executive*."[82]

First, it is important to note that PwC favours zero-rate APD across all 'bands'. Second, there is a difference between the first example – that of exemption – and the second – devolution, which is proposed (to a more limited extent) by the *Finance (No. 4) Bill 2012*.

The Scottish Highlands and Islands are exempt from APD applying to flights departing from their airports (but not on flights returning from other parts of the UK). This is due to a section in the *Finance Act 1994* (as amended by the *Finance Act 2000*) exempting airports in areas with a population density less than 12.5 persons per square kilometre. Though the exemption is effected through the means of population density criteria, the reason for the exception is

[80] Northern Ireland Assembly Official Report, *Committee for Finance and Personnel, 14 March 2012*

[81] DFP email to RaISe

[82] PwC (NI), *Helping economic take off: Devolving Air Passenger Duty*, 16 December 2011

thought to be the peripherality of the region, high costs of service provision and dependency of the highlanders and islanders upon air travel.[83] The same arguments could potentially be made in Northern Ireland's case.

As the provisions in the *Finance Act 1994/2000* were made in Westminster, and did not involve devolution of powers to the Scottish Government, there is no forfeiture from Scotland's block grant of the equivalent shortfall in revenue.

Issues for consideration: if a similar exception was made by the UK Government for Northern Ireland, would an amendment be required to the *Northern Ireland Act 1998?* Would there be a loss to the block grant? As different factors may apply to Northern Ireland as compared to the Scottish Highlands and Islands, would issues surrounding EU legislation governing State Aid arise?

Note: as was explained in subsection 5.6.3 of this paper, the full devolution of APD *may* require an amendment to the *NI Act 1998*. Devolution also requires an equivalent loss in the block grant made to Northern Ireland through the Barnett Formula.

6. Devolution of APD to Scotland and Wales

The Scottish Isles and Highlands have a number of airports to which flights from them are exempt from paying Air Passenger Duty, though flights to these airports from other areas in the UK are still chargeable. The areas under exemption were defined by Order in 2001 under powers granted to the Secretary of State by an amendment to the 1994 Act made in the *Finance Act 2000*. Flights from airports in regions with a population density of less than 12.5 persons per square kilometre are also exempt from APD.[84]

It is important to note that, as this functions as an exemption, the arrangement does not incur a loss to the Scottish Government's block grant; rather, it is a loss to HM Treasury revenue. The Consumer Council believe that this sets a precedent for flexible application of the short haul rate of APD with respect to Northern Ireland as a result of the region's peripherality.[85]

Issue for consideration: would it be possible for Northern Ireland to become exempt from short haul rates of APD, on reasons of dependence and peripherality?

APD revenue from all flights departing airports in Scotland 2010-11 was estimated at £183 million, having gone up from £94 million in 2006-07.[86] In June 2009 the Commission on Scottish Devolution (known as the Calman Commission) recommended a devolution of Air Passenger Duty (amongst other excise duties), with a corresponding reduction in the block grant, to the Scottish Government. This was on the basis of improving the financial

[83] Scottish Council for Development and Industry, *Reform of Air Passenger Duty*, June 2011

[84] *The Finance Act 2000*, s 19 inserted new sections 4B, 4C and 4D into the Finance Act 1994, s 31, giving the Secretary of State power to exempt regions from being chargeable for the purposes of APD on flights from their airports. The subsequent Order, *The Air Passenger Duty (Designated Region of the United Kingdom) Order 2001*, SI 2008/808 made provision for exempting the Scottish Highlands and Islands. See HMRC's *Guide to Air Passenger Duty* for the airports affected by this.

[85] Consumer Council, written submission to the Committee for Finance and Personnel, March 2012

[86] Office for National Statistics, *Government Expenditure and Revenue Scotland 2010-11*, 7 March 2012, table 3.1

accountability to the Scottish Government to its electorate.[87]

An Early Day Motion (EDM), tabled on 12 October 2011 by Mr Angus MacNeil MP and sponsored by other Scottish MPs, called for the devolution of APD to the Scottish Government. It argued that the power to lower APD would benefit the Scottish economy and create a more level playing field for air operators in Scotland to compete with those to the south of their border.[88] A similar EDM on 17 May 2011 had called for a repeal of the proposed extension of APD to helicopters, which could adversely affect the North Sea offshore oil industry. The Motion also called for the full-scale devolution of APD to Scotland.[89]

The Scottish Minister for Transport and Infrastructure, Mr Keith Brown, has called for APD to be fully devolved to Scotland in order to give Scottish airports a competitive edge in retaining and attracting flight routes.[90]

The decision by the UK Government to devolve direct long haul rates of APD to Northern Ireland but not to Scotland caused considerable consternation among Scottish airports and politicians. Those who desired similar treatment to that afforded to Northern Ireland cited the importance of tourism to Scotland and its contribution to Treasury revenue and the regional difficulties faced by airline operators at Scottish airports.[91]

The Scotland Bill, currently under consideration of Lords amendments in the House of Commons, while making no specific provision for the devolution of APD, paves the way for devolution of any tax rate under clause 80B.[92]

A number of Scottish MPs and the Welsh MP Mr Jonathan Edwards (Plaid Cymru) tabled amendments to the *Finance (No. 4) Bill 2012,* which would effectively apply the same principle of devolution of direct long haul rates of APD to Scotland and Wales, as to Northern Ireland. These amendments were either not called of defeated on vote.[93]

7. Air taxation in other countries

Section 7 examines excise duties in other countries similar in form to APD. In particular, the Republic of Ireland's Air Travel Tax (ATT) is closely examined, as it is the equivalent duty that flights from Northern Ireland have to compete with due to the shared land border.

7.1. Republic of Ireland

Until March 2011 the Republic of Ireland had a two-tier Air Travel Tax, introduced in the 2009 Budget. Flights travelled to airports within 300km (186 miles) of Dublin were charged a rate

[87] Commission on Scottish Devolution, *Serving Scotland Better: Scotland and the United Kingdom in the 21st Century*, June 2009, p 10 (recommendation 3.2), p 99, p102, pp 111-13, p 179
[88] Early Day Motion 2235, 12 October 2011
[89] Early Day Motion 1818, 17 May 2011
[90] Scottish Government, *News Release on Air Passenger Duty*, 4 March 2011
[91] BBC News, *Scottish airports disappointed by tax decision*, 6 December 2011
[92] Scotland HC Bill (2010-11), [HL Bill 138] cl 80B Other excise duties such as UK stamp duty land tax and UK landfill tax are to be discontinued in Scotland under the bill as it currently stands, cc 3-4
[93] Committee of the Whole House, *Proceedings on the Finance (No. 4) Bill 2012 on 18 April 2012*, pp 1209-1214

of €2, and all other flights €10, per passenger departing, to be paid for by the airline.[94]

With the exception of a few airports on the Western side of Great Britain, the Irish domestic market benefitted from the lower €2 rate. The European Commission challenged the legality of the two-tier system, claiming that the higher rate would disadvantage travellers from other Member States who had to pay more to (re)enter their own country. European Law states that access to fares for air services should not discriminate on the basis of the nationality or residency of customers.[95]

As of 1 March 2011 a new rate of €3 applies on all flights.[96] Air Travel Tax is set to be completely abolished by the Fine Gael/Labour Government, subject to further talks with airlines.[97] The European Commission withdrew its infringement procedure at the behest of this adjustment to a single rate on all flights.[98]

7.2. Other European countries

The only other European Union countries to currently impose air travel excise duty are Germany, Austria and France. Others have recently abolished air passenger taxes, such as Sweden, Denmark and Malta.

Notably, the Netherlands introduced an air passenger tax for passengers departing from Dutch airports on 1 July 2008. This was subsequently set to €0 on 1 July 2009 and completely abolished by the Government in 2010. The reason for this swift change in policy was due to the undesirable effect the tax had on the air travel industry in Holland. Passengers, put off by the increase in fees (€11.25 to EU destinations and €45 for all other international destinations) elected to travel to land-bordering countries, where no air passenger duty was in place, and depart from their airports. This led to a massive drop in passenger numbers departing from Dutch airports, partly exacerbated by the global financial crisis but confirmed by surveys at German and Belgian airports. The Dutch Ministry of Finance had initially predicted a €350m intake in tax revenues; a later study estimated that imposing the tax cost the Dutch economy €1.3bn.

Despite the adverse experience of the Netherlands, from January 2011 the neighbouring German Government decided to impose air passenger tax on all departing flights (€8 short haul, €25 medium-haul and €45 long haul). Though this is charged to the airlines it is likely that the cost will be passed on to consumers through ticket price increases.[99]

The Spanish Government recently announced, in its draft budget, that it intends to increase airport fees at the state-owned AENA network of airports by an average of 10.5%. The European Commission is investigating if this move breaks EU directives relating to airport

[94] Office of the Revenue Commissioners, *Guide to Air Travel Tax* (accessed 3 April 2012)

[95] Council Regulation (EC) 1008/2008 of 24 September 2008 on common rules for the operation of air services in the Community [2008] OJ L293/3 (Chapter IV, Articles 22-24)

[96] Department of Finance (RoI), *Summary of Budget 2011 Measures – Policy Changes*, 7 December 2010, p B.10

[97] *Financial Statement of the Minister for Finance*, Michael Noonan TD, 6 December 2011 and Irish Times, *A rise in passengers could see flight tax abolished*, 20 February 2012 (both accessed 23 April 2012)

[98] European Commission, *Press release IP/11/734: Irish Air Travel Tax*, 16 June 2011 (accessed 23 April 2012)

[99] German Federal Ministry of Finance, *Aviation Tax*, 7 September 2010 (accessed 3 April 2012)

regulation.[100] In response to this, Ryanair immediately announced that any increase in charges would be passed on to customers, even if they had already bought their tickets.[101] This effectively amounts to a taxation increase similar in nature to APD: a charge paid on passengers departing, payable by the airline, but passed on to their customers.

8. Conclusion

- Paragraphs 7-15 of schedule 23 of the *Finance (No. 4) Bill 2012* devolves to the Northern Ireland Assembly the power to alter the rates of Air Passenger Duty in Bands 'B', 'C' and 'D' (long haul) flights direct from Northern Ireland, in either class of travel, including the ability to set these to a rate of £0.
- As this is the devolution of tax-setting powers, and not an exemption from APD, there will be a reduction in the block grant of an estimated maximum of £5 million, in order to ensure compliance with EU State Aid rules.
- The Northern Ireland Assembly will not have the power to change the Band 'A' rates of APD in either class of travel, nor will it have the power to alter the structure of APD, under the provisions of the *Finance Bill*.
- Long haul rates of duty on flights from Northern Ireland have been held at the UK short haul rate of duty since 1 November 2011, in order to ensure the continuation of the sole long haul flight from NI.

Issues for consideration:

- The Committee may wish to consider at what rate(s) it wishes to set long haul rates of duty, though the ultimate decision will be made by Act of the Assembly, as introduced by the Minister of Finance and Personnel.
- The Committee may wish to consider whether it will pursue the devolution of short haul rates of duty in the future:
    - A provision for this option is not contained in the *Finance (No. 4) Bill 2012.*
    - This option may require an amendment to the *Northern Ireland Act 1998* in Westminster, as it involves the full devolution of a UK-wide excise duty.
    - The cost of this option will be in the region of approximately £60 million.
    - Legal advice on issues surrounding the devolution of tax powers in accordance with the *Northern Ireland Act*, and the issue of EU State Aid rules may be beneficial to the Committee's future consideration of APD.

[100] Tumbit, European Commission may investigate Spain airport fee hike, 19 April 2012
[101] The Independent, Ryanair threatens backdated fare increase, 19 April 2012