

DFP RESPONSE TO HMT REFORM OF AIR PASSENGER DUTY CONSULTATION

Summary

The Department of Finance and Personnel (DFP) Northern Ireland, while accepting the Government's requirement for revenue, believes that Air Passenger Duty (APD) is a tax that no longer meets the basic requirements of being fair to everyone, that is structured simply, and that does not unduly impede consumers, business or industry. Aviation makes a significant contribution to the Northern Ireland economy. The introduction of the EU Emission Trading Scheme has removed the original rationale for the duty to reduce emissions and help address climate change. The current and proposed rates of APD (particularly beyond Band A) are prohibitively high relative to others. All business sectors in Northern Ireland are adversely affected but it is particularly damaging for our tourism sector and to our ability to attract Foreign Direct Investment (FDI). APD is unfair as its impact is particularly severe in Northern Ireland given the lack of alternative transport options to other parts of the UK and because of the different tax arrangements and therefore the competition from the Republic of Ireland for both domestic and international air traffic. It damages and constrains the Government's and the Executive's wider effort to rebalance our economy. The continued application of this tax should be reviewed. If APD is retained it should have a single rate no matter the distance flown and that this rate should be akin, or lower, to that currently applied to Band A. The DFP would wish to give more consideration to the proposal to devolve APD and to have further discussions with the Government on the possible devolution of the duty.

Introduction

1. The Department of Finance and Personnel (DFP) Northern Ireland welcomes this opportunity to respond to the Government's consultation on the reform of Air Passenger Duty (APD). As a starting point we agree that the Government has a basic requirement for revenue within a tax regime that is fair to everyone and that subject to these basic requirements, the taxation of air transport should be structured as simply and efficiently as possible so that taxes do not unduly impede consumers, business or industry. We also accept the need to reduce emissions across all parts of the economy.

Aviation's contribution to the Northern Ireland economy

2. In 2009, the 'Air Transport' sector¹ contributed around £96m to the Northern Ireland (NI) economy, directly supporting 704 employee jobs², with an additional 914 employee jobs attributable to 'service activities incidental to air transportation'. The aviation industry makes a much broader contribution to the local economy in that it connects Northern Ireland with the rest of the UK and other international destinations. This facilitates local firms in doing business with customers outside the region, provides the transport links that are so important to Foreign Direct Investors, and allows tourists to visit NI.
3. Between 2000 and 2010, passenger numbers at NI airports have increased by 55% from 4.5 million in 2000 to around 7.1 million in 2010³. In 2010 passengers flying to and from Band A destinations accounted for 98.5% of total passengers, with Band B destinations accounting for the remaining 1.5%.
4. This connectivity is vital for the local tourism industry in NI and in attracting Foreign Direct Investment (FDI) to the region – both key to growing and rebalancing the NI economy.
5. In NI around 53,000 jobs (8% of total employee jobs) are directly dependent on tourism. In 2009, there was 1.918m out of state visitors to NI generating £337m⁴. The Department of Enterprise, Trade and Investment (DETI) has set ambitious targets to increase the contribution the tourism sector makes to the local economy (tourism's direct contribution of 2.1% of GDP is estimated to be below that of England, 2.9%, Scotland, 4.9% and Wales, 5.8%)⁵. Maintaining and developing air services will be key in this regard, given that a significant proportion of tourist visitors tend to confine their activities to an area in close proximity to their arrival airport. Therefore it is vital that tourists from as many

¹ Annual Business Enquiry, Country and Government Office Region by SIC, 2008

² NI Census of Employment 2009, Employee Jobs

³ NI Transport Statistics 2009/10

⁴ NITB, Tourism Facts 2009

⁵ The economic contribution of the Visitor Economy: UK and the nations, NITB, June 2010

destinations possible are able to travel directly to NI airports as opposed to an airport in the Republic of Ireland (RoI).

6. Between 2003 and 2010, the level of FDI in NI has increased by 42%⁶ from £380m in 2003 to £541m in 2010⁷. Over the same period, the number of additional jobs created in NI through this inward investment has increased from 1,687 in 2003 to 4,190 in 2010, an increase of 148%⁸. This has been a key driver of NI's economic growth over the last decade, and attracting a greater volume of high value added FDI will be an important priority in the new Economic Strategy being developed by the NI Executive.
7. Again, international connectivity and regular air services are important in this regard. Indeed, many Invest NI FDI clients, including the New York Stock Exchange (NYSE), have expressly stated that their presence in NI was only possible on the basis that direct air access to the US Eastern Seaboard capital markets was readily available. This highlights specifically the importance of the United Continental Airlines Belfast/New York service (our only direct link to North America), which provides a vital and strategic access point not just for indigenous companies seeking to trade with North America, but it also provides a very important gateway for inward investors seeking to establish or expand business operations in NI.
8. NI is heavily reliant upon air links to access Great Britain (GB) and other markets as the region has no direct rail links with the rest of GB and a limited ferry infrastructure (there are only currently 5 sea routes/ferry crossings available). Therefore air links are vital for tourism, local businesses and in attracting FDI to NI. This is particularly the case as we seek to rebalance the NI economy, which is a shared objective of the both the NI Executive and the Government.

⁶ Includes both estimated investment and actual investment

⁷ Invest NI, FDI Intelligence database

⁸ Includes both estimated job creation and actual job creation

Rationale for APD – Emissions and Climate Change

9. The DFP agrees with the Government that the EU Emission Trading Scheme (ETS) should be the principal mechanism for delivering on the goals for reducing the global CO2 emissions impact of aviation. This removes the original rationale for the scheme and means that the primary purpose of the duty is now as a revenue raising measure.

Impact of APD on NI (Question 6.2 (d))

10. APD rates have risen sharply in recent years and are now prohibitively high relative to similar taxes in other EU countries, particularly the RoI. While rates are currently frozen, the HM Treasury Budget Report 2011 (Table C3: Current receipts: OBR forecast) records the total revenue from APD rising from £2.2 billion in 2010/11 to £3.6 billion in 2015/16. Based on APD receipts from NI in 2009, HM Treasury raised between £45m and £55m from passengers departing airports in NI.
11. The ROI also levies an aviation duty (APDT) but the gap between the rates applied by the UK and the ROI has widened significantly in the last two years. In March 2011, the Irish Government reduced the rate of APDT from €10 to €3. In May 2011 the Irish Government went further, announcing that this rate would be reduced to zero subject to airlines increasing their passenger numbers. The DFP note that this measure is part of the Irish Government's recovery plan supported by the UK Government as part of the arrangements put in place in relation to the UK's recent bilateral loan to Ireland.
12. The differences in rates of APD places NI at a significant, and unique, disadvantage in attracting and retaining air services because of competitive pressure from the RoI and Dublin airport which is only 100 miles from Belfast. The impact of this has become even more acute following the previous Irish Government's decision to reduce / remove their equivalent tax.

13. These challenges are quite unique in the UK given our land border with the RoI. We are also concerned that NI's competitive position could be eroded further if APD is increased in the future.
14. The impact of APD in NI has been clearly very negative. It impacts on all business sectors but has a particular impact on Band B long haul flights which are important for FDI and tourism. This has been reflected in the case of our single current direct Band B operator – United/Continental airlines - which operates a single route from NI to the US. To be viable these flights must be competitive in terms of price with routes from Dublin. At present the Airline has to cover the difference in APD between what is charged in NI and the rate in ROI which is significantly lower. The difference is too great to make up and United/Continental Airlines cite APD as a key reason why the flight between Belfast and New York is not profitable. The Airline has made strong representations that a continuation of the current rate of APD in Band B is likely to result in a withdrawal of the service.
15. We are also concerned that the current rate of APD in Band B might act as a deterrent for other potential operators.

Conclusion of future of APD

16. The combination of relatively high rates of APD, our land border with the RoI, and the lack of alternative transport choices means that this duty has a disproportionate and therefore unfair impact on NI. It does not therefore meet the basic requirements of the Government's objectives for taxation of this sector. The negative and disproportionate economic impact of APD in NI is directly contrary to the Government's and the Executive's stated aims of rebalancing the NI economy by growing the private sector here. Its levels - particularly beyond Band A - have become disproportionately high at a time when those other EU countries that have this type of duty are recognising its negative impacts and reducing or removing it altogether. Given that the original rationale for the duty no longer applies, that it is unfair, and that it is damaging for the economy, the DFP believe that it should be discontinued or significantly

reduced. At a minimum the DFP believe that the Government must take immediate action to address the competitive disadvantage NI is facing to prevent further damage to the economy. The DFP notes that the Scottish Highlands and Islands have a partial exemption on APD.

Devolution of APD (question 6.2 (e))

17. The DFP note the Government wishes to better understand the possible case for devolving APD powers to NI but that no details on the possible mechanisms for this are included. The DFP would wish to consider and explore this option further with the Government to determine whether a mutually acceptable mechanism could be found. The delivery of other public services should not have to be damaged to enable us to address the unfair and damaging elements of this tax. In terms of any possible devolution, there are a range of complex issues that would need to be considered. These issues and the costs, benefits and associated risks would need to be considered to assess whether devolution was in the best interests of NI.

Response to Consultation Questions on Business Jets (6.2 (a)), Options for Bands (6.2(b)), and Class distinctions for APD (6.2(c))

18. We have no comments to make on the proposal to extend APD to business jets (question 6.2 (a)) and on how the current class distinction affects the market (question 6.2 (c)) other than to say the duty would be simpler without class distinctions.
19. On the proposed options for two bands of APD (question 6.2 (b)) we believe that both options would have a negative impact on NI, as both retain a banding structure and suggest rates of APD for Band B of £60 plus. This represents a continuation of the current APD pricing structure and would continue to leave NI at a competitive disadvantage vis-a-vis the ROI. When APD was an environmental measure different rates for longer distances could make sense. As APD is now to be solely a revenue earning tax this no longer applies and we would suggest that, if APD is retained, one rate be applied to APD, no matter

the distance flown, and that this rate be akin, or lower, to that currently applied to Band A.

Conclusion

20. The DFP, while accepting the Government's requirement for revenue, believes that all business sectors in NI are adversely affected by APD but that it is particularly damaging for our tourism sector and to our ability to attract FDI. It is an unfair tax as its impact is particularly severe in NI given the lack of alternative transport options to other parts of the UK and because of the different tax arrangements in the RoI for both domestic and international air traffic. It damages and constrains the Government's and the Executive's wider effort to rebalance our economy. The continued application of this tax should be reviewed. Active consideration should be given to addressing the particular impact on NI. If APD is retained it should have a single rate no matter the distance flown and that this rate should be akin, or lower, to that currently applied to Band A. The DFP would wish to consider further the proposal to devolve APD responsibility and to have further discussions with the Government on this possibility.

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