

Item:

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Report to Partnership Meeting of 4 April 2008

AVIATION DUTY CONSULTATION RESPONSE

SUMMARY

The Report details the proposed response from HITRANS to Her Majesty's Treasury Consultation into the replacement for Air Passenger Duty in the UK. Responses to the consultation are invited by 24 April 2008.

RECOMMENDATIONS

The Partnership is asked to

1. approve the submission of the enclosed Draft as HITRANS response to Her Majesty's Treasury Consultation into future Aviation Taxation

DETAIL

HITRANS should welcome the initiative by Her Majesty's Treasury to consider alternative ways of taxing the aviation industry to replace the existing Air Passenger Duty scheme, providing that the unique status of air transport in this region of the UK is reflected in the eventual taxation mechanism applied.

As a body charged with considering all aspects of private and public transport provision within the Highlands and Islands, and between this region and the rest of the United Kingdom, HITRANS is clearly anxious to ensure that each mode of transport is treated equitably by Government, and in a manner that will not have proportionately greater impact on this peripheral region than elsewhere in the country.

HITRANS accepts that each transport mode contributes to NO_x and CO₂ emissions, both locally and globally, as well as causing specific localised noise and emission nuisances. As such it should ask that the Treasury ensure that aviation, particularly domestic aviation, is treated in an even handed way in terms of consideration of environmental taxation that reflects the particular nature and function of this sector within the Highlands and Islands.

HITRANS is not an operator of airports or airlines in its region, and should seek instead to provide comment on the impact of the proposed Aviation and Fuel Duties on the supply of and demand for air services to, from and within its region, and the subsequent potential social, economic and environmental impacts and the sustainability of the region.

The draft HITRANS response to the questions posed in the Consultation are given in the appendix to this report, the Treasury questions / comments are shown in *italics*:

Report by: Dave Duthie
Designation: Partnership Director
Date: 29 March 2008

HITRANS Response to the Treasury Consultation on Aviation Duty

HITRANS (Highlands and Islands Strategic Transport Partnership) is the statutory body concerned with the development and coordination of all public transport programmes within the Highlands and Islands of Scotland, but excluding the Shetland Isles, which is represented separately. It also takes a strategic interest in the provision of trunk transport services to and from the region, including air services.

HITRANS welcomes the initiative by Her Majesty's Treasury to consider alternative ways of taxing the aviation industry to replace the existing Air Passenger Duty scheme.

As a body charged with considering all aspects of private and public transport provision within the Highlands and Islands, and between this region and the rest of the United Kingdom, HITRANS remains anxious to ensure that each mode of transport is treated equitably by Government, and in a manner that will not have proportionately greater impact on its peripheral region than elsewhere in the country.

HITRANS accepts that each transport mode contributes to NO_x and CO₂ emissions, both locally and globally, as well as causing specific localised noise and emission nuisances. As such it would ask that the Treasury ensure that aviation, particularly domestic aviation, is treated in an even handed way in terms of consideration of environmental taxation that reflects the particular nature and function of this sector within the Highlands and Islands.

HITRANS is not an operator of airports or airlines in its region, and seeks instead to provide comment on the impact of the proposed Aviation and Fuel Duties on the supply of and demand for air services to, from and within its region, and the subsequent potential social, economic and environmental impacts and the sustainability of the region.

The HITRANS responses to questions posed in the Consultation are given below, the Treasury questions / comments are shown in *italics*:

The basis of the duty: aircraft measure

A.2 The Government's preferred option for an aircraft measure is Maximum Take-Off Weight, however two other options are also considered as part of this consultation. The Government welcomes responses to the following questions:

A.3 Maximum Take Off Weight:

1. What would be the simplest and most transparent method of using maximum take-off weight: banding or straight calculation of either the constant MTOW or some function of MTOW?

If the Treasury following completion of the consultation concludes that airport operators should be the collecting agent for this tax, then the use of the declared MTOW¹ would be simple to collect. It is believed that the majority, if not all, of the UK airports calculate aircraft landing (or departure) charges on the declared MTOW of aircraft and would thus be easily able to calculate the aircraft weight component of any tax. There would seem to be no benefit to be obtained from banding the aircraft weight component – this would actually

¹ This is now more commonly known as Maximum Takeoff Mass (MTOM).

increase the complexity and (depending upon the number of bands) penalise certain aircraft types.

HITRANS notes that (ignoring aircraft of less than 5.7 tonnes MTOW) aircraft using Inverness Airport have a relatively constant relationship between the MTOW of an aircraft and the maximum number of seats possible – at 13.2 tonnes and a maximum of 34 seats, the Saab 340 weighs in at 0.39 tonnes per seat, whereas the A319 of easyJet at 64 tonnes and 150 seats averages 0.43 tonnes per seat. There would thus seem to be little benefit from developing a new complex function regarding MTOW.

2. *Are there any possible distortions/problems caused by using MTOW?*

Firstly, it is understood that some airlines deliberately reduce the declared MTOW of their aircraft below the manufacturer's declared MTOW in order to benefit from reduced landing fees and en-route charges. If this is found to be the case it would be possible for the Treasury (if it so chose) to advise UK airports of the appropriate manufacturer's MTOW for taxation purposes.

Secondly, and more importantly, fuel-efficient aircraft would be taxed the same as fuel-inefficient aircraft of the same weight. There would thus be no clear signal given by the Treasury that more fuel-efficient aircraft benefit from application of a tax of this nature – indeed, some modifications made to aircraft to improve fuel consumption add weight to the aircraft and would penalise them still further. If the aim is to encourage environmental responsibility then the MTOW approach is unlikely to be the best approach, albeit it may be the simplest to administer.

Optional safety or security enhancements, or additional instrumentation to improve track-flying, could add weight and therefore tax if they resulted in a change in MTOW rather than a corresponding reduction in the weight available for payload or fuel. One consequence of MTOW tax raising mechanism might be that airlines will be anxious to purchase aircraft with ever-increasing proportions of lighter carbon composites just to save on UK tax, irrespective of their impact on emissions, rather than focusing any investment specifically on reducing the environmental impact of their fleet.

3. *What do you think the environmental benefits of using MTOW would be?*

This will be dependent upon the average cost per passenger compared to the current level of APD. If the overall sum collected does not alter significantly from the current APD regime, and the net effect on passenger cost is negligible, then so will the impact on emissions be negligible.

This (MTOW) method of applying the tax does not reward airlines for taking environmentally-beneficial decisions. Instead, low-cost airlines are likely to examine the impact on MTOW of reducing – say – the number of toilets or catering equipment, or of reducing the weight of aircraft seats, even at the expense of passenger comfort where a change in certifiable or real MTOW was realistic.

4. *How well do you think that using MTOW as the basis for the duty helps the Government achieve its objectives?*

An MTOW approach may be seen purely as a tax-gathering exercise, providing no clear incentives for airlines to improve their emission levels.

An alternative, which would require the Treasury to undertake more detailed research, might be to base the charges not on MTOW but on an assumed maximum payload at MTOW.²

A.4 *NOx emissions in the landing and take-off cycle:*

5. *What would be the simplest method of using NOx emissions: banding or straight calculation of either the constant NOx emissions or some function of NOx emissions?*

HITRANS believes that either NOx or CO₂ emissions should be used as the basis for taxing airlines as they appear far more accurate than the simple measure of MTOW in correlating with environmental pollution, both local and global. In examining Charts 2.2 through to 2.5 provided in the Consultation, the impression obtained is that the measurement of CO₂ during the landing and take-off cycle may give the closest correlation, but HITRANS is not competent to determine which may be marginally more representative, and defers to expert analysis by others.

This answer to question 5 thus also applies to question 8.

As with MTOW, HITRANS believes that any taxation ought to be based on actual measurements of NOx or CO₂ emissions by aircraft type and sub-type, rather than on banding, which may penalise some aircraft at the edges of each band, and would better focus on actual environmental impact. Once a specific value has been obtained for each aircraft fleet or sub-fleet, it would be a one-off exercise for HM Treasury to circulate this information to all UK airports and a further one-off exercise for each airport to allocate the necessary data against each aircraft in its own database which will currently include MTOW and other charge data for each aircraft. Aircraft owners and manufacturers should have the ability to challenge the value as determined by the Treasury. But this must recognise ICAO and related international impacts of such actions.

6. *Are there any possible distortions/problems caused by using NOx emissions in the landing and take-off cycle as the basis for the duty?*

No significant distortions are foreseen. It would be expected that the signal given by this tax should in the longer term encourage airlines to replace aircraft with poor environmental performance by aircraft with much lower emissions wherever possible. The only possibility is that it should encourage aircraft manufacturers to concentrate on reducing emissions solely on approach and departure from airports rather than on reducing emissions during cruise, but it is likely that any such developments would also improve cruise emission performance. In addition, the capital cost differential between new and second-hand aircraft is such that the duty / tax would need to be significantly increased to accelerate the changeover and offset the difference between higher operating costs and higher ownership costs.

² It is recommended that as part of this exercise the Treasury should seek advice on Aircraft Weight Statements. This should include the recognition of the various definitions of weight as applied to aircraft operations. This should include an understanding of what comprises and the relationship between: Maximum Take Off Weight, Maximum Taxi Weight, Maximum Landing Weight, Dry Operating Weight, Operating Weight Empty, Aircraft Prepared for Service.

7. *What would be the best source of robust data on NOx emissions in the landing and take-off cycle?*

HITRANS is confident that advisers to the Treasury will be able to establish appropriate up-to-date emission information on the majority of the aircraft flown to and from UK airports today, based on their use of data for 62 aircraft types from the European Environment Agency's CORINAIR Emissions Inventory Guidebook. It is noted that one of the aircraft types listed is 'Executive Jet Chapter 3', which suggests that the Treasury would be able if necessary to band together certain aircraft types where individual data for each type is not immediately available. It is our view that the 62 types for which data is already provided will constitute in excess of 95% of all projected taxation revenue.

A.5 *CO₂ emissions in the landing and take-off cycle:*

8. *What would be the simplest method of using CO₂ emissions in the landing and take-off cycle: banding or straight calculation of either the constant CO₂ emissions or some function of CO₂ emissions?*

See the answer to question 5.

9. *Are there any possible distortions/problems caused by using CO₂ emissions in the landing and take-off cycle as the basis for the duty?*

See the answer to question 6.

10. *What would be the best source of robust data on CO₂ emissions in the landing and take-off cycle?*

See the answer to question 7.

A.6 *Other basis questions:*

11. *Is there another aircraft measure that would be better for aviation duty than the three options described above?*

Ideally, aircraft ought to be charged on the actual amount of NOx and CO₂ emissions caused by flights from airports in the U.K., and this could be most easily determined by the amount of fuel actually consumed, with – perhaps – different charges for aviation gasoline and aviation turbine fuel³. However, the Consultation makes it clear that such an approach is not permitted by Article 24 of the Chicago Convention, and that international agreement will be needed to achieve such an objective. No other aircraft measure would seem to be as well-suited to the task as the proposal to measure NOx or CO₂ emissions on landing and take-off.

12. *The Government would also welcome views on the extent to which the new aviation duty could play a role in covering other environmental costs as well as incentivise airlines to use quieter aircraft.*

The current proposals put forward in this Consultation presuppose a calculation of 'x' units of aircraft (whether MTOW or emissions-based) times 'y' units of distance times a constant of £ 'z' to give a total charge of £ 't' per departure.

It is not felt that a modification to 'x' 'y' or 'z' would be relevant to local noise, as the environmental nuisance of this will be identical whether the flight is taking off for a journey of 60 or 6,000 miles. This will be based on the noise contours which will have been prepared utilising the MTOW figures.

It would however seem to be only a minor change to introduce a noise factor 'n' to take account of neighbourhood noise around an airport based on the current noise quotient of zero and 0.5 to 4 by aircraft type already used in the determination of night quota

³ It should be recognised that in the UK for internal UK operations use by aircraft Jet A1 – Kerosene – incurs VAT at 5% and no duty, whilst AVGAS incurs full duty and VAT.

movements. Each major aircraft type already has a UK-agreed noise classification, and this information could be given to airports and added to the MTOW and emission data for each aircraft type. Each airport would then be given an individual factor 'f' reflecting the number of people resident within – say – the 57dBa contour, so that a noisy aircraft would pay significantly more to depart from Heathrow than from Inverness. Multiplying 'n' by factor 'f' and a constant of £ 'c' would give an element in the applied tax to cover noise nuisance. This element of tax could be added by the airport operator to the total invoice to the aircraft operator.

A.7 The Government recommends that the distance factor used in the calculation of aviation duty is determined by placing destinations into three geographical bands. The Government welcomes views on this recommendation, and, in particular would be interested in answers to the questions below:

13. Do you agree that banding is the most appropriate measure?

No, unless the banding is significantly more fine than the three bands proposed by the Consultation. It seems inappropriate to HITRANS that a domestic flight of – say - 80 miles from Belfast to Prestwick on a Ryanair B737-800 should be charged the same amount as the same aircraft flying 2,350 miles from Glasgow to Larnaca. This would benefit those (predominantly leisure) passengers that were emitting up to 30 times more NO_x and CO₂ compared to those on the domestic flight, being used for business and for visiting friends and relations providing economic and social benefits to these regions of the UK. A very coarse banding could lead to the cessation of vital short distance domestic flights where there is no obvious surface alternative.

14. Do you agree with the banding system that the Government has suggested?

No, for the reasons given above. The Treasury has in introducing this new tax the opportunity to bring in a more finely-honed instrument that reflects the actual amount of emissions. If the Aviation Duty is to be reflected in an extra cost by airlines in determining their pricing policies, there would seem to be no benefit to passengers to know whether it was part of a simple three-band pricing policy which did not reflect their actual journey and its environmental impact.

HITRANS has no strong views about the non-EU bands proposed, but is concerned that it could influence passengers to take short-haul flights to Europe to connect with long-haul flights, or that airlines themselves may insert traffic stops at EAA destinations en route to Africa, Asia and America. Such an approach could be to the detriment of attracting and retaining inward investment in our region as it could reduce connectivity between the Highlands and Islands and key business interests out with the EU, which is key to our economic viability.

HITRANS would recommend that consideration be given to either that the EAA band is replaced by a great circle measurement for each route, or is composed of a minimum of four distance-bands, such as 0-200 miles, 200 – 500, 500 – 1000, and 1000 plus.

15. *How well does a banded approach to distance achieve environmental objectives, given the need to avoid a perverse incentive to fly via intermediate hubs?*

In Paragraph 2.24, the Consultation states that:

One of the key objectives behind the reform of aviation taxation is to make it better correlated to distance travelled, in order to align it more closely with actual environmental costs. The Government therefore believes that a criterion based on distance should be used in conjunction with an aircraft measure in order to determine the basis of aviation duty.

It is acknowledged that the main problem faced by the Treasury is that a high charge on passengers departing the UK for intercontinental destinations would lead to many passengers taking local flights to Dublin, Paris, Brussels, Amsterdam and Frankfurt in order to join flights upon which there is no penal environmental tax. Airlines might also seek to insert en-route stops wherever they believed it would not discourage too many travellers. The net result is that UK airports will be avoided wherever possible, and transfer and transit traffic will prefer to use continental airports to British airports wherever possible. It could in time lead to a significant reduction in the number of passengers transferring at London Heathrow between international and linked domestic flights. This has already happened at Heathrow due to the reduction in the number of UK domestic points served, including Inverness and Aberdeen, as a result of runway slot pressures.

Such a change in practice would achieve no benefit in environmental terms. Instead, the passenger who subsequently chooses to fly from London to Amsterdam and then on to Singapore will cause more emissions than if they had flown non-stop from Heathrow – but they would pay significantly less. Only when the UK can work collectively with the other European governments to introduce similar legislation will such loopholes be closed off.

16. *What are the possible distortions/problems caused by using distance?*

The benefit of using distances is that passengers flying 6,750 miles non-stop from London to Singapore would pay ten times more aviation duty to the UK Government than one flying 700 miles to Barcelona, reflecting the probable environmental impact. The downside is that long-haul flights from London (and Scotland) would probably be reduced in frequency and lose out to intermediate hubs as passengers sought to minimise their taxation costs.

The result of such an approach would be that short-haul passengers would pay substantially more per mile flown, because far fewer of them would need to use intermediate hubs. The most ‘captive’ of all passengers would be those on domestic flights, as they would have no ability to travel via a European hub. Already, economy passengers from Inverness to Manchester pay £10 APD but only £40 to fly to New Zealand, some 40 times further. This anomaly in environmental impact included in APD should not be transposed into the new Aviation Duty tax.

17. *What would the advantages/disadvantages of using great circle distance be?*

The advantage is that every airline – and therefore every passenger and tonne of freight – would be demonstrably charged according to the amount of pollution and contribution to global warming they are adjudged to have made. Each airport would need to compile a list of Great Circle distances for every airport served – this would not be a substantial task.

The downside is that the number of direct non-stop intercontinental flights from UK airports would be reduced as both passengers and airlines first took short sector hops to a European airport before travelling on. This would dramatically impact, not only on passenger journeys and on airline finances, but also on the overall UK economy, including that in the Highlands and Islands, as London would no longer be a preferred hub for airlines. The Highlands and Islands have currently no links to European hub airports outwith the UK.

18. *How would you combine distance with other criteria?*

As discussed above in relation to question 12, it is assumed that there would be ‘a calculation of ‘x’ units of aircraft (whether MTOW or emissions-based) times ‘y’ units of distance times a constant of £ ‘z’ to give a total charge of £ ‘t’ per departure’.

19. *Are there other alternatives for including a distance factor, not already covered?*

None that improve upon the Great Circle and banding options put forward.

General and business aviation

A.8 *The Government welcomes views on the proposal that a 5.7 tonnes de minimis limit for aviation duty is applied, with all fixed wing aircraft below this level subject to fuel duty. In particular, responses would be welcome on the questions below:*

20. *Do you agree that a de minimis limit based on the weight of an aircraft a suitable measure?*

Yes. Based on the 80:20 Pareto principle, the necessary effort expended to obtain the taxation from the owners and operators of small aircraft would be wholly disproportionate to the amount of taxation raised, especially when another source of taxation from such aircraft is readily available.

21. *Is 5.7 tonnes a suitable level at which to set a de minimis limit?*

Yes. The 5.7 tonnes (or 12,500 pounds) limit is well-established worldwide as the weight which separates ‘light’ aircraft from ‘other’ aircraft. The two main scheduled passenger aircraft currently operated on local lifeline services to our island communities at the smaller airports of the Highlands and Islands are the 9-seat Islander at some 3 tonnes, and the 18-seat Twin Otter at a fraction under 5.7 tonnes. Other potential future replacements for such services, such as the Cessna 208 Caravan, fit within this category.

22. *Is there an alternative measure that you feel is more appropriate?*

No. It is believed that that the principle of charging fuel duty on all aircraft of below 5.7 tonnes is the simplest and fairest way of ensuring that all aircraft pay an environmental tax. It would however need to be clearly established that the level of fuel duty applied to this sector is proportionate to the comparative environmental impact of these aircraft with those covered by the proposed Aviation Duty levels

23. *Can you suggest an alternative way in which to ensure that aviation is captured either by aviation duty or fuel duty while minimising administrative burdens and complying with international law?*

No. However, it should be noted a degree of policing of this split may be necessary as aircraft operators that have aircraft both larger and smaller than 5.7 tonnes using the same fuel could potentially fill up their larger aircraft with zero tax fuel and then transfer it to their smaller aircraft. This potential form of tax evasion may be difficult to police at low cost. One option would be to adopt a “red diesel” approach with potential safety, operational, production, storage and certification impacts.

24. *Do you agree that all helicopters should be placed within the fuel duty regime rather than the aviation duty regime?*

Yes. There will obviously be some problems caused with international flights, particularly those to oil rigs in the North Sea, but the principle is correct. The costs of helicopter operation are however so great that there is little likelihood of operators electing to use helicopters for short-haul services to Europe to avoid paying aviation duty. Use on emergency and utility operations should remain exempt.

Exemptions

A.9 *The Government welcomes responses on the issue of potential exemptions. In particular, there is interest in answers to the questions set out below:*

25. *Do you think that there is a strong case for any of the exemptions listed above?*

Yes. HITRANS accepts the legally required exemptions for military and diplomatic flights. HITRANS also supports exemptions being considered for the four of the five categories of operation listed in Paragraph 4.7 – that is to say, for emergency services, for public services, for training flights and for maintenance flights, but not for public aerial display flights, subject to those operators affected providing sufficient evidence to the Treasury for those flights to be so treated.

With regard to flights within and from the Highlands and Islands, HITRANS and Highlands and Islands Enterprise have consistently successfully argued the case for the current exemption from paying Airline Passenger Duty for these flights and believe that the same arguments should be accepted and exemptions applied with regard to the proposed aviation duty. The evidence relates to the absolute reliance of this region with significant island and remote communities upon scheduled passenger services for many of their regular day-to-day needs – work, education, health and essential supplies. Air services provide vital and unique links to the rest of the country not effectively available by land based transport. They ensure the social cohesion of the region, and with this, its economic sustainability.

HITRANS does not seek to replicate that evidence here, but is prepared with Highlands and Islands Enterprise and the Scottish Government to give evidence to the Treasury if it is required.

One difference between the APD regime and the proposed aviation duty plus fuel duty regime proposed is that, for the first time, turbo-prop aircraft of less than 5.7 tonnes will now have to pay fuel duty on flights to and from the Highlands and Islands. Thus the Twin Otter Flights serving Barra, Tiree and Campbeltown will now have an additional cost to bear, as will the inter-island services operated by the nine-seat piston-engined Islander, which currently pays aviation duty and VAT on its Avgas.

HITRANS proposes that, not only should aircraft over 5.7 tonnes operating scheduled services to and from airports in the Scottish Highlands and Islands be exempted from paying aviation duty, but that aircraft of less than 5.7 tonnes operating similar scheduled flights should be exempt from the payment of the equivalent tax through application of fuel duty. All other modes of public transport are supported by Government through fuel duty rebates and it is inappropriate that this necessary public transport sector that serves some of the most remote areas in the UK should not receive similar dispensation in reflection of its function.

Paragraph 3.17 it is stated that:

Currently, international law compels the United Kingdom to provide a rebate for fuel duty on international flights and this rebate will continue to remain in place. This means that operators of aircraft under 5.7 tonnes who make international flights would continue to be able to reclaim the proportion of duty paid on fuel used in the international segment of a flight.

HITRANS makes the recommendation that, as with international flights, operators of such scheduled services in the Highlands and Islands be allowed to reclaim the proportion of duty paid on fuel used for these flight segments.

26. *Are there any other categories of flight for which there is a strong case for exemption? If so, how would those exemptions be defined and enforced?*

HITRANS is strongly of the view that all UK scheduled domestic flights subject to the payment of aviation duty be granted a 50% rebate on aviation duty. A passenger travelling between Inverness and Belfast will pay the tax twice, once on departing Inverness, and again on departing Belfast; whereas a passenger flying to Dublin will pay only once, at least until such time as the Irish (and other) Governments introduce a similar aviation tax. This will harm domestic air travel, much of which is either over water, or of such length as to make road and rail alternatives nonviable. The situation is compounded by multi-sector services – for example, the daily service from Inverness to Southampton operates via Leeds Bradford. Our understanding of the proposed application of Aviation Duty is that a round-trip passenger to Southampton will pay Aviation Duty four times, which will make many domestic air services totally uneconomic on routes where land based transport is not a practical alternative. A passenger to Southampton is likely to pay more than one from London to Auckland. Even with a 50% discount, it will still be twice as expensive as flying to Dublin on the assumption of a standard EAA charging band.

We would ask the Treasury to give serious consideration as to how Aviation Duty can be re-shaped to overcome these two anomalies.

27. *Would there be a strong environmental case against any of the possible exemptions?*

With respect to scheduled flights to and from airports in the Highlands and Islands there will of course be a certain level of noise and emission pollution associated with such flights, but studies undertaken have consistently shown the impacts to be de minimis, and in some cases of less environmental impact than the equivalent land and water based movement. The majority of these flights are by turboprop aircraft which do not reach sufficient altitude on these short sectors to be a significant contributor to emissions in the upper atmosphere.

Freight

A.10 *The Government's intention is that aviation duty will apply to aircraft carrying freight as well as those carrying passengers. Although decisions on rates are yet to be made, in considering the impact, it is envisaged that the duty levied per flight will be of a similar magnitude to the amount of APD paid on a similarly sized aircraft. However, responses on the following questions will be welcomed:*

28. *What economic impacts do you think there will be? You might wish to consider the Impact Assessment of freight in Annex B.*

29. *What would be the economic impacts on freight-only flights?*

30. *How might freight operators pass the costs through to consumers? How sensitive have consumers been in the past to a change in price?*

31. *What would be the environmental impacts of applying aviation duty to freight?*

32. *What would be the impact on freight hubs and modal transfers of goods from these hubs?*

33. *Do you have any other comments about the application of aviation duty to freight?*

HITRANS has no strong views on the subject of aviation duty on freight. It is currently a relatively small element in commercial aviation either within the region, or from the region to the world. It would argue that commercial freight flights to airports in the Highlands and Islands, predominantly over-water flights carrying newspapers and mail, should be granted the same exemption as would apply to passenger flights, whether concerning aviation duty, or the ability to reclaim on fuel duty. Such flights do help reduce the peripherality of the region and improve social cohesion.

Regarding other all-cargo services, almost all air-freight from Inverness and the rest of the Scottish Highlands and Islands is conveyed by road vehicle to Glasgow, Manchester, London or airports on the near continent such as Ostend and Luxembourg. It is believed that the air freight industry is best placed to provide the necessary guidance to the Treasury.

Transit/transfer passengers

A.11 The Government is minded that aviation duty, as a per plane duty, should apply irrespective of the passengers carried. However, responses on the following questions will be welcomed, and carefully considered:

34. What evidence can you provide about the impact of moving to aviation duty on the provision of transfer services?

HITRANS has no evidence to put before the Treasury, but it understands that – at present – passengers from Inverness to Europe and beyond currently pay the appropriate APD according to the destination and the class of travel. In future, they will pay one Aviation Duty charge to fly to London, and then an additional charge to fly on to their final destination. No other airport in the HITRANS area has direct flights to London and passengers from these airports would – in the absence of the requested exemption – have to pay Aviation Duty on a domestic Scottish flight, before paying to depart from a Scottish hub airport to London, and then pay a third time on departing London.

Not surprisingly – and depending upon the total Aviation Duty involved – passengers in this region will investigate the total costs of flying to their eventual destination by alternative routes. With only three international flights a week from the region today (from Inverness to Dublin) the options are limited, but in time might lead to some airlines considering offering direct flights to European cities and bypassing the British Hub airports.

Passengers who currently fly from Inverness to Edinburgh to support their local international flights will now be further penalised compared with those who drive between the two cities and by doing so add to local road based congestion and increased emissions, the aircraft on the route being turboprops.

These trends are likely to reduce the number of people using English and Edinburgh airports for transfer purposes to reach Northern Scotland, and may reduce the total level of air traffic to and from the region, with knock on detrimental impacts on the sustainability of the local economy.

The net effect is that passengers seeking to use international aviation to and from the peripheral regions of the United Kingdom will once more be penalised compared to South East England. This will increase the costs for commerce and industry in such peripheral regions, and make it more expensive for foreign and business travellers to access the regions. The net effect will be an increase in GDP in the South East of England (and additional pressure on housing and the provision of services) and a corresponding decrease in the peripheral regions, which already lag far behind in the South East in terms of GDP.

35. What are the economic and environmental implications of these impacts?

The economic implications are discussed above. The environmental implications will benefit from a small decrease in the number of passengers flying between the Highlands and Islands and points further south, being partially replaced by additional car travellers.

36. How might airlines change their business model in response to this design of the duty?

Firstly, airlines are likely to terminate all multi-stop domestic routes, as the cost for passengers travelling from end-to-end will dramatically increase. This will reduce the number of cities served directly from minor destinations such as Inverness. For example, not only will passengers be unprepared to pay four Aviation Duty charges at the EAA band for a day-trip to Southampton via Leeds Bradford, the route to Leeds Bradford itself will become unsustainable without the added contribution of passengers travelling on to Southampton.

Passengers are being penalised for having to use multi-stop flights even though they would much prefer to fly non-stop. One partial solution to this would be to base the Aviation Duty on Great Circle distances between origin and final destination, at least domestically, so as to minimise this impact.

Secondly, it will be much more difficult for airlines to justify opening any new routes or increasing frequencies, either domestic or international, because they will now have to pay the full aviation duty for the start up period while they hopefully build up the traffic from low initial levels. Airports understand this, and normally offer substantial landing charge rebates to airlines to encourage them to seek out new routes which will support the local economy. The Department for Transport supported this approach with its Route Development Funds which were designed to encourage such new routes. This Treasury proposal would be totally counter-productive to the DfT initiative unless it also agrees to exempt new routes from Aviation Duty for the first one, two or three years while airlines establish a routes viability. This could have a serious impact on future route, schedule and network development from the region within which a large number of passengers currently travel by car to airports outwith the region to start the air segment of their journey.

Thirdly, airlines will be more reluctant to use small aircraft. Statistically it is far more difficult to achieve an 80% passenger load factor on a 34 seat aircraft than on a 340 seat aircraft. Passengers on thin routes in remote areas or flying to those airports that can only support small aircraft (including London City and many smaller airports in Scotland) will be paying higher rates of Aviation Duty per head than those on larger aircraft that can achieve higher load factors.

Airlines operating small aircraft such as the Saab 340 could face problems in replacing these aircraft in future, because the world's aircraft manufacturers are no longer focussing on making commercial aircraft with less than 50 seats. Not only will the airline have to purchase a more expensive replacement aircraft that is initially too large for the markets to be served, it would be further penalised by having to pay excessive aviation duty on non-exempt routes related to that extra size, with few passengers available to absorb the cost. The simpler solution for operators may just be to abandon the route, which may in turn lead to a need for Government to support the lifeline services so provided. An option on some routes of allowing Single Engine Turbine aircraft to operate in Instrument Meteorological Conditions (as is permitted in North America and other parts of Europe) would require changes to current CAA operational regulations.

37. How might passenger behaviour be affected? How sensitive have consumers been in the past to a change in price?

HITRANS has not conducted its own sensitivity analyses on air passengers to investigate fare increases on air routes, and will be reliant on studies undertaken elsewhere. Anecdotal evidence suggests that passengers will examine other ways of reaching their destination where the total airline and airport ticket price might be lower than the current route.

HITRANS would point out that the Air Discount Scheme was introduced in the Highlands and Islands of Scotland to reduce peripherality through subsidising airline fares for island residents and has had a significant impact on increasing traffic and connectivity between the islanders and relatives and service providers on the mainland, demonstrating the cost sensitivity of air travel in the region. Any increase in cost through the levy of a duty, if not continuing to be exempted as with APD, would be likely to reverse that process to the significant detriment of residents and the economy of the region. The cost of running PSO air services supporting the most remote communities through the public purse would also increase.

Although not directly affecting Northern Scotland, passengers who currently transit a London airport en route from – say – Eastern Europe to the USA will find that the cost of that routing will now be greater because of the extra charge by the UK Treasury for the London-USA portion. Alternative routings through Copenhagen, Frankfurt, Amsterdam, Brussels, Paris and even Dublin might now prove more attractive. HITRANS would expect the number of international to international transfer and transit passengers at London to decrease substantially. This will lead to reduced frequencies, or routes, or aircraft sizes to and from London, and may well damage the ability of these airports to compete as global hubs. London is the only effective access point from our region to international destinations and reductions in flights through London will reduce the attractiveness of our region for inward investment and tourism alike.

38. What, if any, specific routes would be affected?

Airlines that currently transit London (for example Kuwait Airways between Kuwait and the USA) may choose to route via Paris instead. Airlines that rely heavily on transfer traffic joining their flights at Heathrow and Gatwick, particularly international transfer traffic, may cease to operate. Airlines operating multi-sector domestic routes where transit passengers will be double-charged are likely to discontinue or reduce frequency on these routes.

Administration of per plane duty

A.12 The Government welcomes views on the administrative options that have been set out, and in particular would be interested in responses to the questions below:

HITRANS has no strong views as to whether Aviation Duty should be the responsibility of either the operators or the airports, but makes the following comments which may be helpful to the Treasury:

A.13 Option a: aircraft operators to collect and account for aviation duty:

39. Would having all aircraft operators registering to pay the duty be an appropriate and workable way of administering the duty?

As always in any industry, there will be a few large companies for whom this would cause no problem, and a large number of small companies for whom this will be an extra headache and one for which they will not be structured. This would be particularly true for small foreign aircraft operators that only occasionally fly to the United Kingdom.

40. Do aircraft operators have the means to report the appropriate information on the number of flights taken and any relevant information on the duty basis to HMRC? Would any of the measures mentioned under the duty section cause problems for aircraft operators?

It is likely to add to the operators' administration costs which would potentially be passed on in increased charges, or discourage such operators from offering competition in the UK market.

41. What reporting requirements do aircraft operators have to airports, the CAA and other bodies? How are these carried out i.e. monthly, annually, per flight?

If an operator holds an Air Operators Certificate (AOC) then they have to make regular returns of both operational and financial data to the CAA. The operators of all aircraft (including commercial and General Aviation) are required to "book in and out" from all airfields used, whether licensed or unlicensed, to meet Home Office requirements.

42. Do the estimates in the Impact Assessment for the administration burden reflect your expected costs?

HITRANS does not have a view.

43. What problems might arise from having aircraft operators as the registered tax payer?

In principle, an airline flies its passengers to and from the UK, and then at a much later date submits the information to the Treasury. At that time it might find that it should have charged its passengers or freight significantly more than it had collected. It is suggested that an airline would much rather receive an invoice from an airport so that it knows immediately how much to charge its passengers and freight, and how much to set aside for the Aviation Duty.

A.14 Option b: licensed airports to collect and account for the duty. When answering these questions please consider how collecting the duty would fit in with current fee structures, how other fees are collected, how debt management currently works at airports and possible distortions that could be caused by this method.

44. Would the alternative of using airports to collect the duty be an appropriate and workable arrangement?

- For the users of licensed airports?*
- For licensed airports themselves?*

HITRANS believes that the answer is 'yes' for the users of licensed airports, and possibly 'yes' from the airports themselves. It would not seem at face value to be a difficult problem for airports to add an Aviation Duty component to each flight invoice – the only data it needs added to its database are great circle distances or banding for each non-stop destination, and possibly the relevant emission categories by aircraft type, plus the current rate per tonne of MTOW or per unit of emissions.

45. Do licensed airports have the means to collect and report the appropriate information? Would any of the measures suggested for the duty basis cause issues for these airports in collecting the duty?

It is for airports to answer, but in theory there should be no difficulty as long as the Treasury supplies airports with standard MTOW or emissions data and banding or Great Circle distance information; but there would inevitably be an increase in cost of administration and associated processes to be met.

46. To what extent could general aviation and business aviation traffic move to non-licensed airports?

Most business aviation flights, particularly air taxis, could not move to non-licensed airports, because (it is understood) of the insurance implications for commercial passengers. Few other general aviation aircraft will be heavier than 5.7 tonnes, and most non-licensed airfields would be unable to handle them. The Treasury would have to contact the non-licensed airfields to ensure that they invoice all aircraft over 5.7 tonnes for Aviation Duty to ensure equity of application of the Duty.

47. Please refer to the Impact Assessment; does our assessment of the administration burdens for airports collecting the duty reflect your knowledge of how much this might cost? If not please let us know where it differs.

No view.

48. Any further comments on this issue?

No.

49. Are there any comments raised on the issue of the impact on unlicensed airfields?

There are a large number of unlicensed airfields in the Highlands and Islands, mostly with runways of less than 800 metres, and mostly not capable of handling aircraft larger than the Twin Otter at 5.6 tonnes. Although a small number may escape 'detection' for a while, it will certainly be easier to control a fixed number of airfields in the United Kingdom than a continually fluctuating, and much larger, number of aircraft operators, many of them foreign. The issue of the method of application of the Duty to sea plane operations which do not use land based airports should also be considered.

HITRANS will be pleased to answer any questions arising from this evidence.

End.