



HM Treasury

Options for supporting English regional airports from the impacts of air passenger duty devolution: *summary of responses*

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ISBN 978-1-911375-40-1
PU1996

Contents

		Page
Chapter 1	Introduction	3
Chapter 2	Summary of responses	5
Chapter 3	Next steps	7
Annex A	List of respondents	9
Annex B	APD background note	11

1 Introduction

1.1 The government is moving forward with its vision of a strong economy supporting strong public services. Closing the productivity gap between the capital and our regional cities will be key to Britain's future outside the European Union. The government remains committed to regional devolution to rebalance the economy by boosting growth outside of London and the South East. To date the government has delivered the Smith Commission Agreement for Scotland and is delivering the St David's Day Agreement for Wales and the Stormont House Agreement for Northern Ireland, as well as further devolution to cities, towns and counties in England. The government continues to drive both the 'Northern Powerhouse' and 'Midlands Engine' by pushing ahead to deliver a package of devolved powers for major cities and investing in transport and infrastructure.

Air passenger duty and devolved administrations

1.2 The government has taken a bespoke approach to air passenger duty (APD) devolution across the UK, recognising that what is right for one nation is not necessarily right for others.

1.3 In July 2012, the government devolved powers over rates of APD for direct long haul flights to the Northern Ireland Assembly. As the only part of the UK to share a land border with an EU member state, it is important that the Assembly has the ability to respond to rate changes in the Republic of Ireland.

1.4 In accordance with the cross-party Smith Commission Agreement, APD will now be devolved to the Scottish Parliament in April 2018. In February 2015, the government announced it would consider the case and options for devolving APD to the Welsh Assembly, informed by a review of options to support English regional airports from the potential impacts of APD devolution.

1.5 After the publication of the discussion paper, the Wales Office Minister confirmed to the House of Commons on 12 September 2016 that the government did not intend to devolve APD to the Welsh Assembly as doing so could have caused significant market distortions in what is effectively a single aviation market in South Wales and South West England. As English and Welsh customers use both airports interchangeably, this could have caused negative consequences for both sets of customers.

APD within England

1.6 Regional airports in England have expressed concern about the potential impacts of APD devolution on their business. Specifically, regional airports are concerned that a decision to lower APD rates in Scotland could draw passengers and airlines away from English airports.

1.7 The government recognises that regional airports provide a valuable contribution to the UK economy by stimulating the regional economy, and in helping a variety of businesses to create new jobs. In 2015, regional airports saw 5% growth in passenger numbers, a success which has helped to improve connectivity for people in their areas and increase domestic and global trade.

1.8 The government has therefore reviewed potential options to support regional airports. As part of this review the government published a discussion paper at Summer Budget 2015 in order to further the debate on three possible options:

- i. devolving APD within England
- ii. varying APD rates within England

iii. providing aid to affected airports or regions within England

1.9 The discussion paper highlighted key points for consideration, including legal and operational constraints which might need to be addressed. The government also called for views on the options, together with any further evidence on the likely impact of the options on airlines, airports, passenger numbers and growth – both in specific regions and across the UK as a whole.

1.10 The government received 53 responses to the paper from stakeholders and welcomes the constructive and valuable contributions made by respondents. A list of respondents can be found in Annex A.

2 Summary of responses

2.1 The discussion paper explored three options to support regional airports, identifying key issues for consideration on each option.

2.2 The government received 53 responses to the discussion paper. Several responses called for the government to support regional airports by matching any APD rate cuts made by devolved administrations – an option which was outside the scope of the discussion paper. This chapter summarises the views put forward in response to the options explored in the discussion paper.

Devolving APD within England

2.3 The discussion paper set out the option of devolving APD, fully or partially, to local authorities or combined authorities (including mayor city-regions) within England. This would enable areas within England to set their own rates of APD in exchange for bearing the administrative and fiscal costs of these decisions.

2.4 Respondents to the discussion paper, including local and combined authorities, airports and airlines, were broadly not in favour of this option.

2.5 While some respondents saw this option as an opportunity to increase competition between airports, a number of widely shared concerns were identified across all groups of respondents about the practicality and consequences of the option.

2.6 Certain combined and local authorities had questions and concerns about the implications that APD devolution would have on their funding. Some respondents pointed out that airports located in local authorities with larger tax bases would have a competitive advantage over those located in smaller local authorities with less ability to afford a rate cut. Similarly, some respondents believed that the diversity in size and resources of local authorities across England would weigh on the deliverability of APD devolution across England.

2.7 Airports and airlines tended to warn that devolution within England, leading to rate differentials between airports with closely overlapping catchment areas, would create significant market distortions. Moreover, the creation of a patchwork of rates across the UK would make APD a more complicated and burdensome tax to administer.

Varying APD rates within England

2.8 The discussion paper set out the option of varying the rates of UK APD according to specific criteria, resulting in different rates in different parts of the country, while retaining central government control over APD rates. Such rate differentials would incentivise redistribution of passengers towards regional airports. Responses to this option were mixed.

2.9 Most regional airports strongly supported this option believing that it should be considered further by the government. In their response, a group of regional airports presented analysis which suggested that a significant reduction in APD at non-congested airports would offer benefits to these airports, such as the development of new destinations, particularly in the long-haul market.

2.10 Other airports took the opposite view, seeing the use of a congestion metric as a distortionary and anti-competitive response that would penalise success. As a consequence, some respondents gave the view that using this option to support regional airports would be incompatible with State aid rules.

2.11 Most other respondents supported this view, also noting concerns that this approach might complicate the tax system, lead to unpredictable results and an overall reduction in the UK's international connectivity and hub status. Some respondents noted that the Airports Commission made similar conclusions in its interim report in 2013, ruling out this option as a suitable response to easing capacity constraints in the South East of England.

2.12 Respondents across all groups also commented that creating a system of varied APD rates across the country would unfairly penalise those who happened to live near congested airports.

Providing aid to affected airports or regions within England

2.13 The discussion paper set out the option of providing direct aid to those airports or regions particularly affected by APD devolution. The discussion paper set out an existing example of direct aid already provided to airports, the Regional Air Connectivity Fund, and explained the legal constraints of providing direct aid to larger airports.

2.14 All responses on this topic focused on issues surrounding offering aid to airports themselves, rather than to projects of wider regional interest.

2.15 Responses from smaller regional airports expressed support for the existing Regional Air Connectivity Fund and for further development of the fund. Certain regional airports also advocated the introduction of a long term fund to help mitigate the impacts of devolution and support regional airports' growth ambitions. However, some airports identified that the application process for a fund may be time-consuming and slow, making it ill-suited to the fast-moving and dynamic aviation industry.

2.16 Most other responses pointed out that State aid rules meant that only the smallest regional airports would qualify for direct aid. Many respondents argued that means that this option fails to address possible effects on traffic patterns created by APD devolution which may impact airports of varying sizes. Some larger airports also responded that this would put larger airports at a disadvantage and would create competitive distortions between larger and smaller airports.

Other options

2.17 Several responses to the discussion paper discussed additional options which they had identified.

2.18 One frequently suggested idea was for the government to cut APD across the country, in order to match any decisions that devolved administrations may make on future APD rates. This option would have significant consequences for the public finances. The government has decided that consideration of this idea is outside the scope of this discussion paper. In the absence of any taxation of international aviation fuel and no VAT on international or domestic flights, APD ensures that the aviation sector contributes its fair share to reducing the budget deficit.

3 Next steps

3.1 The responses to the options explored in the discussion paper illustrate that no single option has widespread support. Many respondents noted that devolution of APD within England would lead to various problems; most notably causing significant market distortions. Furthermore, devolution within England is contingent on local support for such a transfer of power. In the absence of support from local decision makers and industry groups the government is ruling out pursuing this option any further at this stage.

3.2 The responses also indicate that there are opposing views on whether to vary APD rates within England. Some airports argued this option was anti-competitive and would penalise success. This was opposed by many regional airports who strongly supported this option. The government notes that some respondents believed that the current State aid rules have rendered this option undeliverable. While the government believes that State aid could be provided, it believes it could only be given in highly restrictive circumstances.

3.3 Likewise, there were mixed views about the option of providing direct aid to all affected airports or regions within England, as respondents noted that doing so would create competitive distortions between large and small airports. Many of the same issues about State aid rules are also pertinent to this option.

3.4 These mixed responses indicate the complexity of the policy options. The government does not, however, believe that these issues are insuperable. However, a number of new and material considerations have arisen since the review was launched.

3.5 In particular, at the time of launching the review, the United Kingdom had not yet held the referendum on the UK's membership of the European Union. Until exit negotiations are concluded, the UK remains a full member of the European Union and all the rights and obligations of EU membership remain in force. This includes the application of EU rules on aviation, State aid and tax devolution issues. This may impact on how the government designs some of the options for support that were put forward for consultation. The government has not yet begun negotiations for a new set of relationships with the European Union as part of our exit, and hence considers it wise to wait for a clearer indication of what legal instruments will continue to govern this area, before taking further support measures for regional airports.

3.6 Secondly, recent decisions have been taken that could alter how far English airports would be affected by devolution:

- In Scotland, the incoming Scottish Government has set out for consultation its plans for a replacement tax to APD, and ideas for potential rates. The government will need to take those updated plans into account.
- The government decided in September 2016 that APD would not be devolved to the Welsh Assembly. It took this decision in light of this review of the effects of devolution, and the responses that were received to this discussion paper also informed the government's decision.
- The recent decision by the government on expanding runway capacity in the south-east of England, which over time may have substantial potential effects on future air traffic.

3.7 These developments are likely to affect the size and scale of changes to air traffic patterns in the UK, and the measures the government could legally put in place to support regional airports

that are affected by devolution. In particular, it is important that the government takes into account the precise nature of the legal settlement for leaving the European Union.

3.8 With these developments in mind, the government does not intend to announce any specific support measures on this issue at this time, but will revisit this issue once the UK has left the European Union. During this time, the government will continue to work closely with local stakeholders to discuss any relevant further evidence or analysis.

A List of respondents

The government thanks all respondents who contributed to the discussion paper.

Aberdeen International Airport Committee	International Air Transport Association
Air France/KLM	Leeds Bradford Airport
Airlines for America	Liverpool and Sefton Chambers of Commerce
Airlines UK	Liverpool City Region Local Enterprise Partnership
Airport Operators Association	Liverpool John Lennon Airport
Association of British Travel Agents	London First
Aviation Environment Federation	Manchester Airports Group
Birmingham Airport	Newcastle Airport Consultative Committee
Bristol Airport	Newcastle International Airport
Board of Airline Representatives in the UK	North East Chamber of Commerce
Chartered Institute of Logistics and Transport	North East Combined Authority
Chartered Institute of Taxation	Regional and Business Airports Group
Confederation of British Business	Regional and City Airports
Consumer Council	Royal Aeronautical Society
Cornwall Airport Ltd	Scottish Passenger Agents Association
Doncaster Sheffield Airport	Southampton International Consultative Committee
Durham Tees Valley Airport	Tees Valley Unlimited
EasyJet	Thomas Cook
Essex County Council	Tourism Alliance
Federation of Small Businesses	Transport for the North
Flybe	UKinBound
Friends of Liverpool Airport	Virgin Atlantic
Gatwick Airport	Visit Britain
Greater Birmingham Chambers of Commerce	Visit England
Greater Manchester Combined Authority	Welsh Government
Institute of Chartered Accountants of Scotland	
International Airlines Group	

We also had responses from a number of individuals.

B APD background note

B.1 Air passenger duty (APD) is a tax levied on the carriage of passengers on aircraft taking off from UK airports. It becomes due when a flight departs, and is payable by the operator of the aircraft. The amount due is dependent on the final destination and class of travel of the chargeable passengers on board the flight.

Table 3.A: 2016/17 APD rates

Band (miles from London to capital of destination)	Reduced rate (economy class)	Standard rate (other classes)	Higher rate (business jets)
A (0-2000) 'Short-haul'	£13	£26	£78
B (2000+) 'Long-haul'	£73	£146	£438

Source: HM Treasury

B.2 In line with the International Civil Aviation Organization (ICAO) rules, the UK does not tax fuel used for international flights. Whilst many other countries levy VAT on domestic flights, there is also no VAT on flights from the UK.

B.3 In the absence of any tax on flying, aviation would be relatively under-taxed compared with other goods and services. APD recognises this fact and ensures that the aviation sector contributes toward general taxation. In 2015-16 APD raised £3.1 billion, making an essential contribution towards tax revenue and reducing the deficit.

Reform

B.4 Budget 2014 reduced the cost of flying to countries over 4,000 miles from London by reforming APD from a 4-band system to a 2-band system (essentially Europe and non-Europe) from 1 April 2015. This scrapped the two highest band rates for APD and cut the cost of flying to the furthest long-haul destinations.

B.5 Autumn Statement 2014 exempted children under 12 from the reduced rate of APD from 1 May 2015. This was extended to children under 16 on 1 March 2016. These new exemptions are in addition to the existing exemption for children under two without their own seat.

Devolution

B.6 In response to the uniquely challenging situation faced by Northern Ireland, the only part of the UK to share a land border with another EU member state, the government took the decision, in line with the wishes of the Northern Ireland Executive, to devolve powers over APD rates for direct long-haul flights to the Northern Ireland Assembly (NIA). This was provided for in Finance Bill 2012 and in November 2012 the NIA passed the Air Passenger Duty Bill. This bill set the APD rates on direct long-haul flights departing from Northern Ireland airports to zero from 1 January 2013.

B.7 In accordance with the cross-party Smith Commission recommendation to devolve APD to Scottish Parliament, the government has passed the Scotland Bill and agreed a Scottish Fiscal Framework that will allow APD to be devolved to Scotland in April 2018. This will give the Scottish Parliament the power to introduce its own APD, with rates at the levels it chooses.

B.8 As agreed in the February 2015 St David's Day Agreement on the future of devolution in Wales, the government has considered the case and options for devolving APD to the Welsh

Assembly, informed by a review of potential options to support English regional airports. The government announced on 12 September 2016 that it does not intend to devolve APD to the Welsh Assembly due to the potentially negative effects devolution would cause to both Welsh and English customers and businesses.

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