

AIR DEPARTURE TAX – HIGHLANDS AND ISLANDS EXEMPTION STATE AID ISSUES

1. The exemption from UK Air Passenger Duty (APD) for flights from airports in the Highlands and Islands was introduced in 2000 by the UK Government in recognition of the reliance on air transport in the only UK region at that time to have a population density of less than 12.5 people per square km.

State Aid

2. State aid is a European Commission (EC) term which refers to forms of public assistance, given to undertakings on a discretionary basis, which has the potential to distort competition and affect trade between Member States of the European Union. The State aid rules are set by the EC and comprise various articles of the Treaty on the Functioning of the European Union (TFEU), Regulations, Frameworks and Guidelines - which set out what aid can be given and under which circumstances. The EC governs Member States' compliance with these rules and many aid measures must be notified to the Commission for approval.

3. In order to establish whether a measure or intervention is regarded as State aid it is necessary to apply the 4 tests. State aid is only present if the answer is yes to all 4 tests:

<ul style="list-style-type: none">• Test 1	<ul style="list-style-type: none">• There has been an intervention by the State or through State resources which can take a variety of forms.
<ul style="list-style-type: none">• Test 2	<ul style="list-style-type: none">• The intervention gives the recipient an advantage on a selective basis, for example to specific companies or industry sectors, or to companies located in specific regions.
<ul style="list-style-type: none">• Test 3	<ul style="list-style-type: none">• Competition has been or may be distorted.
<ul style="list-style-type: none">• Test 4	<ul style="list-style-type: none">• The intervention is likely to affect trade between Member States.

Tax Exemptions and State Aid

3. In principle, a tax measure which is open to all economic operators within a Member State is considered a general measure. This would then be considered non-distortive and would comply with the four tests as set out in the table above. In order to be considered a general measure, any exemption must be effectively open to all businesses on an equal access basis. This means that tax exemptions applicable to all undertakings, capable of satisfying the relevant criteria, are not normally regarded as entailing State aid. Furthermore, any exemption from a tax should be justified by the nature and objective of the tax itself (e.g. an environmental tax could contain an exemption for firms who use only renewable energy sources).

Azores Criteria

4. Under State aid rules, national tax rates must not vary in a way that is more favourable to individual regions if a selective economic advantage is provided to businesses operating in those regions. When tax powers are devolved within a Member State, the regional authority to which they are devolved must bear a sufficient degree of fiscal and economic autonomy from central government. The Azores criteria were established through case precedence and although the EU investigation did not find in favour of the Portuguese authorities, criteria were established which have been used since to assess the economic and fiscal autonomy of regions. The judgement in the Azores case set out clear conditions on the relationship between tax devolution and State aid. When devolving tax powers, regions must have Institutional, Procedural and Economic Autonomy from central government.

Notification to the European Commission

6. As the SG is legislating for the first time on this matter and under the Scotland Act (1998), the SG and Scottish Parliament cannot act in a way which is contrary to EU law. It is likely that the nature of an ADT exemption would require notification to and assessment by the European Commission under State Aid rules before implementation, in compliance with EU law.

Relevant Air Tax Cases

Irish Air Travel Tax Case: (SA.29064)

9. This and subsequent cases involving Aer Lingus and Ryanair established the principle that airline operators benefiting from a reduced rate of travel tax are undertakings that compete in markets that are open for competition. The reduced rate therefore distorts or threatens to distort competition in the internal market and is likely to affect trade between EU Member States.

German Case: Tax reduction for flights to and from certain North Sea Islands (SA.32020)

10. Germany argued that its air travel tax discount did not affect intra-community trade because the effects of the notified measure are confined to a particular region; the number of passengers is low and all domestic and foreign airlines that offer the relevant transport services may benefit from the reduction. The European Commission ruled that it could affect intra – community trade “because of the inherent international character of intra EEA air transport....*Flights have tourists, workers, and businesses using the service which can influence trade flows. Also those airlines eligible for the tax reduction could result in higher passenger numbers and could boost their competitive position.*”

Air Discount Scheme in Scotland

11. The current Scottish Air Discount Scheme offers a significant discount on air fares for travellers from remote communities. It offers a 50% discount on core air fares¹ on eligible routes for residents of Caithness and North West Sutherland, Colonsay, Islay, Jura, Orkney, Shetland and the Western Isles. State aid cover for ADS is provided by the EU General Block Exemption Regulation which allows provision for ‘Social aid for transport for residents of remote regions’. Aid can be granted for passenger transport on a route linking an airport in a remote region with another airport within the European Economic Area.

Brexit

12. For as long as it is as a member state the UK will retain its obligations and responsibilities under European Union rules on Competition, including those on State aid. State aid is a cornerstone of the Single Market/free trade and Scottish Ministers have made clear their current position that they want to remain as close to the Single Market as possible.

Scottish Government State Aid Team
June 2018

¹ The ADS discount is applied to the core fare charged by the participating airline on an eligible route. Taxes, fees, charges and surcharges are not therefore eligible for the ADS discount.