OECD'S MEMORANDUM ON TRANSFER PRICING

DOCUMENTATION AND
COUNTRY BY COUNTRY REPORTING

IATA

FOREWORD

The following position paper has been prepared by the International Air Transport Association (IATA) as a consequence of the OECD Base Erosion and Profit Shifting (BEPS) Action Plan 13 Transfer Pricing Documentation: Country-by-Country Report, Master File and Local File.

The International Civil Aviation Organization (ICAO), which is an affiliate of the United Nations and the international government organisation concerned with aviation, has adopted a consolidated Resolution regarding taxation of international air transport. The primary principle of ICAO policies on taxation is that there should be reciprocal exemption for taxation on earnings of international air transport by States in respect to international airlines. As such, international airlines ordinarily only pay income taxation on income in their own fiscal domicile removing the need to allocate income to those other States in which they operate. The consensus in favor of exclusively residence-based taxation of airlines' income from international traffic is reflected in Article 8 (Shipping, inland waterways transport and air transport) of the United Nations Model Tax Convention and Article 8 of the OECD Model Tax Convention.

Action 13 in the OECD's BEPS Action Plan seeks that governments develop requirements for taxpayers to report income, taxes paid and indicators of economic activity according to a common template, comprising: a Country-by-Country Report, a Master File and a Local File. This position paper seeks official confirmation of the following:

1. An exemption be provided to airlines from country-by-country and transfer pricing reporting where airline activities are limited to the transportation of passengers in international traffic or activities that are considered ancillary or incidental to such activities given the exclusive residence-based taxation rules that exist for international airlines;

2. Where no exemption is provided, reporting should account for the various practical issues highlighted in this Position Paper (e.g. what and where information should be required to be reported, what mechanisms should be developed for reporting purposes, etc.) and also be limited to information or data readily available to corporate management.

IATA acknowledges that there is a need to balance the usefulness of the information reported to tax administrators for risk assessment purposes and the compliance burden placed on taxpayers.

The information contained herein is intended to assist various Government departments and international organisations in understanding how airlines' currently report income for the purposes of paying tax, the information available to airlines to complete the country-by-country report and relevant transfer pricing Master and Local Files in order to both provide a rational basis for discussion between Government authorities and international airlines and also outline a consistent methodology for governments to adopt as it relates to reporting for the airline industry when designing and adopting country specific rules to implement Action Plan 13 of the OECD BEPS initiative.

This position paper was prepared by the Industry Taxation Working Group (ITWG), reporting to the Financial Committee of IATA.

BACKGROUND

BEPS addresses concerns over the ability of multinational corporations to minimize taxation through sophisticated tax planning, and thus reduce tax revenues in affected nations. The OECD's 15 action items (endorsed by the G20) target base erosion and profit shifting (BEPS) and are designed to limit untaxed or "stateless" income. Of particular and immediate concern to international airlines is Action 13 due to the specific characteristics of the airline sector, which recommends a three-tiered reporting regime for multinational firms to provide foreign governments with high level visibility into their international tax operations, including:

1. A country-by-country report submitted to the home country of a multinational firm;

2. A "Master File" submitted by a multinational in most instances to both the home country and also foreign regulators; and

3. A "Local File" filed by the multinational company with local tax authorities.

Generally, the Country-by-Country (CbC) report aims at providing a financial picture of a multinational enterprise (MNE) broken out by tax jurisdiction, the Master File is intended to provide a "high-level" blueprint of an MNE's global operations, and the Local File is intended to provide information on an MNE's operations in a specific tax jurisdiction.

Many nations are moving forward with implementing some or all of these reporting requirements, which will unavoidably affect many international airline companies. Indeed, many jurisdictions have now proposed regulations on country-by-country reporting and some foreign nations have already put such rules in place.

The Country-by-Country (CbC) Report

1. Action 13 recommends that MNEs file with their ultimate parent (or home country) tax authority, the country by country report, which shows the global allocation of its income and taxes paid and the tax jurisdictions of its economic activity. The CbC report includes three tables on income, tax and financial and additional economic activity among tax jurisdictions.

2. The CbC report includes, on a group-wide, per jurisdiction basis:
   A. Revenue, both:
      i) related-party (within the MNE group) and
      ii) unrelated-party (outside the MNE group), including:
         a. service
         b. royalty and
      iii) interest income
   B. Before tax profits
   C. Income tax paid on a cash basis
   D. Income tax accrued for the current year
   E. Stated capital
   F. Accumulated earnings
   G. Number of employees, and
   H. Tangible assets (other than cash and cash equivalents).

The CbC report as suggested by the OECD is depicted in a table in **Appendix 1** as an "Overview of allocation of income, taxes and business activities by tax jurisdiction".

The Master File

Action 13 also recommends that countries require MNEs to submit a "Master File," to "provide a high-level overview in order to place the MNE group's transfer pricing practices in their global economic, legal, financial and tax context." This "blueprint" of the MNE group will contain five categories of information:

1. The MNE group's organizational structure;
2. A description of the MNE's business or businesses;
3. The MNE's intangibles;
4. The MNE's intercompany financial activities; and
5. The MNE's financial and tax positions.

The Local File

The third tier of the new BEPS reporting regime is a "Local File" reporting requirement. While the Master File contains a high-level review of the MNE group, the Local File provides more detailed information relating to specific intercompany transactions and transfer pricing within a given tax jurisdiction.

Broadly, the Local File report requires three areas of information.

1. Descriptive information on the local entity, including the management structure of the local entity, a local organizational chart, a description of the individuals to whom local management reports, and a detailed description of the business and business strategy pursued by the local entity including any business restructurings or intangible transfers;

2. Information on transfer pricing, specifically, on controlled transactions involving the local group affiliate; and

3. Relevant financial information on the local affiliate.

The Local File will contain similar information traditionally included in transfer pricing documentation reports. Like the Master File, the Local File can be collected directly by foreign tax authorities but will ultimately depend on local legislation requirements.

The OECD did not recommend an implementation schedule for the Master and Local Files in the same manner as the CbC reporting requirement. However, several countries have already begun implementing requirements consistent with Master and Local Files reporting, requirements that could affect many airlines without specific exemption or more detailed guidance.

1. IATA RESPONSE

1.1 IATA is an association of world air transport enterprises operating scheduled air services under flags of countries eligible for membership in the International Civil Aviation Organization (ICAO). The stated purposes of IATA include the promotion of safe, regular and economical air transport for the benefit of the peoples of the world, the fostering of air commerce, and the study of related problems. IATA's Charter also commits it to cooperate with other international organisations, including ICAO and the United Nations. The membership of IATA, as shown in **Appendix 2**, represents some ~ 260 airlines or 83% of total air traffic in some ~ 130 countries (virtually every country around the globe).

1.2 IATA is concerned with the approach of certain States to taxation of income of international airlines serving these States. Our member companies' ability to conduct their air transport operations without facing crippling compliance burdens and multiple taxation risks depends almost entirely upon the consensus in favor of exclusively residence-based taxation of airlines' income from international traffic, as reflected in Article 8 (Shipping, inland waterways transport and air transport) of the UN Model Tax Convention and in the identical language of Article 8 of the OECD Model Tax Convention.

1.3 In contrast to IATA, ICAO is an intergovernmental organisation and the specialised agency of the United Nations concerned with international civil aviation. The Convention on International Civil Aviation of 1944 (Chicago Convention) sets out the charter of ICAO. Additional information regarding ICAO can be found in **Appendix 3**.

1.4 From the outset, it should be made clear that IATA and its members do not object to the payment of non-discriminatory, justly and equitably levied income taxes. They do however object most strenuously to taxes imposed, contrary to ICAO recommended practice, on gross receipts or turnover and to income taxes imposed on bases which do not take into account the profitability of the airline operations in that State. The industry respects fully the right of autonomous States to impose taxes, but the nature of international airline operations which form the network of global air commerce gives it a unique place in the economy of the States concerned.

1.5 Further, IATA supports the need for taxation transparency as a measure to aid in the prevention of BEPS activity. However, there is a need to balance the usefulness of the information reported to tax administrators for risk assessment purposes and the compliance burden placed on taxpayers.

1.6 Specifically, for the reasons elaborated on further in this report, IATA seeks official confirmation of the following:

- An exemption be provided to airlines from CbC and transfer pricing reporting where airline activities are limited to the transportation of passengers in international traffic or activities that are considered ancillary or incidental to such activities. In the event there is more than one airline within a group of companies, the proposed exemptions from CbC reporting should apply to each individual airline within the group. In the event there are groups of companies which include both airlines and entities whose primary business is non-airline activities, the proposed exemptions should apply to the airlines within the group; or
- Where an exemption is not provided, reporting should consider the various practical issues highlighted in this Position Paper and also be limited to information or data readily available to corporate management so that companies will not need to go through a time consuming and expensive process of constructing new purpose built data.

1.7 It is important to note that IATA has been actively involved since the beginning of the BEPS initiative with respect to engaging with the OECD on Action 13 in relation to transfer pricing documentation and CbC reporting. From the first communication between IATA and the OECD's Centre for Tax Policy and Administration in 2013 on Action 13, and several further submissions in relation to the various OECD memorandums and discussion drafts on this topic, IATA has continuously called for an exemption from CbC reporting for airlines with respect to income from international transport and related/ancillary services, where a tax treaty or similar bilateral agreement allocates taxing rights over such income to the country of residence and/or effective management of airlines.

1.8 Consequently, the exemptions sought in this Position Paper are consistent with IATA's prior communications and submissions to the OECD in an effort to ensure the CbC reporting requirements are compatible with the pre-existing provisions of the OECD's Model Tax Convention and existing international treaties/agreements and do not unnecessarily create burdensome compliance requirements for airlines.

2. BENEFITS OF INTERNATIONAL AIR TRANSPORT TO COUNTRIES IT SERVES

2.1 The impact of international air transport on national economies is considerable in terms of benefits directly and indirectly traceable to airline operations. The more significant benefits include income flow from expenditures and the income multiplier effect, employment, commercial and trade advantages brought by air connectivity, the speed of business air travel and air freight, tourism, improved communications, civil aircraft maintenance and overhaul, foreign exchange earnings and contributions to balance of payments. **Appendix 4** includes additional details on the significant economic and social benefits that are derived from international air transport.

3. INCOME TAX: RECIPROCAL EXEMPTION

3.1 ICAO has a longstanding policy and guidance material for States on the taxation of certain aspects of international air transport, namely: the taxation of aviation fuel, lubricants and other consumable technical supplies; airline income and aircraft and the sale and use of international air transport, such as on tickets, passengers and airline gross receipts. The ICAO Council has undertaken a number of revisions to the policies on taxation and in February 1999 adopted a consolidated resolution published in the Third Edition of Doc 8632, ICAO's Policies on Taxation in the Field of International Air Transport, issued in 2000. This document reaffirms and strengthens the principles underlying ICAO's policies in this field which, among other things, supported a policy of reciprocal exemption in respect of the income of international air transport enterprises, as outlined in **Appendix 5**.

3.2 In accordance with the ICAO Resolution, IATA's position is that the most reasonable and equitable means of dealing with income taxation in foreign States is on the basis of reciprocal exemption either by operation of income tax law, or by treaty.

3.3 Negotiation of full taxation treaties involves consideration of many factors and requires the ratification by the governments of both countries. However, in many States the income tax legislation makes provision for the exemption of profits from the operation of aircraft of a foreign country where that foreign State allows a reciprocal exemption. In these circumstances, the responsible Minister or the Commissioner of Taxation is empowered to enter into an agreement by an exchange of letters, or something equally simple.

3.4 The policy of including in treaties a reciprocal exemption for income from the operation of aircraft in international traffic dates back as far as the 1928 League of Nations Model Tax Convention. The rationale then was the same as it is today, namely recognition that for businesses operating in this sector, "lack of implementation of this rule of reciprocal exemption involves either multiple taxation or considerable difficulties of income allocation in a very large number of taxing jurisdictions."

3.5 In spite of the recommendations of ICAO, some States still do not provide for the reciprocal exemption of profits derived from the operation of foreign aircraft either pursuant to statutory provisions in the tax laws of the two States or by negotiation of tax treaties. Airlines from such States subsequently may be subject to income tax in other States when they come within the jurisdictional reach of those tax administrations.

3.6 In jurisdictions where there is no applicable tax treaty, airlines generally have to use a complicated calculation formula (i.e. Maritime, Calcutta or Massachusetts formulas) to allocate income (and expenses) to the particular non-treaty jurisdiction. This involves time consuming administrative work and compliance costs and is the basis for why Article 8 was inserted into the Model Tax Convention.

3.7 As ICAO has further noted, decisions in favor of reciprocal exemptions were made because "multiple taxation on the … income of international air transport, as well as taxes on its sale and use, were considered as major obstacles to further development of international air transport. Non-observance of the principle of reciprocal exemption envisaged in these policies was also seen as risking retaliatory action with adverse repercussions on international air transport, which plays a major role in the development and expansion of international trade and travel."

3.8 Airlines may engage in activities that do not fall within the exemption afforded by Article 8 or reciprocity, for example the transportation of passengers or freight wholly within a foreign territorial jurisdiction (i.e. not international transportation but domestic) where bilateral air services agreements allow such activity. Alternatively, an airline may incorporate an entity within a foreign jurisdiction to conduct related activities such as airline crew employment, ground handling, maintenance, holidays and tourism packages. Such activity is ordinarily immaterial for most airlines and exists to support the main activities of airline transportation. Any profits from such activities ordinarily are subject to taxation within the jurisdiction in which those activities are performed.

4. TRANSFER PRICING

4.1 In light of the extensive tax treaty network and the protections they afford in revenue preservation, and the regulatory requirements that airlines must meet simply in order to conduct flight operations, it is submitted that the airline industry is not generally susceptible to engaging in BEPS activity such as transfer pricing manipulation. Further, most airlines do not produce detailed profit and loss information by country.

4.2 Bilateral air service agreements (ASAs) between States (or groups of states) have emerged as the main way for engaging in international air transportation services. While there has been a lot of progress in opening up of air transport markets, ownership and control restrictions are a common feature of these agreements. As part of ASA agreements, Contracting States will designate their national airlines the right to operate flights between States. Most States specify limits on foreign ownership and control for their national airlines as well as often require comparable restrictions for carriers to be considered to be from the other ASA Contracting State. Airlines commonly need to exhibit characteristics of substantial ownership and effective control by State's nationals to be qualified for designation. The 'nationality' feature in the airline industry makes it very unlikely for BEPS issues to be of concern. While greater ownership and capital market liberalization has been supported by several key stakeholders in industry and some States, the practical reality is that a wide-spread liberalized approach to ownership and capital market liberalization is still some time away and unlikely to be seen in the short to medium term.

4.3 Airlines ordinarily structure their foreign operations within a branch structure in order to avail themselves of these legal, regulatory and taxation concessions. At times, where airlines seek to access bi-lateral air transportation rights they will be required to incorporate themselves within that foreign jurisdiction. In certain instances, such entities have certain foreign control requirements that could prevent the airline from holding more than a certain amount of ownership in that foreign entity. As a result, an airline's branch structure is established for bona fide operational purposes and not for the purpose of avoiding or mitigating taxation or BEPS related activities.

4.4 Airline profits from activities that are not ordinarily afforded Article 8 treaty exemption or reciprocity and therefore subject to taxation within jurisdictions that are foreign to the airline are not ordinarily material for most airlines. Where such activities exist they are subject to appropriate OECD transfer pricing principles.

5. COMPLIANCE COSTS

5.1 The OECD has highlighted the difficulty of reporting income for multinational groups. This difficulty is exacerbated for airlines, as in most instances the preparation of financial statements in non-home jurisdictions is not statutorily required or produced and often tax filings are not even required (for example, where an Article 8 treaty exemption is provided). The industry generally operates through an overseas local branch structure because of the regulatory requirements in order to conduct flight operations. There is often no requirement under the branch structure operated by airlines for local books and records to support statutory filings. Therefore, information is not ordinarily available to provide the country-by-country suggested reports.

5.2 For airlines to comply with country-by-country reporting requirements to disclose income and taxes will require substantial and very costly system changes. These changes to the way airlines currently operate will add another layer of administration cost and burden to an industry already operating on very narrow margins.

6. ACCOUNTING & REPORTING WITHIN THE INDUSTRY

6.1 All airlines from Member States are required to furnish annually to ICAO, the global operating results and statistics of the enterprise in a standard format. This takes the form of a profit and loss statement, a balance sheet and a statement of retained earnings (Form EF).

6.2 Each year these statistics and financial statements are published by ICAO online in www.ICAOdata.com, the subscription for which is on payment by the users. As a consequence, all international airlines maintain their accounts on substantially similar lines. The amortisation and depreciation policies adopted by each airline do not vary greatly from airline to airline due to similarity of operations and the aircraft and equipment utilised. The magnitude of operations carried on and the high standards of cooperation among airlines due to the influence of IATA can justify the statement that the accounting results published by member airlines are not only factual, but represent a high degree of standardisation of accounting techniques.

6.3 In addition, airline accounts are audited by independent outside auditors on a regular and continuous basis so that published statements can universally be accepted as accurate, fair and systematic reflections of the operating results of the airlines concerned.

6.4 The local office/branch of an international airline is not able to prepare accurate profit and loss accounts as all the revenue applicable to that office/branch does not accrue locally nor is all the expenditure attributable to that office/branch paid locally. Consequently there is a significant difference between the accounting operation of the local office/branch of an international airline and, for example, the local branch of a foreign manufacturer.

6.5 The international airline actually earns or produces its revenue mainly while flying over international territory or waters, and consequently, the full cost of operating aircraft used to derive the revenue is not incurred in any one country, nor are those expenses which are incurred in that country necessarily appropriately chargeable solely against the revenue attributable to that country. For example, the cost of fuel and meals uplifted in country A is not a cost of only the first segment flown out of A.

6.6 There is no adequate matching of costs unless the expenditure is apportioned partly to traffic joining the flight at A and partly to the traffic already on board. Therefore, the conventional method of preparing branch profit and loss accounts comprising identifiable local income and expenditure will not produce an accurate result when applied to the branch office of an international airline. Indeed, Article 8 has its genesis in the difficulties associated with trying to allocate profit to a particular jurisdiction.

7. USEFULNESS OF REPORTING

7.1 As highlighted above, the reporting of no or little corporate income tax paid in a particular country will be due to both the relevant income tax treaties and genuine economic conditions and not any BEPS activity.

7.2 The taxes paid by airlines are also not entirely comparable by country. In some jurisdictions, tax is levied on a gross receipts basis (for example, Philippines gross billings tax) and in others, such as where the income calculation formulas mentioned above are used, the starting point for the tax calculation may be worldwide profits with applicable adjustments. Certain tax treaties may also apply reduced tax rates based on the particular airline's place of management.

7.3 There may also be inconsistency between the various jurisdictions in determining the tax base in terms of defining the local jurisdiction income (for example, potential bases could be sales made in a country, sales with a leg starting in a country, or 50% of the round trip income sold for the country) and thereby further contributing to the difficulty of reporting in a particular jurisdiction. This is further complicated with the majority of sales now being online.

7.4 In light of the above and as a result of the treaty network, the value of any information provided in the same format as other industries might only serve to confuse readers of such information instead of enlighten.

7.5 Further, additional information to capture measures of economic activity other than income and taxes (such as revenue by location, stated capital, number of employees and location of tangible assets by country) are unlikely to be easily identified or readily accessible from airlines' existing business systems.

7.6 It is also considered that it is not clear that the provision of this information would better place revenue authorities in a position to effectively carry out risk assessments or provide revenue authorities with a meaningful measure of potential transfer pricing activity by airlines.

8. GUIDELINES FOR REPORTING: THE CASE FOR EXEMPTION

8.1 It is important to note that Paragraph 5 of the Revised OECD Chapter V Transfer Pricing Guidelines on Documentation states that the objectives of the transfer pricing documentation requirements are the following, including:

A *"to ensure that taxpayers give appropriate consideration to transfer pricing requirements in establishing prices and other conditions for transactions between associated enterprises and in reporting the income derived from such transactions in their tax returns;*

B *to provide tax administrations with the information necessary to conduct an informed transfer pricing risk assessment; and*

C *to provide tax administrations with useful information to employ in conducting an appropriately thorough audit of the transfer pricing practices of entities subject to tax in their jurisdiction, although it may be necessary to supplement the documentation with additional information as the audit progresses."*

As detailed in the following sections, requiring airlines to prepare and submit transfer pricing documentation and CbC reports will not meet nor assist in achieving these three objectives in order to better understand, control and address BEPS behaviour, as such behaviour does not exist, by means of the unique structural, regulatory and taxation framework of the airline industry.

8.2 At present, many of the jurisdictions that are in the process of implementing the CbC Reporting requirements as suggested by Action 13 have acknowledged that, in certain circumstances, it will be appropriate to provide exemptions from such reporting requirements (e.g., Australia, Singapore, USA).

8.3 IATA's position is that airlines should be exempt from producing:
a) CbC Reports;
b) Master Files; and
c) Local Files.

However, in the event there is more than one airline within a group of companies the aforementioned exemptions should apply to each individual airline within the group. In the event there are groups of companies which include both airlines and entities whose primary business is non-airline activities, these exemptions should apply to the airlines within the group.

8.4 Alternatively, the exemption to reporting would apply to a scenario where the majority of income from the airline is derived from international transportation that is afforded Article 8 (or a reciprocity) exemption in foreign jurisdictions (such that the income is only subject to home country taxation). The result being that only income that is subject to taxation in foreign jurisdictions would be required to be reported in the CbC Report.

8.5 Should no exemption be afforded to airlines then, at a minimum, airlines should report income according to the jurisdiction in which the airline pays corporate income tax on that income. In effect, this is similar to the above exemption but also requires income to be reported in the home jurisdiction (which may also include Article 8 income) in addition to the income that is subject to foreign taxation. This is supported within the OECD's own recommendations for CbC Reporting.

8.6 Paragraph 55, Action 13, Chapter V of the Revised OECD Transfer Pricing Guidelines on Documentation, reads as follows:

"E.2.2. Which MNE groups should be required to file Country-by-Country Report?

55. It is considered that no exemptions from filing the Country-by-Country report should be adopted apart from the exemptions outlined in this section. In particular, no special industry exemptions should be provided, no general exemption for investment funds should be provided, and no exemption for non-corporate entities or non-public corporate entities should be provided. Notwithstanding this conclusion, countries participating in the OECD/G20 BEPS Project agree that MNE groups with income derived from international transportation or transportation in inland waterways that is covered by treaty provisions that are specific to such income and under which the taxing rights on such income are allocated exclusively to one jurisdiction, should include the information required by the country-by-country template with respect to such income only against the name of the jurisdiction to which the relevant treaty provisions allocate these taxing rights."

9. GUIDELINES FOR REPORTING: WHERE NO RECOMMENDED EXEMPTION APPLIES

9.1 IATA's position is the following:

A. that airlines should be exempt from producing reports as indicated above; or

B. alternatively, where no exemption or only a partial exemption is found to apply, then only the CbC Report should be required to be produced by airlines and that an exemption to produce a transfer pricing Master File and Local File should be afforded by relevant countries as such reporting would most certainly be obvious (i.e. describe a high level airline operation and various in-country local operations such as ground handling, etc.) and not serve any meaningful purpose.

Consequently, we respectfully request that relevant jurisdictions provide official confirmation of the above exemptions within local jurisdictional guidelines or regulations.

9.2 Many jurisdictions in implementing OECD Action 13 dealing with reporting have already indicated that they will provide exemptions in certain circumstances. Please refer below to the discussion on Local File reporting.

9.3 It is IATA's understanding that the OECD only considered the implications of CbC Reporting to airlines and not the associated transfer pricing Master and Local File Reporting.

9.4 Had they done so then it is conceivable that the OECD may have also outlined special rules that might apply to the airline industry with respect to these reports as they did for CbC Reporting.

9.5 The following sections outline specific guidance relevant to completing the relevant reporting requirements of Action 13 should they be required to be completed by airlines with certain jurisdictions and not be afforded exemption. That is:

a) CbC Report
b) Local File
c) Master File

10. CbC REPORT

10.1 As highlighted above, the purpose of Article 8 is to avoid the need for airlines to arbitrarily allocate income and profits associated with airline travel to a particular jurisdiction. Consequently, and in relation to income derived from international transport, there are no transfer pricing implications associated with this allocation of income as such income is wholly allocated and taxed in one jurisdiction. Therefore, transfer pricing documentation and CbC reporting would not assist the respective tax administration with a risk assessment and audit procedures as detailed under the objectives of Paragraph 5 of the Revised Chapter V of the Transfer Pricing Guidelines on Documentation.

10.2 To illustrate this point, if an airline is subject to tax only in its home country on income earned in both its home country and also another country (for example, pursuant to Article 8 of a relevant treaty), then such income should not be required to be reported in the other country. It would be most peculiar to report 100% of an airline's tax as paid in the airline's home country (country of residence) due to Article 8 but be required to arbitrarily report the income, assets and employees of that airline in both the home country and also the countries in which the airline flies to and which offer Article 8 relief pursuant to the home country's double tax treaty network.

10.3 On the other hand, if income earned in a non-treaty country is subject to tax in that non-treaty country (for example, some countries do not provide Article 8 treaty relief or certain income might not qualify as Article 8 income), then such income should be separately reported for that non-treaty country and not be required to be reported in both jurisdictions.

10.4 Thus, the guiding principle should be that an airline only has local reporting obligations in relation to countries where tax is paid in that local country. This would in turn be largely driven by the existence or not of a treaty network. This treatment is supported by Paragraph 34 of Chapter V of the Revised OECD Transfer Pricing Guidelines on Documentation which states:

"For purposes of Annex III to Chapter V of these Guidelines, the Country-by-Country Report should include all tax jurisdictions in which the MNE group has an entity resident for tax purposes"

10.5 In many instances where an airline's income is derived solely from international transport in a foreign jurisdiction and which is treaty protected, the airline is not a local tax resident and as such, is not required to complete and file a local tax return.

10.6 Where the CbC report is required to be completed by airlines then clear guidance will be required for how any additional information should be reported.

Definitions

10.7 Definitional problems are going to exist and in a manner that is unique for the airline industry. For example, what is revenue? How is the term "Revenue" defined and how should it be allocated to specific countries.

Revenue challenges?

10.8 "Sales" are not equal to "Revenue" and "Revenue" is not equal to "Profits".

10.9 The OECD requires that Revenue be disclosed in the CbC Report by MNEs.

10.10 As described above, and supported by the OECD guidance, it would be IATA's opinion that airlines would be best served including all income that they derive as relating to their home jurisdiction unless that income has been subject to taxation in another jurisdiction.

10.11 Ordinarily airlines use one of the acceptable meth odologies to determine the amount of income referable to a jurisdiction when calculating the amount of taxation to be borne in that jurisdiction (refer to **Appendix 6** for further details) where that airline income is not subject to Article 8 of a relevant tax treaty.

10.12 It would seem appropriate for an airline to only report as Unrelated Party Revenue in a Tax Jurisdiction (other than the airline's home tax jurisdiction) that income reported by the airline in the foreign tax jurisdictions tax return that gave rise to the foreign income tax to ensure consistency, avoid confusion and remove any additional compliance burden on airlines to do otherwise.

10.13 In certain tax jurisdictions taxation is levied on gross receipts and not profits. For example, the Philippines Gross Billings Tax. Again, it would be IATA's preferred view that such income be reported on the same basis that the relevant income tax is calculated. The alternate position is that such revenue and taxation is not reported at all – on the basis that accepted transfer pricing principles would not support the taxation of gross receipts.

Stated Capital and Accumulated Earnings?

10.14 "Stated Capital" in the foreign location should be nil as all capital would be in the airline's home country unless the airline group holds a foreign local subsidiary with equity injected within that foreign location, in which case the Stated Capital would report that equity injection with the CbC report for that tax jurisdiction.

10.15 "Accumulated Earnings" – would again only be reported in the home country tax jurisdiction, reflecting the MNE's retained earnings unless that airline Group held a foreign subsidiary holding retained earnings in a foreign tax jurisdiction that had been subject to foreign taxation, in which case it would also report such retained earnings in that foreign tax jurisdiction.

10.16 "Employee Numbers" should only be reported in the home country where those employee activities solely give rise to home country taxation. That is, all employee numbers – both home country and foreign based employees would be included in the airlines home country tax jurisdiction within the CbC report where those employees derived Article 8 income. Further, from a practical perspective, an airline would include only foreign local employees (residents) in a foreign tax jurisdiction, where those employees give rise to a tax obligation in that foreign tax jurisdiction and exclude cabin crew unless that crew were solely carrying on domestic operations in that foreign jurisdiction. To do otherwise, would necessitate an arbitrary allocation of crew between jurisdictions that is not done or required for any other purpose.

10.17 "Tangible Assets" should also exclude aircraft, aircraft equipment and/or parts kept in bonded warehouses. Alternatively, such assets should similarly be reported in an airlines home jurisdiction unless such aircraft derived income from foreign domestic flights (i.e. wholly within a territory) and no aircraft allocation would be required on an arbitrary basis even where income is subject to foreign taxation due, for example, to no Article 8 tax treaty in that tax jurisdiction.

10.18 In summary, if all income derived from international transportation in a foreign jurisdiction is protected by a treaty it should be reported only in the home jurisdiction. Therefore elements related to that income such as foreign employees and foreign assets for the country protected by treaty provisions would need to all be included in the home jurisdiction (not in the foreign jurisdiction).

10.19 The reference to "Treaty provisions" is large and includes any other type of treaty, such as bi-lateral air services agreements, if there is a tax provision contemplating that income would be taxed only in the home jurisdiction.

10.20 A foreign jurisdiction should not request information for their particular foreign jurisdiction that relates to income that was treaty protected and therefore not reported distinctively.

10.21 Airlines should report all employees and assets in the home jurisdiction (despite some of them being located in other jurisdictions) to the extent that those employees or assets are generating income which is Article 8 protected and reported only in the home jurisdiction. Failure to clearly articulate this would be counter to the OECD's objectives of transfer pricing documentation and CbC reporting requirements as described under Section 8.1 above.

10.22 IATA reiterates that in attempting to allocate income and other information to foreign jurisdictions it may only serve to create misunderstanding and confusion. As such, we would request that airlines be exempt from reporting income and the other additional information.

10.23 Again, we would repeat that airline and shipping activities do not constitute "BEPS activity" and such reporting of the information requested within the CbC Report would not be helpful to revenue authorities. In addition, where such information is required, there is a risk that some jurisdictions might seek to challenge or disturb the Article 8 treatment.

10.24 As a result of Article 8 treaty allocation, many airlines do not maintain records that could be used to complete the proposed template set out on Table 1 of Annex III to Chapter V Documentation. Should reporting be required then airlines would incur significant costs to report such information as it is not currently recorded by airlines and the level of system configuration would be substantial.

10.25 In our view the practical difficulties, associated with an airline having to satisfy CbC reporting requirements, only serve to support our contention that it would be appropriate to provide an exemption from CbC reporting, for airlines and shipping companies, associated with (Article 8 income) profits from the operation of ships and aircraft for the international transportation of passengers and freight.

11. Master File

11.1 Action 13 also recommends that countries require MNEs to submit a "Master File," to "provide a high-level overview in order to place the MNE group's transfer pricing practices in their global economic, legal, financial and tax context."

11.2 A Master File provides a high level description of a MNE's global business operations, including an outline of its organisational structure and use of intangibles and intercompany financial activities.

11.3 Airline operations should be obvious and the airline's structure would already be known to regulators and available in audited public financial statements.

11.4 In the vast majority of cases, a Master File is not going to say anything that would be helpful to a regulator from a transfer pricing perspective.

11.5 Unless an airline has significant non-airline operations then it would be IATA's strong recommendation that regulators not seek airlines to prepare a Master File as the cost to do so will be substantial, while not providing any meaningful information to readers of the information.

11.6 It follows that only significant non-airline activities should be recorded in a Master File. Given the majority of airlines only carry out airline-related activities then it would not be expected that a Master File would be required.

11.7 Should an airline be required to prepare a Master File then no specific guidance is apparent to IATA that would be unique to the airline industry.

12. Local File

12.1 As set out above, we reiterate that there should be a special exemption from CbC reporting requirements including the need to produce transfer pricing Local File reporting, in relation to Article 8 airline and shipping income provided a treaty network, a reciprocal note or a local law exemption exists.

12.2 Many jurisdictions have already provided guidance and regulations on the requirements for Local File transfer pricing reporting. Such guidance ordinarily mirrors the requirements for transfer pricing that applied under the relevant jurisdiction's local transfer pricing rules.

12.3 Some jurisdictions have acknowledged that the Local File rules only operate in the context of Parent – Subsidiary groups and not Company – Branch office relationships.

12.4 Where the Local File requirements do not apply to a company and its own branch in a foreign jurisdiction then it is likely that the Local File requirements will not apply to most airlines as, has already been highlighted, most airlines only conduct themselves through a branch legal structure.

12.5 Airlines would therefore only have a Local File obligation under this interpretation where an airline holds subsidiaries offshore and only where such subsidiaries carry on activities that are not protected by Article 8.

12.6 The majority of IATA member airlines only have Article 8 income (therefore such income should be covered by the relevant treaty provision) and do not have entities/subsidiaries that carry on activities that are unrelated to or not ancillary to aircraft operations (such as hotels, manufacturing and production, financial services, etc.).

12.7 Very few airlines would conduct activities that would not be considered as Article 8 income. Any reporting would therefore only likely relate to scenarios where a jurisdiction does not provide Article 8 treaty relief. The profit methodology used to allocate taxing rights and levy taxation would therefore likely be determined by using one of the profit methodologies for allocating airline related activities to a relevant jurisdiction, such as: the Maritime, the Calcutta or the Massachusetts formulae (refer to a separate guide issued by IATA that sets out how airlines should allocate income to foreign jurisdictions where no Article 8 exemption applies). These allocation formulas incorporate transfer pricing principles in terms of apportioning revenues and expenses in an arm's length manner and for purposes of calculating local taxable income in the territory in question.

12.8 As a result of Article 8, it is not appropriate or possible for airlines (or shipping entities) to provide the information outlined without a substantial increase in compliance, administrative and system costs given such information is not currently required to be captured.

12.9 Furthermore, as stated in our previous submissions to the OECD, we do not believe such information would serve any meaningful purpose but rather may confuse or misrepresent BEPS activity where none exists.

12.10 Paragraph 42 of Chapter V of the Revised OECD Transfer Pricing Guidelines on Documentation states:

"Care should be taken not to impose a documentation-related penalty on a taxpayer for failing to submit data to which the MNE did not have access."

Concessional Reporting Requirements

12.11 A further observation is that many jurisdictions are providing exemptions or concessions to companies when completing the Local File such that in some instances (such as not reaching a certain level of materiality) nothing is required to be prepared and in other circumstances (where certain conditions are met), only limited information is required to be produced for the Local File.

12.12 It would be appropriate to envisage a limited form of reporting is required, if any reporting is required at all, having regard to the above reasons and the fact that transfer pricing issues, if any, would not be material to airlines.

12.13 As an example, of concessional reporting, in some jurisdictions (like China and Australia), the Local File is only required where a minimum materiality level is reached with respect to international related party dealings (IRPDs) or certain IRPDS as defined. Furthermore, in some limited cases, entities are only required to produce a shortened version of guidance to the regulator.

12.14 An example of a Local File - short form guidance: Local entity description

Description of the organizational structure for the entity or the foreign entity's business operations carried on through its local permanent establishment (PE) and the reporting lines to offshore personnel from the management of the entity or the foreign entity's business operations carried on through its local PE.

Description of the business and the business strategy of the entity or the foreign entity's business operations carried on through its local PE.

Description of business restructurings affecting the entity (or the foreign entity's business operations carried on through its local PE) in the present and previous year and an explanation of its significance.

Description of any transfer(s) of intangibles involving or affecting the entity (or the foreign entity's business operations carried on through its local PE) in the present and previous year and an explanation of its significance.

The 'key competitors' of the entity or the foreign entity's business operations carried on through its local PE.

12.15 Where a MNE does not fit within the short form reporting criteria then it may have to produce further information (such as a simplified report) but not a full report where it satisfies certain criteria.

That is the Simplified Report is required where a MNE does not meet the eligibility criteria for the Short Form Local File; and the entity was not or is not currently subject to an Active Compliance Activity in relation to its IRPDs; and the entity, or the foreign entity's business operations carried on through its local PE are not material.

12.16 Where one does not meet the criteria for either the Short Form Local File or the Simplified Local File then a Full Local File would be required.

12.17 A Full Local File would include the information in the Short Form and Simplified Local File, plus for each agreement with international related parties, excluding agreements of the kind on an 'exclusion list ':

- Transfer pricing method relied on for agreement and an assessment of the arm's length nature of the transaction(s)
- The arm's length conditions for the agreement
- The records maintained by the reporting entity for the agreement

13. OTHER COMMENTS

13.1 IATA would support transitional arrangements that defer the creation of any Master File or Local File for MNEs until the MNEs Home jurisdiction has implemented rules dealing with CbC reporting, Master File and Local File obligations.

13.2 IATA supports providing MNE's the choice of either local country language or English for the purpose of producing the Master File and Local File transfer pricing documentation.

13.3 IATA supports the OECD 2020 review to ensure the proposed Action Plan is meeting the objectives of the BEPS initiative.

13.4 IATA also supports wherever possible that countries utilise the Master File and Local File transfer pricing reporting requirements rather than creating alternate or additional reporting requirements on MNEs.

14. CONCLUSION

14.1 IATA supports a uniform (and if possible airline industry tailor-made) approach across jurisdictions as being far preferable to every country developing its own reporting requirements. That is a clear framework should be created that takes account of the peculiarities of the airline industry is imperative.

14.2 Article 8 of the OECD Model Tax Convention already provides for special treatment of profits from international air transport to only be taxed in airlines' home countries. In our opinion, this legitimately calls for the OECD (and member countries) to align its BEPS Action Plan to the Model Convention and include similar special treatment for the airline industry.

14.3 Article 8 (shipping, inland waterways transport and air transport) of the UN Model Tax Convention and the identical language of Article 8 of the OECD Model Tax Convention provides exclusive residence-based taxation of airlines' income from international traffic. On this basis IATA and its members believe there is sufficient grounds for an airline industry wide exemption from CbC reporting requirements in relation to Article 8 airline income provided a treaty network, a reciprocal note or a local law exemption exists. It is the submission of IATA that the purpose of Article 8 is to avoid the need for airlines to arbitrarily allocate income and profits associated with airline travel to a particular jurisdiction. Any CbC reporting should ensure this premise continues.

14.4 Failing the achievement of an exemption for Article 8 income, we set out guidance as to how an airline should complete the CbC Report, the Master and Local Files with respect to Article 8 income, related taxes and additional information. Specifically, in the event that airlines would be required to provide such information, they should only be required to do so for countries where a treaty network, a reciprocal note or a local law exemption does not exist and, thus, limited to local reporting where a foreign tax liability arises. That is, airlines should not need to include information for jurisdictions where all income is subject to Article 8 provisions and reported in the home jurisdiction.

14.5 It is considered that the provision of additional information would not better place revenue authorities in a position to effectively carry out risk assessments or provide revenue authorities with a meaningful measure of potential transfer pricing activity by airlines. It is considered that provision of the information in the format proposed will confuse instead of providing transparency and would directly contradict the stated objectives associated with transfer pricing documentation and CbC reporting requirements.

14.6 It is our view the practical difficulties, associated with an airline having to satisfy country-by-country reporting requirements, only serve to support our contention that it would be appropriate to provide an exemption from country-by-country reporting, for airlines, associated with (Article 8 income) profits from the operation of aircraft for the international transportation of passengers and freight.

14.7 In light of the above, it is requested that official confirmation be provided, within relevant jurisdictions local reporting requirements, as to the treatment of the airline industry, and the associated income from international traffic, with respect to the completion of the CbC Report, the Master File and Local File.

IATA appreciates the opportunity to provide these comments to jurisdictions implementing Action 13 within their local laws, regulations and guidelines and looks forward to further consultation and discussions on this important matter in order to address the airline industry's concerns.

APPENDIX 1

Name of the MNE group:
Fiscal year concerned:
Currency used:

Tax Jurisdiction	Revenues			Profit (Loss) before Income Tax	Income Tax Paid (on Cash Basis)	Income Tax Accrued – Current Year	Stated Capital	Accumulated Earnings	Number of Employees	Tangible Assets other than Cash and Cash Equivalents
	Unrelated Party	Related Party	Total							

APPENDIX 2

ABSA Cargo Airline
Adria Airways
Aegean Airlines
Aer Lingus
Aero Contractors
Aero República
Aeroflot
Aerolineas Argentinas
Aerolineas Galapagos S.A. Aerogal
Aeromexico
Afriqiyah Airways
Aigle Azur
Air Algerie
Air Arabia
Air Astana
Air Austral
Air Baltic
Air Berlin
Air Botswana
Air Burkina
Air Cairo
Air Caledonie
Air Canada
Air China Limited
Air Corsica
Air Europa
Air France
Air India
Air Koryo
Air Macau
Air Madagascar
Air Malta
Air Mauritius
Air Moldova
Air Namibia
Air New Zealand
Air Niugini
Air Nostrum
Air SERBIA a.d.Beograd
Air Seychelles
Air Tahiti
Air Tahiti Nui
Air Transat
AirBridgeCargo Airlines
Aircalin
Airlink
Alaska Airlines
Alitalia
All Nippon Airways
Allied Air
AlMasria Universal Airlines
ALS
American Airlines
Arik Air
Arkia Israeli Airlines
Asiana
Atlas Air
Atlasjet Airlines
Austral
Austrian
AVIANCA
Avianca Brasil
Azerbaijan Airlines
Azul Brazilian Airlines
Bahamasair
Bangkok Air
Belavia - Belarusian Airlines
BH AIR
Biman
Binter Canarias
Blue Air
Blue Panorama
Blue1
bmi Regional
Boliviana de Aviación - BoA
Braathens Regional Aviation AB
British Airways
Brussels Airlines
Bulgaria air
C.A.L. Cargo Airlines
Camair-Co
Capital Airlines
Cargojet Airways
Cargolux S.A.
Caribbean Airlines
Carpatair
Cathay Pacific
China Airlines
China Cargo Airlines
China Eastern
China Postal Airlines
China Southern Airlines
CityJet
Comair
Condor
COPA Airlines
Corendon Airlines
Corsair International
Croatia Airlines
Cubana
Czech Airlines
Delta Air Lines
DHL Air
DHL Aviation
Dniproavia
Donavia
Dragonair
Egyptair
EL AL
Emirates
Ethiopian Airlines
Etihad Airways
Euroatlantic Airways
European Air Transport
Eurowings
EVA Air
Federal Express
Fiji Airways
Finnair
flybe
flydubai
Freebird Airlines
Garuda
Georgian Airways
Germania
Gulf Air
Hahn Air
Hainan Airlines
Hawaiian Airlines
Hi Fly
Hong Kong Airlines
Hong Kong Express Airways
IBERIA
Icelandair
InselAir
Interjet
Iran Air
Iran Aseman Airlines
Israir
Japan Airlines
Jazeera Airways
Jet Airways
Jet Lite (India)
JetBlue
Jordan Aviation
JSC Nordavia-RA
Juneyao Airlines
Kenya Airways
Kish Air
KLM
Korean Air
Kuwait Airways
LACSA
LAM
Lan Airlines
Lan Argentina
Lan Cargo
Lan Colombia Airlines
Lan Perú
LanEcuador
LIAT Airlines
LLC "NORD WIND"

APPENDIX 2

LOT Polish Airlines
Lucky Air
Lufthansa
Lufthansa Cargo
Lufthansa CityLine
Luxair
Mahan Air
Malaysia Airlines
Mandarin Airlines
Martinair Cargo
MAS AIR
MEA
Meridiana fly
MIAT
Mistral Air
Montenegro Airlines
Myanmar Airways International
Nesma Airlines
Nextjet
NIKI
Nile Air
Nippon Cargo Airlines (NCA)
Nouvelair
Okay Airways
Olympic Air
Oman Air
Onur Air
Orenair
Pegasus Airlines
PGA-Portugália Airlines
Philippine Airlines
PIA
Precision Air
PrivatAir
Qantas
Qatar Airways
Rossiya Airlines
Royal Air Maroc
Royal Brunei
Royal Jordanian
RwandAir
S7 Airlines
SAA
Safair
Safi Airways
Santa Barbara
SAS
SATA Air Açores
SATA Internacional
Saudi Arabian Airlines
Shandong Airlines
Shanghai Airlines
Shenzhen Airlines
SIA
SIA Cargo
Sichuan Airlines
Silk Way West Airlines
Silkair
SKY Airline
South African Express Airways
SriLankan
SunExpress
Surinam Airways
SWISS
Syrianair
TAAG - Angola Airlines
TACA
TACA Peru
TACV Cabo Verde Airlines
TAM - Transportes Aéreos del
Mercosur Sociedad Anónima
TAM Linhas Aéreas
TAME - Linea Aérea del Ecuador
TAP Portugal
TAROM S.A.
Tassili Airlines
Thai Airways International
THY - Turkish Airlines
Tianjin Airlines
TNT Airways S.A.
TransAsia Airways
TUIfly
Tunis Air
T'way Air
Ukraine International Airlines
United Airlines
UPS Airlines
Ural Airlines
UTair
Uzbekistan Airways
Vietnam Airlines
Virgin Atlantic
Virgin Australia
VLM Airlines
Volaris
Volga-Dnepr Airlines
VRG Linhas Aéreas S.A. - Grupo
GOL
Vueling
Wamos Air
Westjet
White Coloured by You
Wideroe
Xiamen Airlines
Yemenia

APPENDIX 3

INTERNATIONAL CIVIL AVIATION ORGANIZATION

In contrast to IATA, ICAO is an intergovernmental organisation and the specialised agency of the United Nations concerned with international civil aviation. The Convention on International Civil Aviation of 1944 (Chicago Convention) sets out the charter of ICAO.

ICAO works with its Member States and industry groups to reach consensus on international civil aviation Standards and Recommended Practices and policies in support of a safe, efficient, secure, economically sustainable and environmentally responsible civil aviation sector. Additionally, ICAO also coordinates assistance and capacity building for States in support of numerous aviation development objectives; produces global plans to coordinate multilateral strategic progress for safety and air navigation; and monitors and reports on numerous air transport sector performance metrics.
Source: http://www.icao.int/about-icao/Pages/default.aspx

The Chicago Convention therefore recognised from the beginning the need for improving the facilitation of international air transport by removing obstacles to free and unimpeded passage of aircraft, passengers, crews, baggage, cargo and mail across international boundaries.

The purpose of such facilitation is twofold. First to enable air commerce to take full advantage of the pre-eminent speed of the airplane as a medium of transportation and to prevent it from being hampered by excessive delays for documentation and other border-crossing requirements. Secondly, to avoid the imposition by individual countries of onerous burdens on international airlines in the form of taxation, insurance requirements, user charges, and the like, so that the benefits of air transport could be extended to all States served as economically as possible.

Neither the Chicago Convention nor bilateral air services agreements negotiated between States release international airlines from compliance with all of the normal legal and commercial obligations of a foreign enterprise in that State, e.g. company qualifications, registrations and taxes.

The problems of operating in a foreign country are numerous. They include the provision of adequate fuel supplies, the availability of on-board meals for departing passengers, the availability of hotel accommodation in case of aircraft delay, the remittance of proceeds of ticket sales free of exchange restrictions and the employment of qualified experts to service the aircraft and to administer the ground facilities.

The impression that international airlines do substantial business within States they serve is often misleading and inaccurate as the business they conduct in foreign States is incidental and ancillary to their primary international function. International airlines operate in the long term at lower margins of profit than most other businesses and differ materially from foreign business enterprises which engage in manufacturing, merchandising, natural resources extraction or other activities involving substantial internal presence in the States where they are located and operate. Indeed, it is understood that many airlines often trade at margins that rarely meet, let alone exceed, their cost of capital and that the industry has barriers to entry, being high capital costs.

APPENDIX 4

BENEFITS OF INTERNATIONAL AIR TRANSPORT TO COUNTRIES IT SERVES

The impact of international air transport on national economies is considerable in terms of benefits directly and indirectly traceable to airline operations. Specifically, these benefits can generally be categorized as follows, including: the income multiplier effect, employment and productivity, tourism and trade, and other benefits.

Each of these benefits derived from international air transport is elaborated on in additional detail below.

Income Multiplier Effect

Expenditures by airlines, airports, and their staff and airlines' passengers generate further far-reaching income flow through the multiplier process. Airlines and airports pay salaries and wages to their employees, purchase equipment, supplies and services, and pay taxes (such as ticket taxes) and make other payments to governments. Similarly, air passengers purchase goods and services in the countries or cities they visit and these all have multiplier effects.

These income flows give rise to secondary expenditures by airline and airport employees, hotels, restaurants, travel agents, freight forwarders, insurance companies, governments and other industries from which goods and services are purchased, and these too have multiplier effects on the economy. In this way, successive rounds of income and expenditure are generated by the expenditures of airlines and airports and their passengers that have an impact throughout the economy.

Employment and Productivity

One of the most significant advantages of international air transport is the way it acts as a generator of employment, directly and indirectly. Air transport, and to a greater extent the service industries it supports, are labour intensive and their importance as generators of employment is increasing. Worldwide, the scheduled airlines directly employ 2.27 million people and, in addition, airline expenditures and activities, directly and indirectly, generate employment for many millions more. (Source: http://aviationbenefits.org/media/26786/ATAG__AviationBenefits2014_FULL_LowRes.pdf)

As a result of air transport, companies can expand their customer base and benefit from economies of scale and reduced unit costs. Air transport can, in many instances, result in the agglomeration of economic activities in and around airport regions, where companies can benefit from enhanced productivity resulting from pooled labour markets, knowledge sharing and spill overs. According to InterVISTAS (2015), a consultancy, a 10 percent growth in connectivity by air is associated with a 0.5 percent growth in GDP per capita at the national level in Europe.

Tourism and Trade

Tourism plays a significant part in international trade, and international air transport has made an enormous contribution to this development and connecting tourists with their respective destinations. Improved airline services and the availability of attractive air fares to the travelling public have been important factors in this development. Larger and fuel efficient aircraft have made an important contribution by enabling people to travel long distances quickly and by making shorter and more frequent visits possible.

One recent empirical study by PwC (2014) found that in the UK, a 10 percent increase in seat capacity resulted in a four percent increase in inbound tourist levels and a three percent increase in outbound levels. The resulting spending by tourists has a strong regional and local impact, since the service industries required by tourists employ many persons. This impact comes from spending for hotel and accommodation, restaurant meals, travel agents and tour operators, local transport including taxi and car rentals, and other products and services purchased. In turn, these service industries purchase a wide range of products and services in these countries. Thus the benefits of tourist spending flow rapidly into the general economy.

Certain expenditure by the tourist service industries is also made on imported goods and services, thereby stimulating international trade.

By assisting in the development of tourism and foreign trade, the airlines can make an important contribution to balance of payments positions and foreign currency earnings. Airlines are often important earners of foreign exchange in their own right. The existence of good air services also enhances the attractiveness of a country for commercial and industrial interests because of communications and trade advantages. This benefit is of considerable significance in attracting foreign investment and in creating new foreign trade opportunities.

Other Benefits of International Air Transport

Further expenditure and income flows are produced by capital investment, expenditure on fuel, rents, interest, insurance, taxes and many other items. Since civil air transport requires a high rate of investment in aircraft and aviation infrastructure this has also produced beneficial effects on economic growth.

APPENDIX 5

EXTRACT OF COUNCIL RESOLUTION OF 24 FEBRUARY 1999 WITH RESPECT TO THE TAXATION OF INCOME OF INTERNATIONAL AIR TRANSPORT ENTERPRISES AND TAXATION OF AIRCRAFT AND OTHER MOVABLE PROPERTY

… Whereas **with respect to the taxation of income of international air transport enterprises and aircraft and other movable property:**

a) multiple taxation of the earnings of international air transport enterprises and of aircraft and other movable property associated with the operation of aircraft engaged in international air transport can be effectively prevented by the reciprocal agreement of States to limit taxation in these two fields to the State in which any such enterprise has its fiscal domicile;

b) for international air transport enterprises lack of implementation of this rule of reciprocal exemption involves either multiple taxation or considerable difficulties of income allocation in a very large number of taxing jurisdictions; and

c) such exemptions have already been widely obtained, for example, through the inclusion of appropriate provisions in bilateral agreements aimed at avoidance of multiple taxation generally or in those dealing with the exchange of commercial air transport rights or through individual States adopting legislation which grants the exemption to any other State that provides reciprocity;

… The Council resolves that:

… 2. With **respect to the taxation of income of international air transport enterprises and taxation of aircraft and other moveable property:**

a) each Contracting State shall, to the fullest possible extent, grant reciprocally:

- exemption from taxation on the income of air transport enterprises of other Contracting States derived in that Contracting State from the operation of aircraft in international air transport; and

- exemption of air transport enterprises of other Contracting States from property taxes, and capital levies or other similar taxes, on aircraft and other moveable property associated with the operation of aircraft in international air transport;

b) the “taxation” and “taxes” referred to in a) i) and ii) shall include taxes levied by any national or local taxing authority within a State;

c) each Contracting State shall endeavour to give effect to Clause a) above, by the bilateral negotiation of agreements relating to double taxation generally, or by such other methods as the inclusion of appropriate provisions in bilateral agreements for the exchange of commercial air transport rights, or by legislation granting such exemption to any other State that provides reciprocity; and

d) each Contracting State shall take all feasible measures to avoid delays in any bilateral negotiations found necessary to achieve implementation of Clause a) above.

APPENDIX 6

WHAT IS THE DEFINTION OF REVENUE FOR AN AIRLINE

Where there is no tax exemption most jurisdictions allow for the taxation of international airlines on a net income basis.

IATA recognises that the amount of net income derived from any particular State by an international airline, and consequently the income tax payable in respect of that income, may be challenging to determine.

On the one hand, the majority of the distance flown by international airlines is outside the territorial jurisdiction of the State seeking to impose an income tax and therefore it is questionable whether that State has the right to impose income tax on revenues earned outside its jurisdiction.

On the other hand, by normal international fiscal standards, airlines operating to and from one State are often considered to have a branch under domestic tax laws or permanent establishment as defined in most double taxation treaties, and that establishment could expect to come within the jurisdiction of that State.

Operation of an airline to and from one State in its global network has an economic effect on its operations in every other State of its network and vice versa. It has therefore been considered by most tax administrations and by the airlines themselves that apportionment formulas provide a reasonable base on which to levy net income tax in States other than the State of fiscal domicile. As mentioned below, IATA produces another Position Paper, which is publicly accessible on its website (http://www.iata.org/policy/Documents/taxation_intl_air_transport%20profits_final.pdf) that provides an overview of several generally accepted net income apportionment formulas.

Any State which levies tax generally on a net income basis, should allow international airlines doing business within its jurisdiction to apportion expenses and other charges incurred during the year against the revenue derived in that same period. This permits a reasonable determination of the taxable net income of the international airline within the taxing State.

In contrast, taxation based on deemed profit or as a percentage of gross revenue has no relationship to operating profit, could result in double taxation and is discriminatory and regressive. IATA cannot proffer or endorse these methods of taxation.

Further, where the use of net income apportionment formulas by international airlines operating in a State other than the State of fiscal domicile generates a loss for any fiscal period, a carry forward of the resulting loss should be allowed in accordance with that State's domestic tax law provisions on utilisation of trading losses. The nature of international airline profits is highly cyclical due to a number of market forces including competition and the overall economies of the States served. By allowing loss carry forwards the State recognises that airline investments in personnel and infrastructure made in one fiscal period will benefit the State over many periods.

Consideration of some elements of a net income formula

In an effort to determine the net operating profit or loss of an international airline in any State IATA recommends the use of net income formulas for the apportionment of the global operating results. IATA produces another Position Paper that sets out how airlines should allocate income to foreign jurisdictions where no Article 8 exemption exists.

However, as a guide, the following must be considered when applying net income formulas:

A. Global Net Air Transportation Profit

IATA believes the global net air transportation profit in published financial statements of international airlines should be used for determining apportioned local net profit. The use of the published accounts is recommended because these are available in the public domain and are subject to audit by independent professional auditors.

The advantages to the revenue authorities of adopting the published accounts are considerable:

- Figures are easily authenticated.
- The impracticability of adjusting for every minor difference in tax and book treatment is avoided.
- Any differences between the taxable net income assessed by any State and the accounting profit of the airline are substantially eliminated over the course of time.
- Using the published accounts of the international airline instead of other more complicated methods saves considerable time and administrative effort for both the airline and the taxing State while preserving the tax collected.

IATA accepts that some States may choose to apply tax adjustments to published results, for example, to recognise the difference between book and tax depreciation.

B. Local Revenue

The calculation of the gross revenue derived in a country will have a bearing on the amount of income tax payable after application of one of the apportionment formulas.

Some tax administrations assume that airlines derive their traffic revenue in the same manner as shipping companies, i.e. all local sales represent revenue of the selling airline.

There is a significant difference between the derivation of revenue by shipping companies and airlines due to 'interline' agreements and the free negotiability of IATA documentation amongst members which allows passengers to purchase, almost anywhere in the world, travel on any number of airlines as required to get them to their destination. For instance:

- Under the auspices of IATA, interline traffic agreements between airlines provide one airline with the facility to issue its own tickets for travel on another of any number of IATA airlines. For this reason a standard format of flight coupon is used by all IATA airlines including electronic tickets. Additionally, IATA tickets are freely interchangeable unless the class of travel paid for happens to be one restricted to the issuing airline only, e.g. some charter or inclusive tour fares.
- The carrying airline has a legal right to the revenue applicable to its carriage less a standard rate of commission. The selling airline only retains so much of the total sale value of the original transaction as it actually carries, plus the commission received on the balance.
- Where the ticket is sold by a travel agent, the selling airline only retains the portion of the total sale actually carried less the agent's commission on that portion.

All this necessarily imposes on each airline a high degree of standardisation of accounting processes, enabling the pro-ration of the total fare paid by passengers among participating airlines. This can only be accomplished at a central accounting office, requiring highly sophisticated data processing capabilities. Much the same considerations apply to cargo shipments although usually the itinerary agreed at point of origin remains fixed.

Because of the foregoing, it is clear that total local receipts for sales of tickets rarely equals the actual local revenue of the airline issuing the ticket in any State.

In addition, gross revenue, as reflected in the airlines' financial accounts, is flown revenue, the revenue earned when the carriage purchased by the passenger is actually performed and not sales revenue. As such, it is flown revenue which should be allocated to the country of source (see C below).

C. Source of Revenue

The determination of the source of revenue requires consideration of the following:

- The uplifting of a passenger in a particular State does not necessarily determine the source of that revenue.

- A ticket sold in country A for passage on a foreign airline involves the loss of currency to that country when the passenger boards that airline's aircraft in country A, it is reasonable for country A's tax administration to seek tax on the value of the carriage performed by that airline.

- On the other hand, a ticket sold in country B for a passenger who is merely visiting country A should not be taxed in country A as tax is payable in country B based on sale of transportation there. It is unreasonable to determine the local revenue derived by the foreign airline in country A by taking the gross uplifts of passengers. Nevertheless, the passenger from country B contributes considerably to country A's economy, by way of hotel accommodation, meals, local sightseeing tours, purchases of souvenirs, etc.

- Airline tickets are frequently written to include several airlines, depending on the itinerary of the passenger, in addition to the airline who sold the ticket. By agreement, the airline uplifting the passenger claims its share of revenue for carriage from the issuing airline. Additionally, a ticket once issued can be surrendered, partly used, or may be used on airlines different from those named on the original ticket.

- If revenue basis for tax is the issue value of tickets it is impossible to apportion the tax to all airlines involved as these are not known for certain until after the passenger travels, and it is completely inequitable for the issuing airline to bear the whole burden of any income tax.

- As such, revenue sourced to a State should include only revenue accruing to the operating airline, excluding revenue claimed and remitted to other airlines. Airlines are able to produce this information on a consistent and accurate basis although not all use precisely the same accounting methods.

- What has been said of passenger revenue applies equally in respect of cargo.

- Commission can also be assigned to the point of sale if under the tax law it is deemed to have a source at the point of sale, while commission retained by other airlines would be excluded.

taxation@iata.org
iata.org