



Navigating DTAs, ASAs, and Reciprocal Exemptions

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Quick recap – yesterday's session

Why does it matter? What are the risks?

How could be addressed?

ASAs vs DTAs

Q&A



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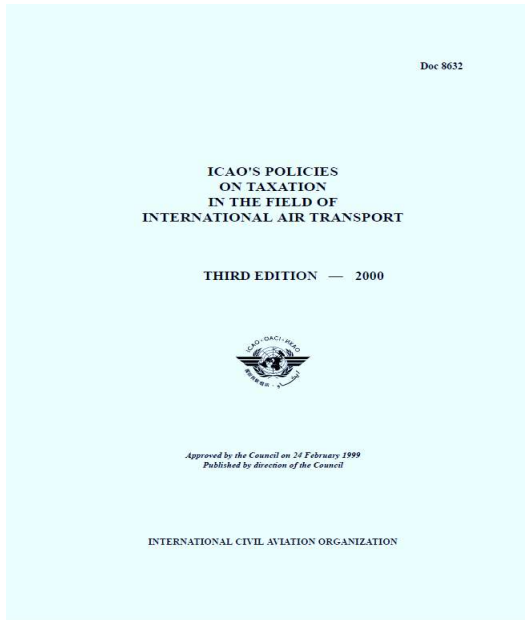


Reciprocal Tax Exemptions



ICAO's Policies on Taxation in the Field of Air Transport as a good regulatory practice

Doc 8632



"International air transport plays a major role in the development and expansion of international trade and travel..."

"...the imposition of national or local taxes on the acquisition of fuel, lubricants and consumable technical supplies for use by aircraft...may have an adverse economic and competitive impact..."

"...lack of implementation of the rule [of reciprocal exemption] involves either multiple taxation [of enterprises] or considerable difficulties of income allocation..."

"...the imposition of taxes on the sale or use of international air transport tends to retard its further development by increasing its cost to the operator...the shipper...and to the traveller..."

- Seeks to **prevent double taxation** of income (profit) relating to the operation of aircraft in international traffic.
- **Exempts fuel**, lubricants, etc. from customs or excise duty – in relation to both fuel and lubricants on-board the aircraft and those that are taken on-board in the foreign territory.



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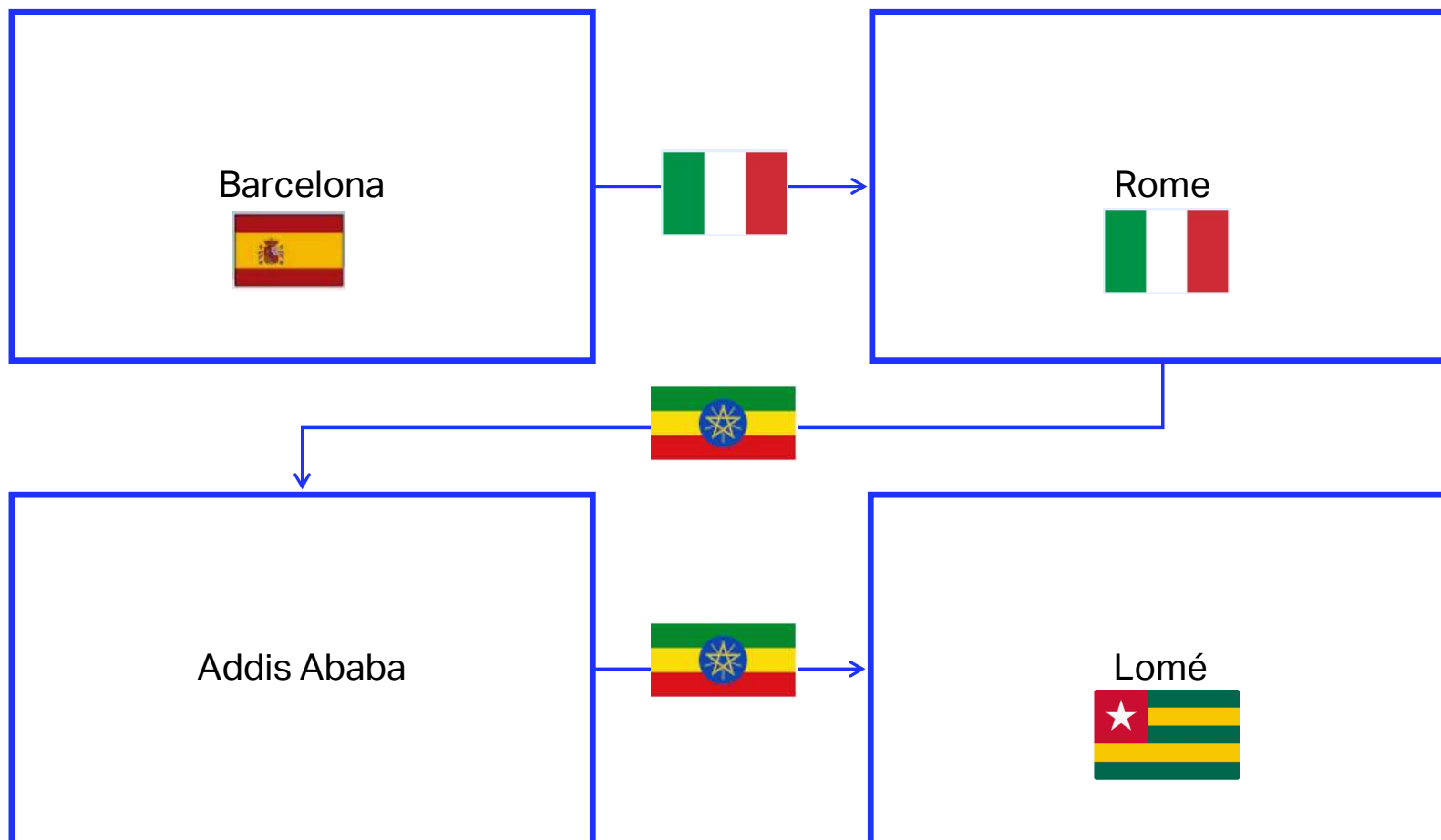
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ASAs vs DTAs

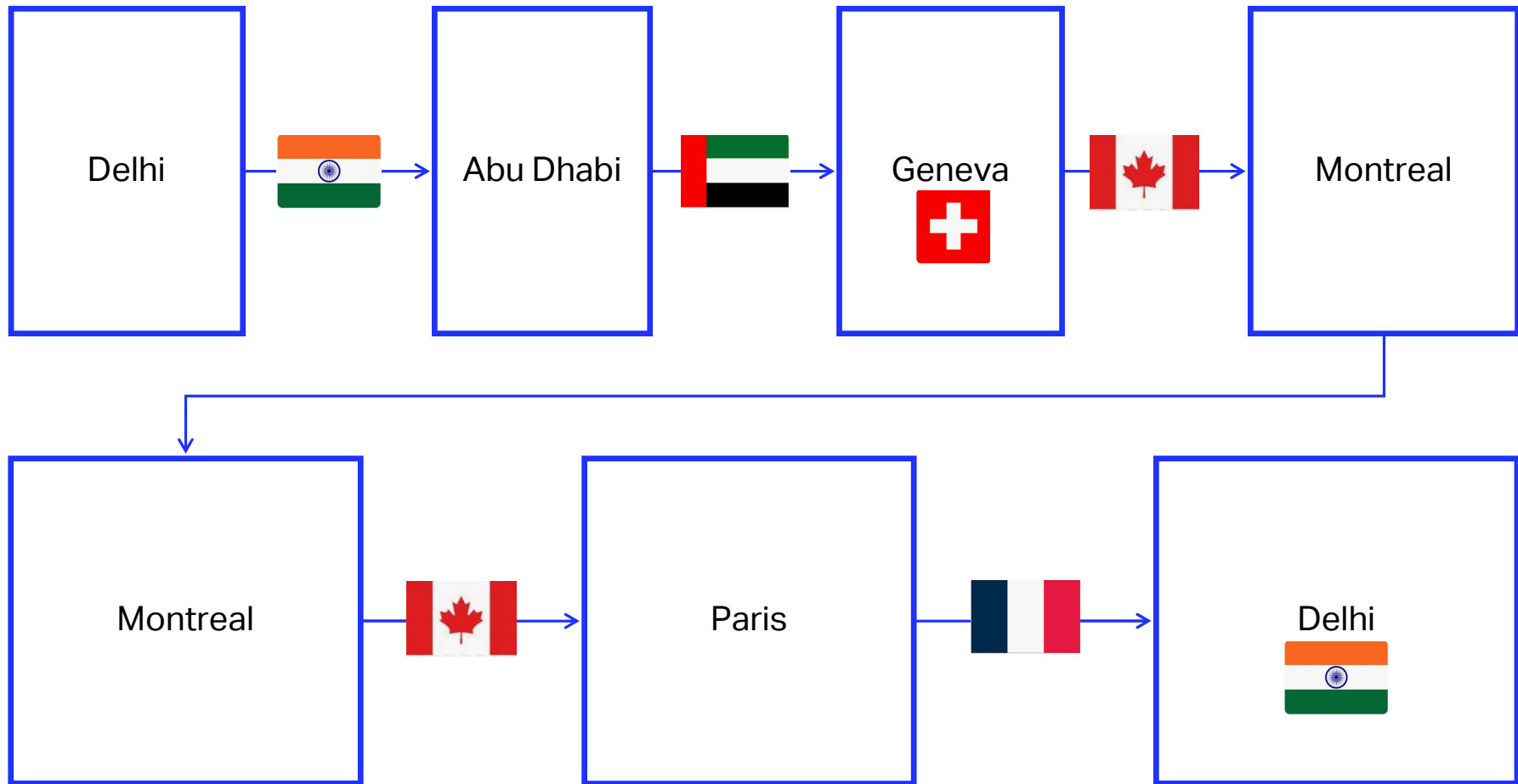
Q&A



Example 1: Alicia (Barcelona)



Example 2: Dhruv (Madrid)



Double Taxation Agreements (DTAs)



- **What is a DTA or Tax Treaty:**

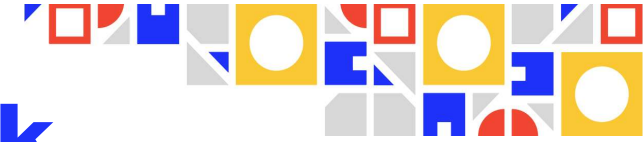
- Special agreement on the distribution of taxing rights for the avoidance of double taxation on income and on capital between the Contracting States on cross-border transactions (e.g. dividends, royalties, business profits). It does not cover indirect taxes.
- International air transport has a specific provision for tax treatment under DTAs (Art. 8).
- The provisions found in Article 8 of a standard bilateral Tax Treaty are similar to the substance of Article 14 of the TASA regarding income taxes (based on ICAO's Policies).
- This offers simplicity and protection from a tax perspective for airlines transporting passengers and cargo internationally.
- Taxation of airlines' income should not be a bargaining chip in negotiations for other income taxing rights. Exclusive residence taxation for air transport should be nonnegotiable.

- **Interaction with national regulations:**

- If a DTA is in place, taxing rights over income need to be allowed under the DTA before national regulation on income taxes applies.
- Subject matter with great complexity and technical content.



Airlines' Legal-Tax Framework



- **Unique regulatory framework:**

- Airlines are subject to unique legal and regulatory requirements for access to foreign airspace and to make international air transport a reality.
- An airline is legally bound and enforced to provide the all-round transport from such framework in its home jurisdiction.

- **Nexus with the State of residence:**

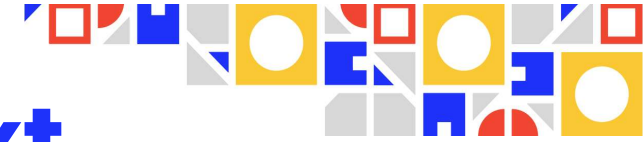
- Under such statutory conditions, the residence of an airline provides an exceptional, strong, nexus to that residence State in exclusivity.
- Taxing rights over an airline's income should not be expanded to the multiple jurisdictions where the physical location (departure or arrival) of the air carriage takes place.

- **Ordinary corporate income tax systems:**

- It is not possible for airlines to engage on profit shifting activities (e.g. digital services).
- Airlines are not subject to the "tonnage tax" regimes applicable to shipping.
- Airlines are not excluded from OECD Pillar Two (Global Minimum Tax Rules).



Airlines' Practical-Tax Context



- **Unique interline system and code-sharing arrangements:**
 - A passenger can buy a single air ticket and travel on any number of airlines as required to get to the destination.
 - Rules for source taxation (in opposition to exclusive residence taxation) based on the physical departure or arrival points do not offer consistent results for air transport.
- **Lack of global tax consensus:**
 - Lack of global consensus on identification of income derived from the air carriage needed for allocation.
 - There is no standard definition of 'revenue' for airlines in the national tax legislations (or even no definition).
 - No technology can solve this lack of global human consensus.



Common objectives

Chicago Convention On International Civil Aviation



"...lack of implementation of the rule [of reciprocal exemption] involves either multiple taxation [of enterprises] or considerable difficulties of income allocation..."

- **Avoid double taxation:**
 - Bilateral agreements allowing source taxing rights between two of the vast number of countries in which an airline operates are unable to avoid double taxation.
 - There are no reliable and technically consistent sourcing rules. The result cannot be other than multiple taxation in multiple jurisdictions. And no basic mechanisms to avoid such multiple taxation on same income can be bilaterally provided under this situation.
- **Reduce tax complexity, alleviate administrative burdens and enhance connectivity:**
 - Patchy regulations on direct and indirect taxes impacting airlines.
 - Inconsistencies to comply with tax obligations (e.g. e-invoicing and tax reporting requirements).
 - Excessive administrative burdens and legal disputes increasing airlines' operating costs in a given jurisdiction.



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Best practice ASA clauses on taxation

In order to address the negative consequences of inefficient taxation, ICAO TASA contains two provisions that address taxation, including: Article 13 and Article 14

Article 13 – Customs duties (indirect taxes)

Provides for a reciprocal exemption from customs duties, excise taxes, inspection fees and other similar duties and charges on: 1) aircraft, 2) fuel, 3) lubricating oils, 4) consumable technical supplies, 5) spare parts (e.g., engines, aircraft equipment) and 6) aircraft stores used in connection with the specified services detailed in the ASA.

The exemption applies to items and goods that are:

- 1) introduced into the counterparty territory; or
- 2) retained on board the aircraft on arrival into or departure from the counterparty territory; or
- 3) taken on board the aircraft in the counterparty territory.

The tax exemption applies irrespective of whether or not the item or good is partially or wholly consumed in the counterparty territory, so long as there is no transfer in ownership.



Best practice ASA clauses on taxation

In order to address the negative consequences of inefficient taxation, ICAO TASA contains two provisions that address taxation, including: Article 13 and Article 14 (cont.)

Article 14 – Taxation (direct profit-based taxes and indirect taxes)

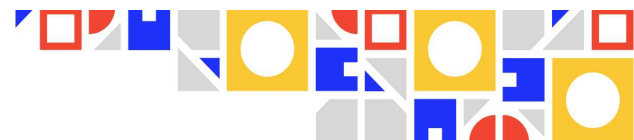
Provides for the taxation of profits from the operation of international air transport services of passengers and/or goods only in the jurisdiction of effective management (e.g., head office) of the airline. As such, airlines are not subject to profit-based taxes in the counterparty territory.

Includes profits associated with inter-airline commercial agreements (e.g., code share arrangements) and joint business ventures.

Likewise, capital (including capital gains) and assets pertaining to the operation of aircraft in international traffic are to be subject to applicable taxation only in the jurisdiction of effective management of the airline.

In addition, provides the option for the reciprocal grant relief from VAT or similar indirect taxes on goods and services supplied to the airline designated by the counterparty and used for the purposes of its operation of international air services. The tax relief may take the form of an exemption or a refund.





Checklist of relevant taxes

ASAs to cover aviation taxation to the maximum extent possible:

Direct taxation (also covered under DTAs)

- Corporate income taxes
- Business taxes and other profit-based taxes
- Withholding taxes on payments

In relation to the 1) provision of international air transport services of passengers and/or goods, and 2) operation of aircraft in international traffic, shall be **subject to applicable taxation and formal obligations only in the jurisdiction of residence of the airline.**

Indirect taxation (not covered under DTAs)

- Customs duties, excise taxes, inspection fees and other similar duties
- VAT, GST and sales taxes

In relation to goods and services supplied to airlines and used for the purposes of their operation of international air services, shall be **reciprocally exempted.**

- Consideration should be given also to: VAT, GST and sales taxes, other taxes, and e-invoicing requirements in relation to the provision of air transport services.

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Interactions between ASAs and DTAs



- **Legal uncertainties:**

- Precedence of DTA over ASA in taxation of income from international air transport?
- Template ASA provides for a tax treaty between the Parties on double taxation to override the provisions of the ASA:

“Where a special agreement for the avoidance of double taxation with respect to taxes on income and on capital exists between the Parties, the provisions of the latter shall prevail.”

- New UN Article 8 Commentary provides that:

“Where there is an existing shipping or air services agreement between the Contracting States that provides for a different allocation rule, such as exclusive residence State taxation, States including paragraph 2 of Article 8 (Alternative A) should clarify how the two agreements interact, which may require modifying or terminating the tax provisions of such agreement in order to provide certainty.”

- *Lex specialis* for taxation matters (DTA) vs *lex specialis* for air services regulation (ASA)?
- *Lex Posterior Derogat Legi Priori*?



Interactions between ASAs and DTAs



- **The willingness of the Contracting States:**

- Ultimately, it's up to states to adopt the best wording in their agreements that better reflects their intent.
- The actual legal effect would mainly depend on the specific language incorporated in the agreements (both ASAs and DTAs) signed between the Contracting States.
- Requires coordination efforts between the State's different negotiation teams (ASAs negotiators and DTAs negotiators).

- **Final remarks:**

- The principle of exclusive residence State taxation for international air transport is well implemented - present in over 3,500 DTAs and ASAs.
- International airlines' ability to conduct their air transport operations relies on the global consensus in favour of exclusively residence-based taxation of airlines' income from international traffic.
- Any deviation from this consensual approach directly implies multiple taxation risks and overwhelming compliance burdens.



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