OPPORTUNITY GREEN

Clearing the air on how we tax aviation fuels

Legal Briefing | November 2024

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Executive Summary

As the global economy faces the twin headwinds of the climate emergency and the cost-of-living crisis, initiatives such as the Global Solidarity Levies Task Force (**GSLTF**) are looking at how the climate finance needed to fight climate change and support vulnerable communities and nature can be raised through progressive international levies on polluting industries. The GSLTF seeks to implement the 'polluter pays' principle: the principle that it is polluters that should finance the costs of damage from pollution, not taxpayers and the vulnerable communities who are most affected by that damage.

One industry stands out for largely being exempt from levies and taxes: aviation. Aviation is responsible for around 4% of all human-caused global heating up to 2021,[1] and this figure is projected to increase as the emissions from air travel are projected to more than double by 2050. By then, aviation could be responsible for around 22% of global CO_2 emissions alone,[2] and CO_2 accounts for only approximately one third of aviation's climate impacts, with the other two thirds being caused by 'non-CO2' emissions.[3] At the same time, aviation is predominantly an activity of the wealthy (only around 2 to 4% of the world's population take international flights[4]) and its climate impacts are disproportionately suffered by the most vulnerable communities (e.g. through the damage caused by extreme weather).[5]

Yet aviation fuel enjoys a 'privileged tax regime',[6] and international aviation fuel is generally exempt from tax around the world. In the context of the climate emergency, aviation's growing share of global pollution and climate damage, and the taxes other sectors pay for using fossil fuels, this position is increasingly being seen as untenable.[7] Whilst global climate targets require all sectors to rapidly and deeply cut greenhouse gas (**GHG**) emissions, the continued tax-free privilege afforded to international aviation fuel, and the absence of clear external cost signals through taxation, is difficult to justify.

Apologists for international aviation fuel's tax exemption often point to restrictions under international law and international legal agreements as the key reason why such exemption is in place.[8] This paper, together with the annexed expert legal opinion of Estelle Dehon KC and Dr Lois Lane, undertakes a detailed legal analysis of that claim, and looks at the capability of states to introduce an aviation fuel tax under current international legal frameworks. Our key findings are set out in the table below.

Our legal analysis concludes that internationally there is likely far more freedom to introduce aviation fuel tax than has been generally acknowledged, and that one of the most commonly assumed 'exemptions' in international agreements is not an absolute

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[1] Milan Klöwer and others, 'Quantifying aviation's contribution to global warming' (2021) 16(104027) Environmental Research Letters, 4 <https://iopscience.iop.org/article/10.1088/1748-9326/ac286e> accessed 11 November 2024.

exemption, rather it in fact allows states to introduce a fuel tax should they wish to. This paper demonstrates that the decision not to tax aviation fuel is therefore on the whole more likely a political decision rather than a response to a legal restriction.

Key findings:

✓ **States can tax the intake of aviation fuel by international aircraft under the Convention on International Civil Aviation (the 'Chicago Convention')**

The Chicago Convention only exempts from tax fuel which was already on board an aircraft on arrival in a contracting state and remains on board of the same aircraft on departure from that contracting state.

✓ **A state which is subject to the common fuel tax exemption 'on the basis of reciprocity' under an air services agreement ('Air Services Agreement' or 'ASA') is free to tax aviation fuel on flights to the other state(s) under that agreement**

As the legal opinion of expert counsel we commissioned shows (see Annex), the common taxation exemption for aviation fuel 'on the basis of reciprocity' found in many bilateral and multilateral air services agreements (**Air Services Agreements** or **ASAs**) is not an absolute exemption, but an agreement that, if one state begins to tax aviation fuel, then the other state may also introduce such a tax, in each case without violating the agreement.

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[2] Martin Cames and others, 'Emission Reduction Targets for International Aviation and Shipping' (2015) Policy PE 569.964, European Parliament's Committee on Environment, Public Health and Food Safety (ENVI) <https://www.europarl.europa.eu/RegData/etudes/STUD/2015/569964/IPOL_STU(2015)569964_EN.pdf> accessed 11 November 2024, 9.

[3] Transport & Environment, 'Airline contrails warm the planet twice as much as CO2, EU study finds' (2020) <https://www.transportenvironment.org/articles/airline-contrails-warm-planet-twice-much-co2-eu-study-finds> accessed 11 November 2024.

[4] Stefan Gössling and Andreas Humpe, 'The Global Scale, Distribution and Growth of Aviation: Implications for Climate Change' (2020) 65(102194) Global Environmental Change, 4.

[5] IPCC, 'Summary for Policymakers' in Hoesung Lee and José Romero (eds), *Climate Change 2023: Synthesis Report. Contribution of Working Groups I, II and III to the Sixth Assessment Report of the Intergovernmental Panel on Climate Change* (IPCC 2023) <www.ipcc.ch/report/ar6/syr/downloads/report/IPCC_AR6_SYR_SPM.pdf> accessed 11 November 2024, 5, 12, 18, 22.

[6] European Commission, 'Proposal for a Council Directive restructuring the Union framework for the taxation of energy products and electricity (recast)', COM/2021/563 final, Recital 21.

[7] For example, a UK House of Commons Library research briefing in 2019 notes that many commentators consider the exemption 'an indefensible anomaly', see Anthony Seely, 'Taxing aviation fuel', House of Commons Library Briefing Paper Number 523 (October 2019), 1; and the explanatory memorandum to the EU proposal to revise the Energy Taxation Directive in 2021 notes that a mandatory fuel tax exemption for international aviation fuel is 'not coherent with the present climate challenges and policies', see European Commission (n 6) Explanatory Memorandum.

[8] See for example, the UK Parliament's ministerial response to a question on aviation fuel in the UK (21 May 2019) <https://questions-statements.parliament.uk/written-questions/detail/2019-05-16/255293> accessed 11 November 2024; and EU Commission 'Excise Duties: Other Energy Tax Legislation' <https://taxation-customs.ec.europa.eu/excise-duties-other-energy-tax-legislation_en> accessed 11 November 2024.

Key findings (cont.):

✓ **Within the EU, Member States can tax aviation fuel used in domestic flights and flights between two or more Member States that have agreed to such a tax.**

Member States have the ability to disapply the general fuel tax exemption under Directive 2003/96/EC9 (the **Energy Taxation Directive** or **ETD**) (which applies to EU Member States as at the date of this paper) in these circumstances.

— **As at the date of this paper, EU Member States cannot generally impose fuel taxes on international flights outside of the EU, subject to certain exceptions.**

The ETD provides that fuel used on international flights outside of the EU shall be exempt from tax.

However, the 2021 proposal to revise the ETD (which was due to apply from 2023) introduces minimum levels of taxation for aviation fuel for intra-EU flights which would ramp up incrementally over a period of ten years, and allows Member States to apply the same levels of taxation to fuel used for extra-EU international flights, without prejudice to states' international obligations.

The EU can also tax fuel used on international flights where provided for in international agreements that take precedence over the ETD (see, for example, the position in relation to the UK below).

✓ **The United Kingdom ('UK') could tax aviation fuel on flights to the EU and the EU could tax aviation fuel on flights to the UK.**

Following Brexit, the EU/UK Trade and Cooperation Agreement explicitly permits the UK to tax fuel used for flights to the EU and vice versa. The EU/UK Trade and Cooperation Agreement, as an international agreement, takes precedence over EU law, including the ETD.

[9] Council Directive (EU) 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity [2003] OJ L 283/51.

Introduction

Background

Aviation fuel has 'traditionally had a privileged tax regime'.[10] Fuel for international flights is generally exempt from tax around the world. This situation has been described by many commentators as 'an indefensible anomaly',[11] for two principal reasons.

First, it does not reflect aviation's significant, and growing, contribution to GHG emissions, global heating and climate damage. Global aviation currently accounts for approximately 2.5% of annual global CO_2 emissions,[12] which could rise to up to 22% by 2050.[13] The total climate impact of aviation is even more significant: 'non-CO2 emissions', including things such as nitrogen oxides, soot and contrails, significantly increase the global heating effect of flying, meaning aviation is responsible for around 4% of all observed global anthropogenic heating up to 2021.[14]

Meanwhile, the sector continues to grow. Global aviation has increased from 310 million passenger journeys in 1970 to 4.5 billion passenger journeys in 2019.[15] Air travel and its emissions are projected to more than double by 2050.[16] Efforts to decarbonise the sector have only achieved minor emissions reductions and it is well established that those reductions have always been far outweighed by the sector's growth.[17] Irrespective of technological advancements, absolute emissions from flying have therefore undergone 'sustained multi-decade growth'.[18]

The climate impacts of such pollution are well established in science.[19] The absence of a fossil fuel tax in the aviation sector is therefore at odds with a key principle of environmental law – the 'polluter pays' principle – which holds that polluters should pay for their pollution, rather than such costs being borne by public authorities and the wider public (for example, through the damage caused by extreme weather events) (see 'Box 1' on p.8). Climate impacts are disproportionately felt by the world's most vulnerable

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[10] European Commission (n 6) Recital 21.
[11] Seely (n 7) 1.
[12] D.S. Lee and others, 'The contribution of global aviation to anthropogenic climate forcing for 2000 to 2018' (2021) 244(117834) Atmospheric Environment 1, 4.
[13] Cames and others (n 2) 9.
[14] Klöwer et al (n 1) 4.
[15] Cames and others (n 2) 9.
[16] Sienna Healy and others 'International Climate Negotiations: Issues at stake in view of the COP28 UN Climate Change Conference in Dubai and beyond' (ENVI 2023) <www.europarl.europa.eu/thinktank/en/document/IPOL_STU(2023)754191> accessed 11 November 2024, 27.
[17] Regulation (EU) 2023/2405 of the European Parliament and of the Council of 18 October 2023 on ensuring a level playing field for sustainable air transport (ReFuelEU Aviation) [2023] Recital 7.
[18] Lee and others (n 12) 4.
[19] See IPCC (n 5) 12, 18, 22.

communities who have contributed least to climate change,[20] whereas flying is predominantly an activity of the wealthy (only around 2 to 4% of the world's population take international flights, and 1% of the world's population are responsible for over half of total emissions from air travel).[21] As such, the liability for the costs of the environmental damage of aviation falling to society as a whole, and disproportionately to vulnerable communities, appears deeply unfair.

Second, the fuel tax exemption is difficult to defend when compared to the taxation approach in other sectors that use fossil fuels. For example, road fuel is generally taxed. In the UK, tax represents '49% of the final pump price for petrol, and 46% of the final pump price for diesel',[22] and in the EU motor fuels are subject to minimum tax rates under the Energy Taxation Directive. The privileged position of aviation, and the absence of clear external cost signals through taxation,[23] is increasingly hard to justify in the context of global, regional and climate targets, which, if they are to be met, require all sectors to rapidly and deeply cut GHG emissions.[24] Indeed, the European Commission has noted that an aviation fuel tax exemption 'is not coherent with the present climate challenges and policies'.[25] Other sectors will likely query why aviation is afforded this treatment; the logical effect of which is that those other sectors have to do more to meet economy-wide climate targets.

As governments are increasingly seeking additional sources of revenue to address the climate emergency, and as initiatives such as the GSLTF[26] gain traction, the privileged tax position of aviation fuel is likely to be brought increasingly into question. In that context, it is important to establish the legal landscape pertaining to taxing international aviation fuel to inform policy-makers' decisions.

The Legal Question

One of the reasons the fuel tax exemption for international aviation seems to have become entrenched practice is the perception that international law prevents such taxation. Indeed, the political dialogue on the question of taxing international aviation fuel often refers to international law to explain or justify the aviation fuel tax exemption.[27]

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[20] ibid 5.
[21] Gössling and Humpe (n4) 4, 9.
[22] As at May 2022. See House of Commons Library, 'Taxation of road fuels' (2022) <https://commonslibrary.parliament.uk/research-briefings/sn00824/#:~:text=Excise%20duty%20is%20charged%20on%20most%20hydrocarbon%20oils.,pump%20price%20for%20diesel%20%28as%20of%20May%202022%29.> accessed 11 November 2024.
[23] Seely (n 7) 2.
[24] IPCC (n 5) 12, 18, 22.
[25] European Commission (n 6)
[26] See Global Solidarity Levies Task Force <https://globalsolidaritylevies.org/> accessed 11 November 2024.
[27] UK Parliament; EU Commission (n 8).

The purpose of this paper is to analyse the international legal frameworks that apply to aviation fuel taxation in order to assess whether or not there are legal barriers to states introducing such taxation. This paper will assess:

- the Chicago Convention;
- the EU's Energy Taxation Directive;
- the position under bilateral and multilateral Air Services Agreements (or ASAs). Due to there being several thousand ASAs,[28] and the only comprehensive database of ASAs of which we are aware being held by the International Civil Aviation Organization (**ICAO**) behind a $3,500–4,000 paywall,[29] this paper will not comprehensively analyse all ASAs; rather it will focus on a common aviation fuel tax clause that aligns with ICAO recommendations and features in many ASAs; and
- the case study of the UK's ability to tax fuel uplifted in the UK for international flights to the EU following Brexit.

This briefing paper will not address questions of domestic law nor will it consider policy questions (for example, the perceived risk of 'tankering'[30]). The focus is strictly on the question of whether international legal frameworks prohibit the taxation of aviation fuel.

BOX 1: What is the polluter pays principle?

The 'polluter pays' principle is a key principle of international environmental law. As the name suggests, it requires a polluter to pay for its pollution, rather than such costs being borne by public authorities and the wider public.

In the EU, the 'polluter pays' principle is enshrined in Article 191(2) of the Treaty on the Functioning of the European Union, which provides that (emphasis added): '*Union policy on the environment…shall be based on the precautionary principle and on the principles that preventative action should be taken, that environmental damage should as a priority be rectified at source and that* ***the polluter should pay****.*'

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[28] Jasper Faber and Aoife O'Leary, 'Taxing aviation fuels In the EU' (CE Delft, 2018), 15 <https://cedelft.eu/wp-content/uploads/sites/2/2021/03/CE_Delft_7R09_Taxing_Aviation_Fuels_EU_Def.pdf> accessed 11 November 2024.

[29] See International Civil Aviation Organization (ICAO), 'World Air Services Agreements' <https://data.icao.int/wasa> accessed 11 November 2024.

[30] Tankering is the practice of carrying excess fuel to avoid refuelling at the destination/stop-over. For more information including a policy proposal for mitigating the risk of tankering, see Bill Hemmings, 'Annex III – Tankering', in Bill Hemmings and others (eds) *Taxing Aviation Fuel: Back to the Future?* (March 2020) < https://www.transportenvironment.org/uploads/files/2020_06_Study_for_TE_Taxing_aviation_fuel_final.pdf> accessed 11 November 2024.

Legal Analysis

The Chicago Convention

The tax exemption enjoyed by international commercial aviation is often linked to the Chicago Convention.[31] However, the Chicago Convention contains no general prohibition on the taxation of aviation fuel.

Article 24(a) of the Chicago Convention provides that (emphasis added):

> *Aircraft on a flight to, from, or across the territory of another contracting State shall be admitted temporarily free of duty, subject to the customs regulations of the State. Fuel, lubricating oils, spare parts, regular equipment and aircraft stores* ***on board an aircraft of a contracting State, on arrival in the territory of another contracting State*** *and retained on board on leaving the territory of that State shall be exempt from customs duty, inspection fees or similar national or local duties and charges. This exemption shall not apply to any quantities or articles unloaded, except in accordance with the customs regulations of the State, which may require that they shall be kept under customs supervision.*

The exemption from 'customs duty, inspection fees or similar national or local duties and charges' is therefore limited to fuel which is already on board the aircraft on arrival and which is retained on board on departure. Additional fuel which is taken on board by an aircraft in a contracting state does not fall within the scope of the Article 24(a) exemption.[32]

Article 15 of the Chicago Convention provides that (emphasis added):

> *Any charges that may be imposed or permitted to be imposed by a contracting State for the use of such airports and air navigation facilities by the aircraft of any other contracting State shall not be higher, (a) As to aircraft not engaged in scheduled international air services, than those that would be paid by its national aircraft of the same class engaged in similar operations, and (b) As to aircraft engaged in scheduled international air services, than those that would be paid by its national aircraft engaged in similar international air services […] No fees, dues or other charges shall be imposed by any contracting State* ***in respect solely of the right of transit over or entry into or exit from its territory*** *of any aircraft of a contracting State or persons or property thereon.*

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[31] UK Parliament; EU Commission (n 8).

[32] European Commission: Directorate-General for Mobility and Transport, 'Taxes in the field of aviation and their impact – Final report' (Publications Office, 2019) 28 <https://data.europa.eu/doi/10.2832/913591> accessed 11 November 2024.

Article 15 applies to (i) charges for the use of airports and air navigation facilities (which are not prohibited, subject to non-discrimination), and (ii) fees, dues or other charges in respect solely of the right of transit over, entry into, or exit from a state's territory (which are prohibited). An aviation fuel tax does not fall into either category: it is not a charge for the use of an airport or air navigation facilities (and provided it was non-discriminatory, would not be prohibited in any case) and an aviation fuel tax is not a fee, due or charge in respect solely of the right of transit over, entry into or exit from the territory.

Further, even if one were to argue that an aviation fuel tax did fall within the scope of the Article 15 categories, domestic courts in both the UK and the Netherlands have considered Article 15 in the context of ticket taxes and have interpreted the provision as an anti-discrimination provision that is compatible with aviation consumption taxes:

- In *R (on the application of the Federation of Tour Operators and Others) v Her Majesty's Treasury*,[33] it was held that Article 15 did not apply to the UK's air passenger duty as 'dues' does not include taxes, and the prohibition is principally an anti-discrimination provision;[34] and
- In *Board of Airline Representatives in the Netherlands v The State of The Netherlands*,[35] the Dutch Supreme Court concluded that the 'Dutch ticket tax' did not infringe Article 15; again finding that Article 15 was designed to prevent protectionist tariffs, and cannot have been aimed at regulatory environmental taxes or consumption taxes.[36]

From the above it is clear that there is no general exemption of aviation fuel from tax under the Chicago Convention, and states that are party to the Convention are not required under the Convention to exempt fuel that is taken on board international flights in their jurisdiction from tax.

KEY POINT: There is no legal requirement to exempt international aircraft refueling in a state from fuel tax under the Chicago Convention. The Chicago Convention only exempts from tax fuel which was already on board an aircraft on arrival in a contracting state and remains on board of the same aircraft on departure from that contracting state.

[33] *R (on the application of the Federation of Tour Operators and Others) v Her Majesty's Treasury* [2007] EWHC 2062 (Admin); [2007] ACD 105.
[34] See further Annex, paragraph 48.
[35] *Board of Airline Representatives in the Netherlands v The State of The Netherlands* NL Supreme Court, Civil Chamber, 10/7/2009, 08/04121, NJ.
[36] See further Annex, paragraph 50.

The European Union's Energy Taxation Directive

The Energy Taxation Directive sets out the EU framework for the taxation of energy products and electricity by Member States, including aviation fuel. As part of the 'Fit for 55' legislative package,[37] the EU is considering replacing the ETD but no political agreement has yet been reached on the proposed replacement. As such, this briefing note will examine first the legal position under the existing ETD, and second the legal position under the proposal for the recast ETD as at the date of this paper (recognising that such proposal may be subsequently revised or may not be implemented at all).

The Energy Taxation Directive

The Energy Taxation Directive sets out the EU framework for the taxation of energy products and electricity.

The ETD includes a general tax exemption for aviation fuel, subject to the right of Member States to waive such exemption in certain circumstances. Article 14(1)(b) of the ETD provides that Member States shall exempt from taxation 'energy products supplied for use as fuel for the purpose of air navigation other than in private pleasure-flying'.[38] The general exemption of commercial aviation fuel from taxation under the ETD is subject to Article 14(2), which provides:

> *Member States may limit the scope of the exemptions provided for in paragraph 1(b) and (c) to international and intra-Community transport. In addition, where a Member State has entered into a bilateral agreement with another Member State, it may also waive the exemptions provided for in paragraph 1(b) and (c). In such cases, Member States may apply a level of taxation below the minimum level set out in this Directive.*

As such, any EU Member State may levy a tax on aviation fuel in respect of:

- domestic flights, without limitation; and
- flights between such Member State and any other Member State with which it bilaterally agrees to do so.

It is therefore open to Member States, under the current legislation, to impose aviation fuel taxes at the domestic level and on international flights between Member States

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[37] The 'Fit for 55' package aims to introduce legislation which reduces emissions in the EU by 55% by 2030 as compared to 1990 levels. See European Council, 'Fit for 55' <https://www.consilium.europa.eu/en/policies/green-deal/fit-for-55/#:~:text=Fit%20for%2055%20refers%20to%20the%20EU%E2%80%99s%20target,EU%20legislation%20in%20line%20with%20the%202030%20goal> accessed 11 November 2024.

[38] 'Private pleasure flying' is defined as 'the use of an aircraft by its owner or the natural or legal person who enjoys its use either through hire or through any other means, for other than commercial purposes and in particular other than for the carriage of passengers or goods or for the supply of services for consideration or for the purposes of public authorities.' See Council Directive (EU) 2003/96/EC (n 9), Article 14(1)(b).

(subject to agreement between the relevant Member States). However, Member States cannot generally impose aviation fuel taxes on international flights outside of the EU (however, the EU can tax fuel used on international flights where permitted to do so under an international agreement that prevails over the ETD; see 'The position of the UK post Brexit', pp.16-17 below).

KEY POINT: Under the Energy Taxation Directive (which applies to EU Member States as at the date of this paper), a Member State may tax domestic aviation fuel and aviation fuel used on flights between that Member State and any other Member State with which it has agreed such a tax.

Whilst EU Member States generally may not tax international aviation fuel used for flights outside of the EU, the EU can tax such fuel where permitted to do so under an international agreement that takes precedence over the Energy Taxation Directive.

Proposed revision of the Energy Taxation Directive

In 2021, the European Commission published a recast proposal for the ETD (the **ETD Proposal**)[39] as part of its 'Fit for 55' legislative package. The 'Fit for 55' package aims to introduce legislation which reduces GHG emissions in the EU by 55% by 2030 as compared to 1990 levels.

The ETD Proposal seeks to address changes in the underlying environmental policy framework since the adoption of the ETD in 2003 and realign the taxation of energy products and electricity with such framework. The explanatory memorandum to the ETD Proposal states that 'the mandatory tax exemption concerning international aviation and waterborne navigation is in particular problematic because it is not coherent with the present climate challenges and policies'.[40]

Under the ETD Proposal:

- fossil fuels used as fuel for intra-EU air transport should no longer be fully exempt from energy taxation in the EU (except cargo-only flights).[41] Instead, aviation fuel for intra-EU passenger flights shall be subject to minimum levels of taxation, which will ramp up incrementally over a transitional period of 10 years. The taxation requirement is stated to be without prejudice to 'international obligations'; and
- Member States may exempt or apply the same levels of taxation applied for intra-EU air navigation to extra-EU navigation according to the type of flight, without prejudice to international obligations.[42]

[39] UK Parliament; EU Commission (n 8).
[40] European Commission (n 7).
[41] European Commission (n 6), Article 14(1).
[42] ibid, Article 14(3).

The 'international obligations' are likely a reference to ASAs (see further pp.13-16 below).

Whilst the ETD Proposal would therefore remove the mandatory tax exemption for aviation fuel for international flights and introduce mandatory taxes for aviation fuel used on intra-EU passenger flights, as at the date of writing the proposal remains under political negotiation despite it having been intended to apply from 1 January 2023. The Council (Economic and Financial Affairs) reported on 30 November 2023 that whilst compromise solutions for some topics had been identified, 'positions among delegations are still divergent on several crucial issues'.[43] Recent reports suggest the EU is in fact considering reversing course, and entrenching the fuel tax exemption until the mid-century.[44] As such, it is unclear if, when, and in what form, such revisions will be adopted.

The revised ETD, if adopted, would allow for taxation of fuel used in international flights. The following section of this paper will address the question of other 'international obligations', and show that the general position under ASAs would not prevent such taxation.

KEY POINT: Whilst Member States can already agree to tax intra-EU flights under the Energy Taxation Directive, the current proposal to recast the Energy Taxation Directive introduces minimum levels of taxation for aviation fuel for such intra-EU flights (except cargo-only flights) which would ramp up incrementally over a period of ten years, and importantly allows Member States to apply the same levels of taxation to fuel used for extra-EU flights, without prejudice to states' international obligations.

However, political agreement has not yet been reached on the adoption of the recast Directive and recent reports suggest the EU is considering entrenching the aviation fuel tax exemption instead.

Air Services Agreements

Air Services Agreements or ASAs are bilateral or multilateral agreements between states that provide the framework under which airlines can fly between those countries.

Taxation of jet fuel is often explicitly mentioned in ASAs.[45] It is beyond the scope of this paper to assess all ASAs; indeed, the only comprehensive database of ASAs is maintained by ICAO and is kept behind a paywall with an annual fee of $3,500-4,000.[46] Instead, this paper will rely on a summary of the general position on aviation fuel tax which is presented in a study undertaken for the European Commission in 2019: that most countries

[43] General Secretariat of the Council of the European Union, 'Draft Ecofin report to the European Council on tax issues - Approval', 16100/23 FISC 275 ECOFIN 1294 (30 November 2023) <https://data.consilium.europa.eu/doc/document/ST-16100-2023-INIT/en/pdf> accessed 11 November 2024, paragraph 40.
[44] Kate Abnett, 'EU countries mull 20-year tax holiday for jet fuel, document shows' (Thomson Reuters, 6 September 2024) < https://www.reuters.com/business/aerospace-defense/eu-countries-mull-20-year-tax-holiday-jet-fuel-document-shows-2024-09-06/> Accessed 11 November 2024.
[45] European Commission: Directorate-General for Mobility and Transport (n 32) 28.
[46] ICAO (n 29).

considered in the study[47] comply with the ICAO policy not to tax the intake of jet fuel on the basis of reciprocity.[48]

The ICAO policy referred to is set out in ICAO policy document 8632,[49] which includes the 'Council Resolution on Taxation of International Air Transport' (the **ICAO Resolution**), and provides, among other things, that:

- fuel for international flights shall be exempt from (or refunded) tax on a reciprocal basis (clause 1(a)(ii) and (iii) of the resolution);
- notes that this reciprocal exemption is the 'common practice of many States' (recitals to the resolution);
- as the exemption is 'based upon reciprocity' no contracting state is obliged to grant to aircraft from another contracting state any treatment more favourable than its own aircraft receive in that contracting state (clause 1(b) of the resolution); and
- 'encourages' contracting states to apply the exemption to the maximum extent possible (clause 1(c) of the resolution).

Whilst clauses 1(b) and (c) of the ICAO Resolution envisage the situation where contracting states may decide to disapply the reciprocal exemption, in any event contracting states are free to unilaterally derogate from ICAO's policy recommendation by notification.[50] Most countries have implemented the recommendation and do not tax international aviation fuel, albeit some countries – including Germany, Norway and Sweden – have included reservations on this policy, noting for example that such a tax could be used to address the environmental impacts of aviation.[51] Germany's reservation also highlights that Germany is 'strictly opposed to ICAO's activities in connection with the sale and use of international air passenger transport services because questions of tax policy in this area to not fall within ICAO's remit'.[52]

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[47] European Commission: Directorate-General for Mobility and Transport (n 32) 14. The study considers all EU Member States as well as a number of other countries outside of the EU.
[48] European Commission: Directorate-General for Mobility and Transport (n32) 28.
[49] ICAO, 'Council Resolution on Taxation of International Air Transport' (2000) <https://www.icao.int/publications/Documents/8632_3ed_en.pdf> accessed 11 November 2024, clause 1(a).
[50] Eckhard Pache, 'Annex I - Taxing Aviation Fuel in Europe' in Bill Hemmings and others (eds) *Taxing Aviation Fuel: Back to the Future?* (March 2020) < https://www.transportenvironment.org/uploads/files/2020_06_Study_for_TE_Taxing_aviation_fuel_final.pdf> accessed 11 November 2024, 58-59.
[51] European Commission: Directorate-General for Mobility and Transport (n32) 28-29.
[52] ICAO, 'Supplement to Doc 8632 (2021)' <https://www.icao.int/publications/Documents/8632_3ed_sup_aug21_en.pdf> accessed 11 November 2024, 79.

The 'policy of reciprocal exemption' in the ICAO Resolution is therefore likely to be widely implemented globally in ASAs. It is reflected, for example, in the US/EU Open Skies Agreement:

> *There shall also be exempt, on the basis of reciprocity, from the taxes, levies, duties, fees and charges referred to in paragraph 1 of this Article, with the exception of charges based on the cost of the service provided […] fuel, lubricants and consumable technical supplies introduced into or supplied in the territory of a Party for use in an aircraft of an airline of the other Party engaged in international air transportation, even when these supplies are to be used on a part of the journey performed over the territory of the Party in which they are taken on board.*[53]

It is important to note that not all ASAs reflect this wording,[54] but many do, including for example, a number of bilateral ASAs entered into by the United States (indeed, it is contained within the US State Department's 'Model Open Skies Agreement Text' published in 2012, as well as within multilateral agreements such as the Agreement on the Liberalization of Air Transport of the Arab League States, and the ASEAN Multilateral Agreement on Air Services between various South-East Asian states).[55]

In the annexed legal opinion commissioned by Opportunity Green, '*In the matter of the United States – European Union Air Transport Agreement ('Open Skies Agreement'): Re: The extent of the exemptions from taxation under Article 11 and the ability of parties to introduce new taxes on aviation fuel*', (see the Annex to this paper), Estelle Dehon KC and Dr Lois Lane conclude that 'the correct interpretation of the phrase 'on the basis of reciprocity' is an agreement that, if one party begins to tax another party (which it may do without violating the agreement), then the other party may also levy such a tax'.[56] This is consistent with a logical reading of the provision and with previous legal interpretations of the same.[57] The legal opinion highlights three key reasons for this interpretation:[58]

- That 'as a matter of logic the phrase ["on the basis of reciprocity"] would be redundant if the exemption from new taxes was absolute and inflexible';
- There is a mechanism under the United States Internal Review Code (section 4221(e)(1)) to discontinue tax exemptions for aircraft of another state where such state has discontinued granting reciprocal tax exemption privileges, and such mechanism has

[53] Council Decision (EU) 2007/339/EC of 25 May 2007 Air Transport Agreement between the United States and EU Member States and the European Community [2007] OJ L 134, Article 11(2)(c).
[54] Faber and O'Leary (n 28) 7.
[55] See further Annex, paragraph 26.
[56] Annex, 1.
[57] Faber and O'Leary (n 28) 25.
[58] Annex, 1-2.

been used to discontinue tax exemptions for Bolivia and reviews have been carried out for other states, including Ecuador and the Dominican Republic; and

- In *R (Air Transport Association of America and others) v Secretary of State for Energy and Climate Change (International Air Transport Association and others intervening)*,[59] the Court of Justice of the European Union recognised that the prohibition of fuel taxes in Article 11(2)(c) of the US/EU Open Skies Agreement is 'subject to reciprocity'.

As such, where a state is party to an ASA which contains a restriction on the taxation of aviation fuel 'on the basis of reciprocity', then it is open to that state to introduce a tax on aviation fuel for international flights. The other state party to the ASA is also free to introduce such a tax.

Whilst it has been beyond the scope of this paper to assess all ASAs that have been entered into, a large number (if not most) of ASAs are likely to include the 'reciprocal' fuel tax exemption,[60] and it can be concluded that states subject to those ASAs are legally permitted to introduce an aviation fuel tax pursuant to the terms of the ASA. Consequently, for states outside of the EU, if the international legal framework which governs air services to and from that state comprises: (i) the Chicago Convention, and (ii) ASAs that only contain a restriction on fuel tax 'on the basis of reciprocity', those states may levy a tax on international aviation fuel without legal impediment.

KEY POINT: The common provision in bilateral Air Services Agreements to exempt fuel from tax 'on the basis of reciprocity' does not prevent states from introducing a tax on international aviation fuel, rather it simply provides that if one party does introduce such a tax, the other can too.

The position of the UK post Brexit

The UK presents an interesting case study following Brexit. The Trade and Cooperation Agreement entered into between the UK and the EU dated 30 December 2020 which entered into force on 1 May 2021 (the **UK/EU Trade and Cooperation Agreement**)[61] specifically addresses the taxation of aviation fuel on flights between the UK and EU.

Pursuant to Article 430(2) of the UK/EU Trade and Cooperation Agreement (emphasis added):

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[59] *R (Air Transport Association of America and others) v Secretary of State for Energy and Climate Change (International Air Transport Association and others intervening)* Case C-366/10 [2013] PTSR 209.
[60] Faber and O'Leary (n 28), 7.
[61] Trade and Cooperation Agreement between the United Kingdom of Great Britain and Northern Ireland, of the one part, and the European Union and the European Atomic Energy Community, of the other part, (signed 30 December 2020, entered into force 1 May 2021) OJ L 149/10.

> *The following goods shall also be exempt, on the basis of reciprocity, from the taxes, levies, duties, fees and charges referred to in paragraph 1 […] (c)* ***lubricants and consumable technical supplies other than fuel introduced into or supplied in the territory of a Party for use in an aircraft of an air carrier of the other Party used in international air transport****, even when those supplies are to be used on a part of the journey performed over the said territory*

As such, the UK/EU Trade and Cooperation Agreement explicitly permits aviation fuel to be taxed, as it is specifically carved out of the tax exemption in Article 430(2). This implements the clear position adopted in the EU's mandate for negotiations prior to the UK/EU Trade Cooperation Agreement that '[t]he envisaged partnership should not prohibit taxation on a non-discriminatory basis of aircraft fuel supplied to aircraft'.[62]

We note recent calls have been made for the UK to introduce such a tax, and analysis shows that charging fuel duty on all jet fuel at the same rate as for car drivers could have raised £5.9 billion in taxes in 2023.[63]

We consider that such an action would likely elicit a response in kind from the EU. Whilst the ETD generally restricts EU Member States from taxing aviation fuel used on international flights, the UK/EU Trade Cooperation Agreement is an international agreement which takes precedence over EU law. Article 216(2) TFEU provides that '[a]greements concluded by the Union are binding upon the institutions of the Union and on its Member States', and the Court of Justice of the European Union has held that international agreements concluded by the EU prevail over acts of the European Union.[64] As such, notwithstanding the terms of the ETD, the EU could tax aviation fuel supplied in the EU for flights to the UK as in this case the UK/EU Trade and Cooperation Agreement supersedes the application of EU law.

KEY POINT: The UK can tax aviation fuel on flights to the EU and the EU can tax aviation fuel on flights to the UK under the terms of the UK/EU Trade and Cooperation Agreement (which takes precedence over the ETD).

If the ASAs the UK has entered into with countries elsewhere in the world include the reciprocal exemption considered above, then the UK can also tax fuel used on flights to all of those destinations (noting a comprehensive review of all of the relevant ASAs would need to be undertaken to confirm that position).

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[62] Council of the European Union, 'Annex to Council Decision authorising the opening of negotiations with the United Kingdom of Great Britain and Northern Ireland for a new partnership agreement', 5870/20 ADD 1 REV 3 (25 February 2020) <st05870-ad01re03-en20.pdf> accessed 11 November 2024, paragraph 67.

[63] Transport & Environment, 'Jet Fuel Duty: How much revenue could have been raised for the UK Government if fuel duty was applied to jet fuel in 2023?' (16 September, 2024) <https://www.transportenvironment.org/te-united-kingdom/articles/jet-fuel-duty-how-much-revenue-could-have-been-raised-if-fuel-duty-was-applied-in-2023> accessed 11 November 2024.

[64] See, for example, *Case C-61/94 Commission v Germany* [1996] ECR I-3989, paragraph 52; and *Case C-308/06 Intertanko and Others* [2008] ECR I-4057, paragraph 42.

Conclusion

This paper has provided an analysis of the international and EU legal frameworks applicable to the taxation of aviation fuel. It has shown that, with the notable exception of EU Member States which are currently generally prohibited from taxing international aviation fuel under the Energy Taxation Directive (subject to its proposed revision and subject to the EU's ability to tax aviation fuel under international agreements such as the UK/EU Trade and Cooperation Agreement), the general position under international law is that states may levy an aviation fuel tax without breaching the Chicago Convention or bilateral/multilateral air services agreements to the extent such air services agreements reflect the general fuel taxation provision considered in this paper, that exempts international flights from aviation fuel tax 'on the basis of reciprocity'.

The legal basis for the aviation fuel taxation exemption has therefore been frequently misunderstood, and sometimes misrepresented. The exemption, rather than being a legal requirement, is something that has become entrenched, as ICAO describes it, as a 'common practice'.[65] The practice's basis of reciprocity allows states to unilaterally levy aviation fuel tax, as the agreement not to tax only applies to the extent both parties elect not to tax. The decision not to tax aviation fuel in such circumstances is therefore a political choice and not a response to a legal restriction.

This paper has also analysed the position of the UK following Brexit, now that it is no longer subject to the EU's ETD. It has shown that the UK is able to introduce an aviation fuel tax on international flights to the EU without legal impediment under its trade agreement with the EU or the Chicago Convention. If such action were taken by the UK, it is considered likely the EU would reciprocate which it is free to do so under the terms of the UK/EU Trade and Cooperation Agreement (which takes precedence over the Energy Taxation Directive).

[65] ICAO (n 49) 7.

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Annex

Legal Opinion of Estelle Dehon KC and Dr Lois Lane of Cornerstone Barristers

IN THE MATTER OF THE UNITED STATES – EUROPEAN UNION AIR TRANSPORT AGREEMENT ('OPEN SKIES AGREEMENT')

Re: The extent of the exemptions from taxation under Article 11 and the ability of parties to introduce new taxes on aviation fuel

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ADVICE

INTRODUCTION

1. We are asked to advise Opportunity Green on the proper interpretation of Article 11 of the United States – European Union Air Transport Agreement ("**the Open Skies Agreement**"), as entered into in 2007 and amended in 2010. In particular, we are asked to consider the meaning of the phrase "on the basis of reciprocity" in Article 11(1) and (2), as regards the exemption from taxes, levies, duties, fees and charges provided for by Article 11(2)(c) in respect of aviation fuel, and whether this phrase renders the exemption conditional on reciprocity, such that either party to the Open Skies Agreement may elect to introduce taxes at any time, on the understanding that the other party may do likewise.

2. For the reasons set out in detail below:
    a) We take the view that the correct interpretation of the phrase "on the basis of reciprocity" is as an agreement that, if one party begins to tax another party (which it may do without violating the agreement), then the other party may also levy such a tax. This is more likely to be correct than an interpretation which construes Article 11 as an outright ban on the imposition of fuel taxes under the Open Skies Agreement. This is for several reasons:
        i) **First**, as a matter of logic the phrase would be redundant if the exemption from new taxes was absolute and inflexible.

ii) **Second**, a mechanism exists within section 4221(e)(1) of the United States ("**US**") Internal Revenue Code, as amended, (26 U.S.C. 4221) for the Secretary of Commerce to inform the Secretary of the Treasury if a foreign country has discontinued granting reciprocal tax exemption privileges and that in such circumstances the privileges granted under subsection 4221(a)(3) shall no longer apply to foreign aircraft. This mechanism has previously been used to discontinue tax exemptions for Bolivia[1] and reviews have been carried out for a range of states, including Ecuador and the Dominican Republic.[2] The existence of such a mechanism supports the correct interpretation of Article 11 as not imposing an outright ban on fuel taxation but as an agreement that, if one Party to the Open Skies Agreement begins to tax fuel, the other may too.

iii) **Third**, in *R(Air Transport Association of America and others) v Secretary of State for Energy and Climate Change (International Air Transport Association and others intervening)* (Case C-366/10) [2013] PTSR 209 ("***ATAA***") the Court of Justice of the European Union ("**CJEU**") recognised at §137 that the prohibition on fuel taxes in Article 11(2)(c) is "subject to reciprocity". Comments in the Opinion of Advocate General ("**AG**") Kokott in the same case at §104 support the interpretation of the phrase for which we contend, though as set out below at §§44-46m there is some tension between the AG's Opinion and judgment of the Court on the direct applicability of Article 11(2)(c).

b) However, if we are wrong about the interpretation of Article 11, there is a risk that US airlines might seek to challenge the validity of any legislation

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1 Discontinuance of Exemption; Republic of Bolivia, 06/15/2006, https://www.federalregister.gov/documents/2006/06/15/E6-9335/exemption-of-foreign-air-carriers-from-excise-taxes-discontinuance-of-exemption-republic-of-bolivia

2 Review of Finding of Reciprocity (Dominican Republic), 09/22/2008, https://www.federalregister.gov/documents/2008/09/22/E8-22032/exemption-of-foreign-air-carriers-from-excise-taxes-review-of-finding-of-reciprocity-dominican; Review of Finding of Reciprocity (Ecuador), 06/02/2010, https://www.federalregister.gov/documents/2010/06/02/2010-13223/exemption-of-foreign-air-carriers-from-excise-taxes-review-of-finding-of-reciprocity-ecuador-26-usc;

introducing new excise duties within the European Union ("**EU**") in the European courts. Previous CJEU caselaw supports their ability to do this to some extent. In particular, the *ATAA* judgment and the AG's Opinion, included the following principles:

i) Article 11(2)(c) is able to be directly relied upon by individuals (i.e. natural or legal persons) to question the validity of EU legislative acts (Judgment §93).

ii) The provision within the Open Skies Agreement itself for dispute resolution mechanisms which do not involve the courts does not automatically prevent the courts from considering the compatibility of EU legislative acts with the Union's obligations under the Open Skies Agreement (Judgment §83).

iii) The EU has expressly committed itself to the observance of its international law obligations (AG's Opinion, §43).

c) Nevertheless, there is uncertainty in the judgment of the CJEU at §93 around the consequences for the direct applicability of Article 11(2)(c) if the EU were to commit itself explicitly to the introduction of a new tax on fuel for intra-EU or transatlantic flights.

REASONS

Introduction

3. We have had the benefit of reading a 2018 report for CE Delft.[3] This sets out that the exemption in Article 11 covers national and European Union ("**EU**") taxation of aviation fuel for international but not domestic flights. Article 11(1) covers fuel already on board an aircraft when it arrives in the territory of a Party to the Agreement, and Article 11(2)(c) covers fuel "*introduced into or supplied in the*

[3] *Taxing aviation fuels in the EU*, prepared for CE Delft by Jasper Faber and Aoife O'Leary, with a contribution by Pablo Mendes de Leon (November 2018) https://cedelft.eu/wp-content/uploads/sites/2/2021/03/CE_Delft_7R09_Taxing_Aviation_Fuels_EU_Def.pdf.

territory of a Party for use in an aircraft of an airline of the other Party". Both exemptions are framed as being "on the basis of reciprocity".

4. The CE Delft report notes in section B.8 on page 25 that there is no definition of reciprocity within the Open Skies Agreement but cites a 1999 report written for the European Commission by a consortium including the International Institute of Air and Space Law, which stated that:

> *"the words "on the basis of reciprocity" could be understood to mean that only as long as the two concerned countries exempt aircraft fuel from taxation, such exemption falls under the scope of the cited provision. Thus, the quoted words would leave the door open for one of the two bilateral partners to go its own way as to tax exemption, because such exemption is subject to the condition of reciprocity. This interpretation has however never put to a legal test."*

5. The CE Delft report goes on to state:

> *"Under this interpretation, then either side (the US or EU) can begin to tax fuel used in international aviation without violating the agreement. The wording of Article 11 is not a ban on fuel taxation, rather an agreement that if one party begins to tax fuel, the other party may too."*

Current legal position within the European Union on the taxation of aviation fuel: The Energy Taxation Directive (2003/96/EC)

6. Within the EU, commercial aviation fuel is currently exempt from excise duties (unlike fuels used for road and rail transport), by virtue of Article 14(b) of Directive 2003/96/EC, known as the Energy Taxation Directive. This article provides, *inter alia*, that:

> *"Member States shall exempt the following from taxation under conditions which they shall lay down[: …] energy products supplied for use as fuel for the purpose of air navigation other than in private pleasure-flying. […]. Member States may limit the scope of this exemption to supplies of jet fuel*".

7. Article 14(2) of the Energy Taxation Directive gives Member States the power to "*limit the scope of the exemptions provided for in paragraph 1(b) and (c) to international and intra-Community transport. In addition, where a Member State has entered into a bilateral agreement with another Member State, it may also waive the exemptions provided for in paragraph 1(b) and (c).*" In other words, member

states may impose a tax on aviation fuel used in domestic flights without limitation as well as on intra-EEA flights between Member States if the affected states have entered into a bilateral agreement to do so. No Member States have yet availed themselves of the opportunity to enter into such a bilateral agreement.

8. Proposals for reform of the Energy Taxation Directive were published by the Commission in 2021. As regards aviation fuel they were summarised by the Commission as follows:

> *"The tax for aviation fuel will be introduced gradually before reaching the final minimum rate after a transitional period of ten years. This means that ten years after the entry into force of the new rules, kerosene used in the aviation industry to power planes for intra-EU flights would be taxed at least €10.75/GJ EU-wide, as for petrol used in road transport. To encourage the use of cleaner energy in both the aviation and maritime sectors, sustainable and alternative fuels will enjoy a zero rate minimum tax rate for a transitional period of 10 years when used for air and waterborne navigation."* [4]

9. However, progress has since stalled in the face of political challenges around achieving unanimity across Member States.

The Open Skies Agreement

The Chicago Convention and the origins of open skies agreements

10. Modern air transport agreements ("**ATAs**") find their origins in the Convention on International Civil Aviation of 7 December 1944 ("**Chicago Convention**"). This was a multilateral convention which set out a range of rights of States with respect to flights over or in their territory by civil aircraft. The rights contained within the Chicago Convention have been implemented in numerous bilateral ATAs. As shall be seen below at §27, the rights in respect of exemption from fuel taxes found in Article 11 of the Open Skies Agreement have been recognised by the Court of Justice of the European Union ("**CJEU**") to derive ultimately from the Chicago

[4] See https://ec.europa.eu/commission/presscorner/detail/en/qanda_21_3662; and 2021/0213 (CNS), https://oeil.secure.europarl.europa.eu/oeil/popups/ficheprocedure.do?reference=2021/0213(CNS)&l=en

Convention, though as will be seen it represents an evolution of the position in terms of the scope of its tax exemptions.

11. Article 15 of the Convention provides, *inter alia*, that:

> *"Any charges that may be imposed or permitted to be imposed by a contracting State for the use of such airports and air navigation facilities by the aircraft of any other contracting State shall not be higher,*
> *(a) As to aircraft not engaged in scheduled international air services, than those that would be paid by its national aircraft of the same class engaged in similar operations, and*
> *(b) As to aircraft engaged in scheduled international air services, than those that would be paid by its national aircraft engaged in similar international air services*
> *[…]*
> *No fees, dues or other charges shall be imposed by any contracting State in respect solely of the right of transit over or entry into or exit from its territory of any aircraft of a contracting State or persons or property thereon."*

12. Article 24(a) provides:

> *"Aircraft on a flight to, from, or across the territory of another contracting State shall be admitted temporarily free of duty, subject to the customs regulations of the State. Fuel, lubricating oils, spare parts, regular equipment and aircraft stores on board an aircraft of a contracting State, on arrival in the territory of another contracting State and retained on board on leaving the territory of that State shall be exempt from customs duty, inspection fees or similar national or local duties and charges. This exemption shall not apply to any quantities or articles unloaded, except in accordance with the customs regulations of the State, which may require that they shall be kept under customs supervision."*

<u>Overall nature and purpose of the Open Skies Agreement</u>

13. The overall goal of the Open Skies Agreement is to facilitate the liberalisation of air services markets in the US and the EU and to promote competition in those markets.

14. The Open Skies Agreement has been approved on behalf of the European Union by Decisions 2007/339 and 2010/465. Consequently, its provisions form an integral

part of the legal order of the European Union as from its entry into force (see *R & V Haegeman v Belgian State* [1974] ECR 449, at §5).

Specific provisions of the Agreement

15. The principle of "fair and equal opportunity" is laid down in Article 2 of the Open Skies Agreement as follows: "*Each party shall allow a fair and equal opportunity for the airlines of both parties to compete in providing the international air transportation governed by this agreement.*"

16. Article 3(4) provides that parties may, for environmental reasons, require a range of measures from airlines of the other party which would otherwise be prohibited under that article, provided that such measures are consistent with Article 15.

17. Article 11 provides, *inter alia*, that:

> *(1) "On arriving in the territory of one Party, aircraft operated in international air transportation by the airlines of the other Party, their […] fuel, lubricants, […] and other items intended for or used solely in connection with the operation or servicing of aircraft engaged in international air transportation shall be exempt, on the basis of reciprocity, from all import restrictions, property taxes and capital levies, customs duties, excise taxes, and similar fees and charges that are (a) imposed by the national authorities or the European Community, and (b) not based on the cost of services provided, provided that such equipment and supplies remain on board the aircraft.*
>
> *(2) There shall also be exempt, on the basis of reciprocity, from the taxes, levies, duties, fees and charges referred to in paragraph 1 of this Article, with the exception of charges based on the cost of the service provided: […] fuel, lubricants and consumable technical supplies introduced into or supplied in the territory of a Party for use in an aircraft of an airline of the other Party engaged in international air transportation, even when these supplies are to be used on a part of the journey performed over the territory of the Party in which they are taken on board*
>
> *[…]*
>
> *(6) In the event that two or more Member States envisage applying to the fuel supplied to aircraft of US airlines in the territories of such Member States for flights between such Member States any waiver of the*

exemption contained in Article 14(b) of Council Directive 2003/96/EC of 27 October 2003, the Joint Committee shall consider that issue, in accordance with paragraph 4(e) of Article 18." (On Article 11(6) see further below at §§21–22)

18. This moves the position on from Article 24(a) of the Chicago Convention because Article 11(2) of the Open Skies Agreement covers fuel and other supplies taken on board an aircraft registered in the territory of one contracting Party while it is in the territory of the other contracting Party and not only those which were already on board.

19. Article 15(3) provides that environmental measures imposed under Article 3(4) must not be discriminatory so as to protect national aircraft. In other words, it places the US and the EU under an obligation not to charge foreign aircraft more than national aircraft. Additional environmental measures and/or charges must be imposed in pursuit of the relevant environmental reason rather than for protectionist reasons.

20. Article 15(8) provides for a dispute resolution mechanism where a party believes that a proposed new environmental protection raises concerns for the application or implementation of the Open Skies Agreement. The concerned party may "*request a meeting of the Joint Committee, as provided in article 18, to consider the issue and develop appropriate responses to concerns found to be legitimate*".

21. Article 18 sets out the mechanism for requesting a meeting of the Joint Committee, comprised of representatives of the parties, to resolve disputes or clarify questions relating to the interpretation or application of the Agreement. In particular, Article 18(4) provides that "*The Joint Committee shall also develop cooperation by: … (e) making decisions, on the basis of consensus, concerning any matters with respect to application of Paragraph 6 of Article 11*."

22. This means that in circumstances where two EU member states are minded to enter into a bilateral agreement pursuant to Article 14(2) of the Energy Taxation Directive to limit the scope of the exemptions provided for under Article 14(1), the

Joint Committee would need to consider the implications of such an agreement for the EU's compliance with the Open Skies Agreement and attempt to reach a decision on the basis of consensus.

23. Article 19 provides that any dispute which is not resolved by a meeting of the Joint Committee may be submitted to arbitration.

Conclusion

24. Drawing the above together, our view is that, both logically and contextually, the correct interpretation of the exemptions in Article 11 of the Open Skies Agreement is that they are not absolute, but rather Article 11 represents an agreement that if one Party begins to tax fuel, the other may do so too. As a matter of logic, the phrase "on the basis of reciprocity" would be redundant if the exemption from new taxes was absolute and inflexible.

The principle of reciprocity in air transport agreements

25. The concept of reciprocity has a range of potential meanings in public international law, from transactional interpretations based upon the conduct of the parties, to broader systemic interpretations based upon commitments to mutual obligations between States based upon a broad principle of equivalence of treatment.[5]

26. Within the field of ATAs, the phrase "on the basis of reciprocity" is not confined to the Open Skies Agreement. It appears in the context of provisions on levies, taxes and duties in bilateral ATAs entered into by the United States, such as the US–Bahrain ATA (Article 9), the US–Canada ATA (Article 10), and the US–Costa Rica ATA (Article 10), [6] and in multilateral agreements among states other than the United States, such as the Agreement on the Liberalization of Air Transport of the Arab League States (Article 21), and the ASEAN Multilateral Agreement on Air

[5] See Arianna Wheelan, *Reciprocity in Public International Law* (Cambridge University Press: 2023), chapters 1-2.

[6] For a full list of US ATAs, see https://www.state.gov/full-list-of-air-transport-agreements-and-record-documents/.

Services between various South-East Asian states (Article 11). It is also found in the US State Department's 'Model Open Skies Agreement Text', published in 2012.[7]

27. This reflects the findings of the CJEU in the *ATAA* case at §91 that the obligations around levies, duties and taxes found in Article 11 of the Open Skies Agreement are not entirely novel. Rather they are an evolution of earlier obligations derived from international treaties, in particular the Chicago Convention.

28. Within the United States, the Internal Revenue Code provides at section 4221(a)(3) that: "*Under regulations prescribed by the Secretary, no tax shall be imposed under this chapter (other than under section 4121 or 4081) on the sale by the manufacturer (or under subchapter C of chapter 31 on the first retail sale) of an article— […] for use by the purchaser as supplies for vessels or aircraft*".

29. However, the section continues at subsection (e)(1) to provide a mechanism for rescinding exemptions in respect of foreign-registered aircraft where the conduct of providing reciprocal exemptions is not being performed by the country of registration:

> *"**Reciprocity required in case of civil aircraft***
>
> *In the case of articles sold for use as supplies for aircraft, the privileges granted under subsection (a)(3) in respect of civil aircraft employed in foreign trade or trade between the United States and any of its possessions, in respect of aircraft registered in a foreign country, shall be allowed only if the Secretary of the Treasury has been advised by the Secretary of Commerce that he has found that such foreign country allows, or will allow, substantially reciprocal privileges in respect of aircraft registered in the United States. If the Secretary of the Treasury is advised by the Secretary of Commerce that he has found that a foreign country has discontinued or will discontinue the allowance of such privileges, the privileges granted under subsection (a)(3) shall not apply thereafter in respect of civil aircraft registered in that foreign country and employed in foreign trade or trade between the United States and any of its possessions."*

[7] Model Open Skies Agreement Text', 12 January 2012, https://www.state.gov/wp-content/uploads/2022/12/Open-Skies-Model-Text-2012-June-2017-update-Accessible.pdf

30. In our view, this shows that that the United States has taken a transactional approach to reciprocity in the context of its international ATAs. It further indicates that the US federal government envisages undertaking periodic reviews of tax exemptions granted by other parties to such agreements.

31. This review mechanism has previously been used for a general review of a range of countries' reciprocal tax exemptions in 2007 and to invite comments on more detailed investigations into whether Ecuador and the Dominican Republic had discontinued tax exemptions for US-registered aircraft in 2008 and 2010 respectively. [8] In 2006, the United States discontinued tax exemptions for aircraft registered in Bolivia, after Bolivia was found to have ceased providing "substantially reciprocal tax exemptions to aircraft of U.S. registry in connection with international commercial operations", [9] which it had previously allowed in line with Article 3 of the US-Bolivia ATA signed at La Paz on 29 September 1948, as subsequently amended in 1988.[10] However, the remainder of the US-Bolivia ATA remains in effect.

32. The use of this review mechanism by the US Secretary of the Treasury and in particular the response to Bolivia's discontinuance of reciprocal tax exemptions demonstrates that, where the other party to an ATA has waived tax exemptions on fuel, the anticipated response is for the United States to discontinue its own tax exemptions, rather than to withdraw from the relevant ATA entirely. This supports the characterisation of Article 11 of the Open Skies Agreement in the CE

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[8] Comprehensive Review of Findings of Reciprocity Eligibility, 24/08/2007, https://www.federalregister.gov/documents/2007/08/24/E7-16823/exemption-of-foreign-air-carriers-from-excise-taxes-comprehensive-review-of-findings-of-reciprocity, Review of Finding of Reciprocity (Dominican Republic), 22/09/2008, https://www.federalregister.gov/documents/2008/09/22/E8-22032/exemption-of-foreign-air-carriers-from-excise-taxes-review-of-finding-of-reciprocity-dominican; Review of Finding of Reciprocity (Ecuador), 02/06/2010, https://www.federalregister.gov/documents/2010/06/02/2010-13223/exemption-of-foreign-air-carriers-from-excise-taxes-review-of-finding-of-reciprocity-ecuador-26-usc;

[9] Discontinuance of Exemption; Republic of Bolivia, 15/06/2006, https://www.federalregister.gov/documents/2006/06/15/E6-9335/exemption-of-foreign-air-carriers-from-excise-taxes-discontinuance-of-exemption-republic-of-bolivia

[10] For the original ATA see United Nations Treaty Series, Vol. 505 at p. 139, https://treaties.un.org/doc/Publication/UNTS/Volume%20505/v505.pdf; for 1988 amendments see United Nations Treaty Series, Vol. 2204, at p. 252, https://treaties.un.org/doc/Publication/UNTS/Volume%202204/v2204.pdf.

Delft report and that the introduction of excise duties on fuel by the EU or its member states would not constitute a violation of the agreement.

The *Air Transport Association of America* case

33. Although decided in the context of an amendment to the directive regarding the EU Emissions Trading Scheme ("**ETS**"), the *ATAA* judgment and AG Kokott's accompanying Opinion are nevertheless instructive when considering the meaning of Article 11 of the Open Skies Agreement and the extent to which any infringement of it by the EU or its member states might provide a basis for legal action by affected US airlines.

34. The claimants, the Air Transport Association of America, American Airlines Inc, Continental Airlines Inc and United Airlines Inc, brought judicial review proceedings against the UK Secretary of State for Energy and Climate Change challenging the lawfulness of measures implementing Directive 2008/101/EC of 19 November 2008, which amended Directive 2003/87/EC so as to include aviation activities within the scheme for greenhouse gas emission allowance trading within the European Union. They contended that the inclusion of aviation within the EU ETS violated several principles of customary international law, as well as various provisions of international agreements, including Article 11(2)(c) of the Open Skies Agreement.[11] The High Court referred the matter to the CJEU for a preliminary ruling of the validity of Directive 2008/101.

35. Giving her Opinion, AG Kokott framed the question for the Court to determine as follows: "*whether and to what extent individuals are entitled to rely in court on certain international agreements and principles of customary international law in order to defeat an act of the European Union*." (AG §4).

36. At §§43–44 of her Opinion, AG Kokott commented on the relationship between EU and international law, noting that the European Union has legal personality under Article 47 of the Treaty on European Union ("**TEU**") and can therefore have rights and obligations under international law, and that Articles 3(5) and 21(1) of the

[11] Provisions of the Chicago Convention and the Kyoto Protocol were also relied upon by the claimants.

TEU and previous CJEU caselaw all establish that the European Union must respect its international law obligations.

37. However:

> *"this does not mean that individuals (that is natural or legal persons) may rely at will on provisions or principles of international law in court proceedings in order to defeat acts of European Union institutions. It is always necessary to determine specifically, with regard to each particular provision and principle of international law at issue, whether and to what extent it can be relied upon, in proceedings initiated by a natural or legal person, as a benchmark against which the lawfulness of European Union acts can be reviewed: the* International Fruit Co *case [1972] ECR 1219"* (AG §45).

38. At §49 she noted that, according to previous CJEU caselaw, provisions of international agreements by which the European Union is bound may be relied upon to question the validity of acts of the European Union where they are "*unconditional and sufficiently precise*".

39. At §104, she set out her view that Article 11(2)(c) of the Open Skies Agreement is "*sufficiently precise to be directly applied*" but is not unconditional:

> "*as it grants exemption only "on the basis of reciprocity". In the* International Fruit Co *case [1972] ECR 1219, para 21 the court considered the principle of reciprocity in the Preamble to GATT 1947 ("on the basis of reciprocal and mutually advantageous arrangements") to be one of several indications militating against the direct applicability of its provisions. Whether an airline can rely on this exemption at a particular point in time vis-a-vis a specific party to the Open Skies Agreement therefore depends upon the conduct of that other party at that time. A US airline can claim the exemption provided for in the Open Skies Agreement vis-a-vis European authorities only if and to the extent to which the authorities in its own state of registration at the same time grant corresponding exemptions to European airlines. In view of this condition the requirements for direct application of article 11(2)(c) of the Open Skies Agreement are not fulfilled."* (Emphasis added)

40. This paragraph of the AG's Opinion supports the interpretation of the wording of Article 11(2)(c) for which we contend. However, in its judgment the CJEU

disagreed with AG Kokott on this point, holding at §93 that, in circumstances where the United States was providing tax exemptions in accordance with Articles 11(1) and (2)(c):

> *"It follows that, as regards fuel specifically, the condition of reciprocity in article 11(1) and (2)(c) of the Open Skies Agreement does not constitute, in particular in circumstances such as those of the present case, in which the contracting parties have reciprocally performed the obligation in question, an obstacle preventing the obligation, laid down in that provision, to exempt the fuel load from taxes, duties, fees and charges from being relied on directly for the purpose of reviewing the validity of Directive 2008/101."*

41. The Court concluded at §94 that Article 11(2)(c) could be relied upon for the purpose of assessing the validity of Directive 2008/101. This was the case even in a context where an alternative dispute resolution mechanism existed under the agreement itself, in the form of meetings of the Joint Committee and arbitration. This was held at §83 not to be sufficient in itself to exclude judicial application of the agreement, by reference to *Hauptzollamt Mainz v CA Kupferberg & Cie KG aA* [1982] ECR 3641, para 20.

42. Ultimately, the AG's Opinion and the judgment of the CJEU were agreed that Directive 2008/101 was not invalidated by Article 11(2)(c) of the Open Skies Agreement. The CJEU's primary reasoning for this conclusion, and the AG's alternative reasoning, was that the requirement to acquire and surrender emission allowances for flights arriving or departing from European airports was not a revenue raising exercise for public authorities but rather a market intervention designed to promote the greatest reductions in greenhouse gas emissions at the lowest cost, and it did not therefore constitute a tax (AG §§214–216; Judgment §§136–147).

43. At §143, the CJEU explicitly distinguished between the EU ETS and a fuel tax on consumption, which had been held to breach the exemption in the relevant directives in *Braathens Sverige AB, formerly Transwede Airways AB v Riksskatteverket* (Case C-346/97) [1999] ECR I-3419, at §23 (notably, those directives did not include wording referring to reciprocity in the same way as Article 11).

44. There is clearly a tension between the AG's Opinion at §104 and the Court's judgment at §93. [12] The CJEU concluded that, because each Party to the Open Skies Agreement had hitherto granted the tax exemptions provided for under Article 11 to aircraft registered in the territory of the other Party, that rendered the provision unconditional and thus able to be relied upon directly in the courts. The unconditional nature of the provision was dependent on the prior conduct of the Parties. Yet any decision by the EU Commission to amend the Energy Taxation Directive so as to impose new excise duties on aviation fuel would seem necessarily to constitute a failure to perform its reciprocal obligations under Article 11 of the Open Skies Agreement. The CJEU also recognised at §137 that the provisions of the Open Skies Agreement prohibiting certain forms of taxation were "subject to reciprocity".

45. To push the logic of the Court to its ultimate conclusion, in circumstances where conditionality is dependent on prior conduct, a decision by the EU to break with prior conduct and impose excise duties on fuel could be argued to render Article 11 conditional. In such circumstances, the Court might conclude that the provision could no longer be relied upon directly in any future legal challenge by US carriers against a hypothetical fuel tax. In essence, this logical 'next step' from the CJEU's reasoning at §§92-93 accords with the Opinion of AG Kokott at §104, notwithstanding the fact that they came to different conclusions on the applicability of Article 11(2)(c) in the specific circumstances of the *ATAA* case.

46. Overall, there is a risk that airlines based in the United States would seek to challenge the validity of EU legislation introducing a fuel tax within the European Courts on the basis of lack of compatibility with Article 11 of the Open Skies Agreement and the *ATAA* case does provide some authority for their ability to do so. However, there is also a case to be made that the AG's Opinion and the ultimate logical extension of the Court's own reasoning indicate that Article 11 would cease

[12] For further discussion of the implications of the judgment see Szilárd Gáspár-Szilágyi, 'EU international agreements through a US lens: different methods of interpretation, tests and the issue of "rights"', *European Law Review* 2014, 39(5), 601-625.

to be directly applicable in circumstances where one of the Parties to the agreement was explicit about its lack of compliance with the tax exemptions set out therein.

Other relevant caselaw

47. While the *ATAA* case and the other judgments cited within it and above are the most relevant for present purposes, two other cases from the domestic courts of (at the time) EU Member States are also worth consideration.

48. In *R (on the application of the Federation of Tour Operators and Others) v Her Majesty's Treasury* [2007] EWHC 2062 (Admin); [2007] ACD 105, the High Court of England and Wales held that Article 15 of the Chicago Convention did not apply to the UK's air passenger duty (a per-flight tax on passengers) because it considered that the prohibition on charging "dues" did not intend to prohibit taxes, or the Convention text would clearly and unequivocally have referred to "taxes".[13] Mr Justice Stanley Burnton (as he then was) held that, read in context, the prohibition on charging "*fees, dues or other charges*" should be construed as a most-favoured-nation or anti-discrimination provision.[14] Since the tax was charged on all aircraft regardless of state origin, and charged even domestic flights, it did not give its national carriers an advantage or significantly disadvantage any particular state carriers and did not therefore contravene Article 15 of the Convention.

49. The tax exemptions found in various US ATAs, including the Open Skies Agreement, can be characterised as most-favoured nation provisions. Article 3 of the US-Bolivia ATA, which previously guaranteed reciprocal tax exemptions for US- and Bolivian-based aircraft but from which both parties had derogated by 2006, was explicitly framed in the text of the agreement as a "*most-favored nation*"

[13] Note that the French, Spanish and Russian language versions of the Convention text *do* refer to taxes, a fact which is acknowledged and considered in the judgment at §§52-54. The English-language version is the only one which does not.

[14] Note that this judgment was unsuccessfully appealed, but on grounds other than the meaning of "dues" in Article 15 of the Chicago Convention.

provision designed to "*prevent discriminatory practices and to assure equality of treatment*" (see above at §§[xx]).

50. The Dutch Supreme Court also distinguished between taxes and other charges in relation to the Chicago Convention in *Board of Airline Representatives in the Netherlands* v *The State of The Netherlands* (2009) Supreme Court, Civil Chamber, 10/7/2009, 08/04121, NJ, concluding that the so-called 'Dutch ticket tax' did not infringe Article 15 of the Convention. The Court agreed with the conclusions of Advocate General PJ Wattel at §7.2 of his Opinion that the drafters of the Chicago Convention aimed to prevent the imposition of protectionist tariffs with Article 15 and cannot have had in mind the kind of regulatory environmental taxes or consumption taxes designed to make the true social and environmental cost of kerosene pollution visible, of which the Dutch ticket tax was one. At §7.13, AG Wattel also cited the judgment of Stanley Burnton J in the *Federation of Tour Operators* case.

51. There is precedent in domestic European courts, therefore, for finding aviation consumption taxes compatible with Article 15 of the Chicago Convention and as noted above, the CJEU in the *ATAA* case at §91 found Article 11 of the Open Skies Agreement to be an evolution of earlier obligations found in the Chicago Convention.

52. Neither of these two cases are referred to in the *ATAA* judgment. Should any hypothetical fuel tax be litigated in the CJEU, these cases provide a useful precedent for an argument that Article 11 of the Open Skies Agreement should be construed narrowly as an anti-protectionist measure, which does not prohibit the introduction of regulatory environmental taxes.

CONCLUSIONS

53. To conclude:

    a) For all the reasons set out above, we consider that, both logically and contextually, the correct interpretation of the exemptions in Article 11 of the Open Skies Agreement is that they are not absolute, but rather that Article

11 represents an agreement that if one Party begins to tax fuel, the other may do so too.

b) The US Internal Revenue Code, section 4221, provides a mechanism for the United States to review and potentially revoke tax exemptions for foreign aircraft in circumstances where they are no longer being reciprocally provided. This mechanism has been used to review many countries' reciprocal exemptions under various bilateral ATAs and in the case of Bolivia to discontinue the exemption. This is significant for two reasons. First, because it shows the intention of the parties to the Open Skies Agreement was that the tax exemptions contained in Article 11 be contingent upon continuing and *reviewable* reciprocity. Second, because, in practical terms, were the European Union to introduce a fuel tax, the US Federal Government would likely revoke reciprocal exemptions under this mechanism, but the rest of the Open Skies Agreement ought to remain in force. Although, there is a risk that the United States would seek to rely upon the enforcement mechanisms in Articles 18 and 19 of the Open Skies Agreement (the Joint Committee followed by Arbitration).

c) There is also a risk that US-based airlines or industry bodies would seek to challenge the validity of any EU legislation introducing a fuel tax within the European courts, as they did in relation to the introduction of allowance trading for aviation under the EU ETS. The *ATAA* case is *prima facie* authority for the proposition that Article 11(2)(c) of the Open Skies Agreement may be directly relied upon by individuals to challenge the validity of EU legislative acts. However, the position if a Party to the Agreement were explicitly to cease performing its reciprocal obligations under Article 11 is rather less than clear cut. A case could be made that the Article would no longer be unconditional in such circumstances and therefore no longer directly applicable.

d) There is some limited authority from national courts for the proposition that, even leaving aside questions of reciprocity, the tax exemptions under the

Open Skies Agreement – as an evolution of earlier obligations under the Chicago Convention – are not intended to encompass regulatory environmental taxes in any event, and the Article 11 should be construed narrowly as an anti-discrimination, most-favoured nation provision. However, this question has not been tested by the CJEU and such an argument is rather speculative.

54. A summary of our advice is given in §2 above. Please do not hesitate to contact us if anything requires clarification, or if we can be of further assistance.

22 July 2024

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