



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 30.11.2006  
COM(2006) 742 final

**COMMUNICATION FROM THE COMMISSION TO THE COUNCIL**

**in accordance with Article 19(1) of Council Directive 2003/96/EC (private pleasure-flying)**

## **1. INTRODUCTION**

In accordance with Article 19(1) of Council Directive 2003/96/EC<sup>1</sup> restructuring the Community framework for taxation of energy products and electricity (hereafter referred to as the "Energy Tax Directive" or the "Directive"), in addition to the provisions foreseen in the Directive, in particular in its Articles 5, 15 and 17, the Council acting unanimously on a proposal from the Commission, may authorise any Member State to introduce further tax exemptions or tax reductions for specific policy considerations.

The Commission shall examine the requests. Afterwards, it shall either present a proposal to the Council or, alternatively, shall inform the Council of the reasons why it has not proposed the authorisation of such a measure.

Within a broader framework of review of derogations expiring in the Energy Tax Directive by the end of 2006, France, Portugal, the United Kingdom, Malta and Sweden submitted a request for authorisation to derogate from 2007 onwards from the provisions of the Energy Tax Directive for fuel used for private pleasure-flying, i.e. air navigation not covered by the obligatory exemption provided for in Article 14 (1) (b) of the Energy Tax Directive. These letters were registered with the Directorate General for Taxation and Customs Union<sup>2</sup>.

The purpose of this communication is to inform the Council of the reasons why the Commission has not proposed such authorisation.

## **2. SUMMARY OF THE REQUEST**

### **2.1. The French request**

France would like to apply a full tax exemption to fuel used for private pleasure flying. The aim of the measure is to compensate the negative consequences for the sector derived from the increase in prices and on the other hand, to preserve national policies oriented to organize the territory avoiding the concentration of companies around the Parisian region.

The request foresees a date of termination by 31 December 2012.

### **2.2. The Portuguese request**

Portugal would like to apply a full tax exemption to fuel used for private pleasure flying. The purpose of the measure is to avoid the administrative burden derived from the need to implement a complex system of control related to the shift to the standard tax treatment.

The request foresees a date of termination by 31 December 2012.

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<sup>1</sup> Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for taxation of energy products and electricity (OJ L 283 of 31.10.2003 p. 51; Directive last amended by Directives 2004/74/EC and 2004/75/EC (OJ L 157 of 30 April 2004, p. 87 and p.100).

<sup>2</sup> Letters registered on 16 October 2006 (France, Portugal, United Kingdom and Malta) and on 31 October 2006 (Sweden)

### **2.3. The United Kingdom request**

The United Kingdom would like to apply exemption from excise duties to fuel used for the purpose of private pleasure flying. Private use of jet fuel would be fully exempted from duties and aviation gasoline would be taxable at a reduced rate of half the tax rate for leaded gasoline.

The United Kingdom maintains that there are minimal benefits from the shift to the standard tax treatment in comparison to the costs and other consequences associated with the expiry of the derogation. Therefore the main objective of the measure is to avoid costs of transition.

In particular, the United Kingdom highlights the compliance costs on suppliers of aviation fuels and on the industry and stress the administrative costs and enforcement difficulties for the administration associated with the expiry of the derogation. The United Kingdom further explains the negative effects on both the private pleasure-flying sector and many small businesses associated with it. Furthermore, it would increase the cost of training which would grow the trend for pilots to train in the United States. In addition, removing the derogation would raise safety issues if users were tempted to put unleaded petrol rather than aviation gasoline. On the other hand, the United Kingdom points out the insignificant revenue gain and the small benefit in terms of carbon emission saved associated with introduction of the general tax treatment.

The request foresees a date of termination by 31 December 2011.

### **2.4. The Maltese request**

Malta would like to apply full tax exemption to the jet fuel and aviation gasoline used for private pleasure flying on outbound voyages.

The purpose of the measure is to promote the development of the sector and the associated services which have an incidence in the niche tourism. According to Malta its comparative advantage in this area is being eroded by the strong competition from operators based in non-European countries which are not subject to Community excise legislation. Furthermore, Malta considers that the measure would not be detrimental to the proper functioning of the internal market nor result in distortions of competition, due to its geographical position and the rigorous controls in place to ensure the correct application of the measure

The request foresees a date of termination by 31 December 2012.

### **2.5. The Swedish request**

Sweden would like to apply full tax exemption to jet fuel and gasoline used for private pleasure flying.

Sweden refers to its extended territory and large sparsely populated areas particularly in the north and considers that well functioning means of transport and infrastructure are essential in order to maintain opportunities for all regions in Sweden to develop and be part of the economic growth. Long distances to necessary public functions are frequent, particularly in the interior parts of northern Sweden.

Furthermore, Sweden considers that a tax exemption for air fuels for private flying leads to more frequent air navigation which has a positive effect on the knowledge of the air

navigation and the willingness to carry out civil surveillance missions. Furthermore, according to Sweden, it would involve an extensive administrative burden for the tax authorities to administrate taxation of fuel for private pleasure-flying. Also, in the view of Sweden, the administration is complicated by the fact that the same plane can several times a day change between being used for private and commercial purpose.

The request foresees termination by 31 December 2012.

### 3. BACKGROUND TO THE REQUESTS

Article 14(1)(b) of the Energy Tax Directive states that Member States shall exempt from taxation energy products supplied for use as fuel for the purpose of air navigation other than private pleasure-flying. This provision had originally come into force in 1993 under the Mineral Oils Directive<sup>3</sup>. Private pleasure-flying<sup>4</sup> was thus not subject to the obligatory exemption set out for commercial aviation (due in particular to existing international legal obligations), nor indeed did it benefit from any optional tax advantages under the Directives. As a result, private pleasure-flying is subject to standard taxation according to national rates in compliance with the Directive, unless a particular derogation is available under Articles 18, 18a or 19 of the Directive.

With the aim of making Community transport, environment and fiscal policy more coherent, the Commission already proposed to abolish the derogations in point, now contained in Articles 18 and 18a with annexes II and III to the Directive, for the first time in 1996<sup>5</sup>. Subsequently, a gradual phasing-out of these derogations was initiated by the Commission in 2000 when it stated that these derogations should end with the forecasted entry into force of the Energy Tax Directive or, in any case, at the latest on 31 December 2002<sup>6</sup>. In the end, the derogations were extended until 31 December 2006 and were later incorporated into the Energy Tax Directive (Article 18 and Annex II) with the view to allow for their smooth phasing-out. The same termination date was chosen for Malta in the context of its accession to the Community (Article 18a and Annex III).

In its June 2006 Communication *Review of derogations in Annexes II and III of Council Directive 2003/96/EC that expire by the end of 2006* (hereafter referred to as "the 2006 Communication")<sup>7</sup> the Commission stated that the favourable tax treatment of fuel used for the activity in point, compared to fuel used for comparable (transport or leisure) activities, should not be renewed. The Commission has at the same time invited the Member States in case they consider that for specific policy considerations a further derogation is still necessary

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<sup>3</sup> Council Directive 92/81/EEC of 19 October 1992 on the harmonization of the structures of excise duties on mineral oils (OJ L 316 of 31.10.1992); Directive repealed together with Council Directive 92/82/EEC of 19 October 1992 on the approximation of the rates of excise duties on mineral oils as from 31 December 2003 by means of Council Directive 2003/96/EC.

<sup>4</sup> 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.

<sup>5</sup> COM (1996) 549 of 14 November 1996.

<sup>6</sup> COM (2000) 678 of 15 November 2000.

<sup>7</sup> COM(2006)342 of 30 June 2006 *Review of derogations in Annexes II and III of Council Directive 2003/96/EC that expire by the end of 2006*.

to submit a request in accordance with Article 19 of the Directive duly justifying the policy needs.

#### 4. EVALUATION BY THE COMMISSION

The Commission considers that France, Portugal, the United Kingdom, Malta and Sweden have to an important extent merely reiterate arguments already examined in the 2006 Communication (in particular high compliance and administrative costs and risk of fraud related to the expiry of the derogation)<sup>8</sup>. Neither these nor the more detailed and/or complementary arguments put forward at this stage are valid, in the Commission's view.

At the outset, the Commission would like to recall that the Council, acting unanimously under the procedure set out in Article 93 EC, has already had the opportunity to strike a balance between policy considerations that might plead in favour of a derogation in the area at stake, on the one hand, and those pleading in favour of standard taxation, on the other. The latter interests are fundamentally those set out in Article 19(1), third indent, of the Directive and include the proper functioning of the internal market, the need to ensure fair competition and Community health, environment, energy and transport policies.

As mentioned in the 2006 Communication, the Council has deliberately chosen, as a general regime, to subject private pleasure-flying to standard taxation. It was excluded from the obligatory exemption under Article 14(1)(c) of the Energy Tax Directive and not included into the list of optional exemptions or reductions set out in Article 15 of the Directive. It follows from the 23<sup>rd</sup> recital of the Directive that air navigation other than private pleasure-flying was exempted for particular reasons only, which according to the same recital, do not apply to private-pleasure flying itself. At the same time the Council has indicated that the derogations in favour of the latter activity should only be temporary in nature (30<sup>th</sup> recital and Articles 18 and 18a with annexes II and III to the Directive).

Against this background, an authorisation under Article 19 should not be granted for reasons which are merely inherent in the switch from the derogation to standard taxation. This applies obviously to the administrative burdens and compliance and/or enforcement difficulties, including safety issues<sup>9</sup> resulting from the change itself. It also applies, however to the general business consequences (for the sector, for associated businesses, tourism or training industry) that could follow from standard taxation of the activity in question, even in a longer term perspective. By definition, such general consequences do not correspond to the notion of specific policy considerations within the meaning of Article 19 of the Energy Tax Directive.

The interests and policies set out in Article 19 (1), third indent, equally oppose the granting of an authorisation by reference to the above mentioned grounds.

From the point of view of the **internal market and fair competition**, it must be pointed out that due to the very nature of aviation, the completion of the internal market required that common rules for taxation of aviation fuel were established for the Community as of 1993. Such rules were established as the most common denominator of practices existing in the EU Member States at that time and included common treatment of private pleasure flying. More

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<sup>8</sup> Cf. the 2006 Communication, *sub* 2.2.1.

<sup>9</sup> As regards environmental and safety aspects, these are dealt with in corresponding legislation. They are unrelated to the rules of the Energy Tax Directive.

generally, the interests of the internal market and fair competition imply that taxation should be as neutral as possible to avoid tax induced behaviour within the Community without fiscal frontiers.

The derogation granted to several Member States does not affect this reasoning. It should be considered as aimed at overcoming initial difficulties encountered with the implementation of a new legislation. Taking into account that fuel used in private pleasure flying has, in principle, been taxable in the Community since 1993 and that Articles 18 and 18a of the Energy Tax Directive have put a clear time limit to the corresponding derogation within this Directive, those reasons of transitional nature do not justify, today, an authorisation under Article 19 of the Directive.

To the extent that any anticipated loss of business activity (as alleged by some of the Member States concerned by the derogation) would reflect corresponding gains of Member States applying standard taxation, this would confirm that reasons of fair competition plead against the granting of an authorisation under Article 19 of the Directive, which would perpetuate the distortion.

The authorisation requested would also contradict the Community **environment, energy and transport policies**, primarily because it does not accurately reflect negative external costs of such activity.

It is appropriate, in addition, to consider certain more specific arguments raised by some of the applicant Member States.

First, the Commission cannot accept the argument presented by Malta. It is true that harmonised taxation may in certain cases have effects on competition with third countries. However, these have already been taken account by the Council within Article 14 of the Energy Tax Directive. In this regard, the Council has found that these aspects warrant so far an exemption in the case of commercial navigation, but not in the particular field concerned by the present communication, namely private pleasure-flying (cf. 23<sup>rd</sup> recital of the Energy Tax Directive).

Secondly, with respect to the Swedish argument concerning the specific nature of its territory and the need for well functioning means of transport and infrastructure, the Commission does not consider that tax exemption for fuel used in air navigation is the right policy response to such argument. More in general, also with reference to related arguments presented by Sweden (e.g. the willingness to carry out civil surveillance missions) and to the arguments made by France regarding regional development, the Commission would like to stress that they relate to concerns of national policies primarily of regional nature and that these might, in a Member State's view, justify corresponding public support. However, there are means of supporting such aims that are much better fitted, both in nature and in scope, without the community interests mentioned above being affected by an anomalous exemption from harmonised taxes. As a consequence, the said general concerns raised by France and Sweden cannot justify the authorisation sought for.

Finally, the Commission cannot accept the proportionality argument raised by the United Kingdom. This argument takes the temporary derogation granted under Article 18 as the starting point, which directly conflicts with the fact that the Community legislator, acting in accordance with Article 93 EC, has set standard taxation as the starting point. This also puts into the right perspective a related argument made by the United Kingdom, namely that

environmental benefits of a switch to standard taxation would be limited. The mere fact that the overall consumption through private pleasure-flying may not exceed certain limits simply means that the exemption is limited in reach. It does not mean that proportionality would require unequal treatment with comparable transport or leisure activities. Moreover, the fact that the implementation may require some extra effort cannot be decisive either. It is in the nature of tax administration that implementing costs may differ across the various fields, and this does imply specific policy considerations which would need to be taken into account in the context of Article 19 of the Directive.

## 5. CONCLUSION

All in all the Commission considers that the applicant Member States have not presented any specific policy considerations that would justify the need to further derogate from the legislation enacted in the EU on unanimity at two occasions already and that would justify the existence of a fiscal measure that clearly contradicts several Community policies.

The Member States concerned have had enough time to adjust to the new situation taking into account that this and similar derogations have been under discussion in the Community at least since 1996 and the Commission repeatedly insisted on the necessity to phase them out. This is equally valid for Malta in which case the time limit for the derogation under Article 18a of the Energy Tax Directive was fixed so as to coincide with the time limit fixed for similar derogations available at that time for some of the fifteen existing Member States.

Should the expiry of the derogation cause difficulties in very specific or particular circumstances, and provided that they respect Community law in all respects<sup>10</sup> the applicant Member States may adopt measures aimed at alleviating or mitigating problems of transition to the regime of standard taxation.

The Commission therefore concludes that the conditions set out in Article 19 are not fulfilled. Consequently, **the Commission does not propose the authorisations requested.**

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<sup>10</sup> Including, in particular, the Treaty rules on State aids.