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FLYING WITHIN THE EUROPEAN UNION

The “airline” VAT exemption in the European Union

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OPMAS

All AOC holders can be "airlines" if their operation is chiefly international

On July 19th 2012 the European Court of Justice (ECJ) gave a judgment - a preliminary ruling - in a case (C-33/11) referred to it by the Finnish courts. The questions submitted were (in other words):

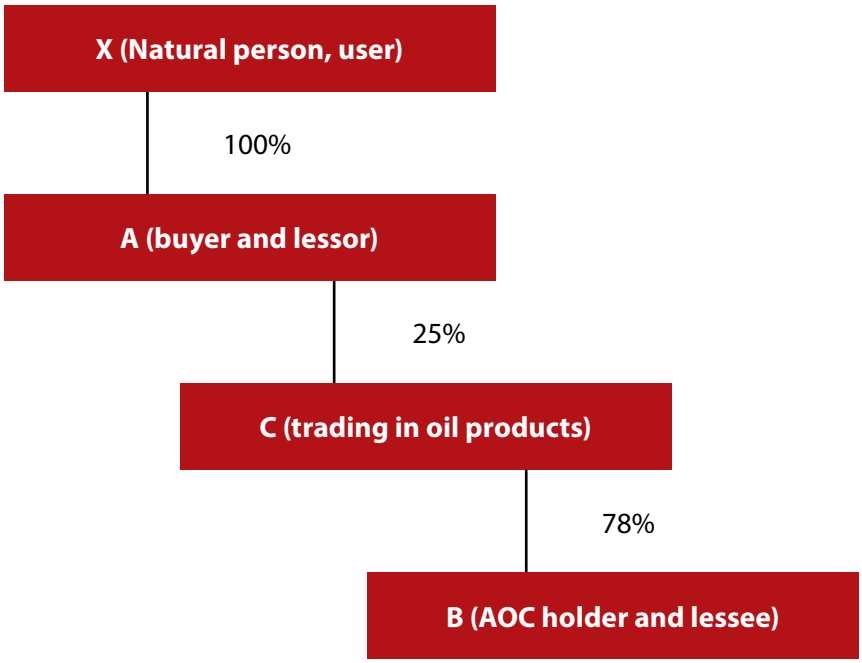
1 - Is a charter operator also an "airline"? The short answer is YES!

2 - Must it be the airline itself taking supply? The short answer is NO!

3 - Does the actual usage of the aircraft matter? The short answer is it doesn't matter a lot.

Read on!

In 2002 and 2004 respectively, the Finnish company A acquired two jet aircraft from a French manufacturer. A was registered as the owner of the aircraft while B, a company which operates as an international charter operator, was registered as their user. Natural person X owns all of the share capital in A. For its part, A owns 25% of C, while B is 78% owned by C.



Under the contract concluded between the two companies, B was entitled to lease the aircraft from A for its own commercial purposes and to invoice the latter company for maintenance work on the aircraft and for flights.

A's total turnover for the accounting periods from 1 January to 31 December 2002, on the one hand, and from 1 January 2003 to 30 June 2004, on the other, consisted entirely of accounting entries made on the basis of sales invoices addressed to X. Those invoices addressed to X, the owner of A, were based on the invoices, which B issued to A for use of the aircraft. Likewise, the expenditure entries relating to the aircraft primarily concerned the invoices issued by B for the maintenance of the aircraft and flights. The tax inspection found that the invoices had been passed on to X virtually unchanged and the authorities challenged the whole setup. It was then brought before the Finnish administrative court.

The court stated that the acquisition of the aircraft constituted a taxable intra-Community acquisition of goods which A had failed to declare, and that A did not operate on international routes, but rather that it acted in practice as the owner of C, which was engaged in international oil product trading. According to a statement made by B about its activities, that company did not use the aircraft on international routes. The agreement between the two companies was aimed exclusively at taking care of the personal transport needs of X. Accordingly, the administrative court concluded that A was not entitled to a deduction or refund of the VAT payable on the intra-Community acquisition of goods.

On appeal the higher court referred the questions above to the ECJ for a preliminary ruling.

To be specific for the legal minds: the reference for a preliminary ruling in the case concerned the interpretation of the VAT exemption applicable to the supply of aircraft to be "used by airlines operating for reward chiefly on international routes", (Article 15(6) of Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment (OJ 1977 L 145, p. 1), as amended by Council Directive 92/111/EEC of 14 December 1992 (OJ 1991 L 384, p. 47) ('the Sixth VAT Directive'))

Is a charter operator also an "airline"?

The first question is if a charter operator qualifies for 0% VAT or it must be an airline with scheduled flights? The Advocate General was of the opinion that ANY AOC holder with mainly international traffic (more than 50-55-60% as regulated by national law) qualifies for VAT exemption.

I agree with this and the Danish VAT act and the practise by Customs in Denmark is also in line with this. We have handled imports successfully for several international charter operators including helicopter operators at 0% VAT based on the AOC VAT exemption.

That said I feel it is prudent to add that in my opinion non-AOC holders - regardless of their traffic pattern - do not qualify as an airline. Obviously I know that some service providers and Customs in specific member states are of different opinions however it is my firm belief that it has no sound basis in the Sixth VAT directive and if contested would never fly with the ECJ... The Advocate General specifically mentions the complexity and the cost involved in getting an AOC as one of his reasons for granting the VAT exemption ref. the grey box on page 4.

Since exceptions to the general principle, that VAT is to be levied on all services supplied for consideration by a taxable person, are to be interpreted strictly I see no way this privilege can be extended to non-AOC holders.

Effective lobbyism has paved the way for such interpretations however the companies using such a scheme run the risk of a retrospective reversal of their exemption should the ECJ at some point decide on this matter.

I will go so far as to say that that last interpretation - that non-AOC holders in relation to VAT can be airlines under certain circumstances - is so far out that it has not even been considered by the Advocate General.

Here is the Advocate Generals suggestion as to question 1:

Article 15(6) of the Sixth Directive must be interpreted as meaning that the concept "airline operating for reward chiefly on international routes" also refers to a commercial airline operating for reward chiefly on international charter routes for the requirements of companies and private persons.

Here is the wording from the judgment:

The wording 'operating for reward on international routes' within the meaning of Article 15(6) ... ... must be interpreted as encompassing also international charter flights to meet demand from undertakings and private persons.

Must it be the airline itself taking supply?

The second question relates to VAT exemption being granted to e.g. a leasing company, which in itself does not qualify as an airline but leases to a qualifying airline. The Advocate General is of the opinion that a supplier to a qualifying airline can use the exemption also and I agree with that. It is quite clear from the text also in the Danish VAT Act - "aircraft **used** by an airline". Here is the Advocate Generals suggestion as to question 2:

Article 15(6) of the Sixth Directive must be interpreted as meaning that the exemption provided for therein applies not only to that supply of aircraft which takes place directly to airlines operating for reward chiefly on international routes, but also to the supply of aircraft to an operator which does not itself operate for reward chiefly on international routes, but which in turn supplies the aircraft for the use of an airline which carries on that activity.

> Further, it should be borne in mind that in order for an aircraft to be used for the commercial transportation of cargo or passengers, it is necessary to obtain a number of specific permits, which make it easier to establish that that aircraft will in fact be used by an airline.

Accordingly, there is nothing to preclude the application of the exemption in those cases, provided that it is known at the time of purchase of the aircraft that that aircraft is to be used by an airline of the kind referred to in Article 15(6) of the Sixth Directive and proof of that fact is submitted to the tax authorities.

Here is the wording of the judgment:

Article 15(6)... ..., must be interpreted as meaning that the exemption for which it provides also applies to the supply of an aircraft to an operator who is not itself an 'airline operating for reward chiefly on international routes' within the meaning of that provision but which acquires that aircraft for the purposes of exclusive use thereof by such an undertaking.

Further to the statement above with this it is even harder to justify that a supply to a non-AOC holder with no permits or supervision by a NA/CAA should be exempt.

Does the actual usage of the aircraft matter?

In its third question, which to a certain extent supplements the previous question, the referring court asks whether, having regard to the reply given to the second question, any of the facts of the instant case are significant, in particular, the fact that the company which owns the aircraft in turn makes a charge for the use of the aircraft to a private person who is that company's shareholder and who uses the procured aircraft principally for his own business and/or private use, taking into account the fact that the airline has also been able to use the aircraft for other flights.

The view is that those facts set out in the order for reference are of no significance in relation to the reply to the second question and do not, in principle preclude the grant of the exemption concerned to an operator which assigns the right to use the procured aircraft to an airline operating on international routes.

As pointed out above, it is clear from Article 15(6) of the Sixth Directive that the sole criterion for determining the applicability of the exemption is whether an aircraft is used by an airline operating for reward chiefly on international routes.

Here is the Advocate Generals suggestion as to question 3:

If the company, which acquired the aircraft, is able to prove that the aircraft are effectively used for commercial exploitation by an airline of that kind, any commercial or other relationship which may exist between the company which owns the aircraft, its majority shareholder and the airline itself should not have any effect as regards VAT.

Thus, although there is partial use of the aircraft by the owner, which is responsible for meeting certain costs, and although the operation as a whole may be advantageous to the owner from a non-VAT tax perspective, none of those factors are ***of any significance*** *for the purposes of the exemption if the airline exploits the aircraft commercially in the course of its ordinary activity.*

Only if it can be established that the aircraft are not genuinely intended to be exploited commercially by the airline and that instead they are solely for private use – in short, final consumption – by a natural or legal person, will it be possible to refuse the exemption on the ground that the conditions laid down in Article 15(6) of the Sixth Directive are not satisfied. In any event, it is for the national courts to assess all those matters.

Here is the wording used in the judgment:

The circumstances referred to by the national court, namely the fact that the purchaser of the aircraft passes on the charge corresponding to its use to an individual who is its shareholder and who uses that aircraft essentially for his own business and/or private purposes, with the airline also having the opportunity to use it for other flights, are not such as to affect the answer to the second question.

Before anyone gets too excited it should be borne in mind, as pointed out by the Finnish Government in its observations, that it is common ground that the application of the European Union legislation cannot be extended to cover abusive practices by economic operators, that is to say, transactions carried out not in the context of normal commercial operations, but solely for the purpose of wrongfully obtaining advantages provided for by European Union legislation, and that that principle of prohibiting abusive practices also applies to the sphere of VAT (see, inter alia, Case C-255/02 Halifax and Others [2006] ECR I-1609, paragraphs 69 and 70 and the case-law cited).

The effect of that principle is therefore to prohibit wholly artificial arrangements which do not reflect economic reality and are set up with the sole aim of obtaining a tax advantage (Case C-162/07 Ampliscientifica and Amplifin [2008] ECR I-4019, paragraph 28).

Thus, in the interpretation of the Sixth Directive, an abusive practice can be found to exist if, firstly, the transactions concerned, notwithstanding formal application of the conditions laid down by the relevant provisions of that directive and the national legislation transposing it, result in the accrual of a tax advantage the grant of which would be contrary to the purpose of those provisions and, secondly, it is apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain such a tax advantage (see Halifax and Others, paragraphs 74 and 75, and Case C-425/06 Part Service [2008] ECR I-897, paragraph 42).

It is for the national court to verify in accordance with the rules of evidence of national law, provided that the effectiveness of European Union legislation is not undermined, whether action constituting such an abusive practice has taken place in the case before it (Halifax and Others, paragraph 76).

So what can be learned from this?

Well - it all corresponds perfectly with the way this has been handled in Denmark so far. Charter operators can be airlines. A leasing company leasing an aircraft to a qualifying airline may take supply of that aircraft without the seller charging VAT or paying import VAT. Any aircraft used by a qualifying airline is VAT exempt. That includes aircraft not listed on the OS under the AOC for example the N-registered single engine turboprop used by the airline management only or aircraft used by an Aircraft Training Organization (ATO) - as long as the ATO is part of a qualifying airline.

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It is noteworthy that the French seller sold using the EU reverse charge VAT rules, which was a mistake. The buyer did not declare the purchases as intra-Community acquisitions nor as VAT exempt purchases, which was also incorrect. The sales should have been VAT exempt. These mistakes had no effect on the result though.

If you have any questions or comments, please do email me directly: lr@opmas.dk

Best regards
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EXTRA RESOURCES
The European Court of Justice

The entire judgement

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At OPMAS, we have dealt with aircraft customs handling for more than two decades. Since the beginning of the EU Single Market in 1992, we have imported more than 3,000 aircraft, which is the only service we provide; we are not involved in offshore tax structures, tax planning, or yachting. We strictly focus on aircraft importation and admission matters for aircraft owners and operators flying within the EU. Over these last 20 years, we have learned that long-term local presence and know-how are essential for aircraft importation and admission to avoid unpleasant surprises. Our acquired knowledge and expertise and invaluable approach with the Danish authorities ensure a smooth handling process.

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