



6 November 2013

VIA E-MAIL

Mr. Joseph L. Andrus
Head of the Transfer Pricing Unit
Centre for Tax Policy and Administration
OECD
2, rue André Pascal
75775 Paris Cedex 16
France

E-mail : TransferPricing@OECD.org

Re: OECD Memorandum on Transfer Pricing Documentation and Country By Country Reporting

Dear Mr. Andrus,

On behalf of the International Air Transport Association (IATA), I am writing to express our interest in the work to be undertaken by the OECD following release of its Memorandum on Transfer Pricing Documentation and Country By Country Reporting (dated 3 October 2013) (“Memorandum”) ahead of an OECD Working Party meeting and public consultation process in November 2013.

The Memorandum outlines important implementation issues identified by the OECD in developing a template for the country by country reporting of income, taxes paid and economic activity to governments. We understand this work reflects the OECD’s BEPS Action Plan in addressing transfer pricing documentation and performance of risk assessment by governments.

IATA is the trade association for the world’s airlines, representing some 240 airlines or 84% of total air traffic. The outcome of the OECD’s discussion on, and development of, country by country reporting is extremely important to the IATA membership, and we believe we could contribute very constructively to the OECD’s analysis of the issues. Accordingly, we have prepared the attached preliminary comments on the Memorandum.

I would also like to take this opportunity to express IATA's interest in contributing further to any ongoing work the OECD may undertake with respect to this specific development.

Please do not hesitate to contact me if you would like to pursue this offer of further dialogue.

Thank you very much for your kind consideration of this letter.

Sincerely,

A handwritten signature in black ink, appearing to read 'Charlotte Fantoli', with a stylized flourish at the end.

Charlotte Fantoli
Manager, Industry Taxation
fantolic@iata.org

Attachment: IATA Preliminary Comments on the Memorandum

CC: Pascal Saint-Amans, Director, Centre for Tax Policy and Administration, OECD

Jacques Sasseville, Head of Tax Treaties Unit, OECD

INTERNATIONAL AIR TRANSPORT ASSOCIATION (IATA) :
PRELIMINARY COMMENTS ON OECD’S MEMORANDUM ON TRANSFER PRICING DOCUMENTATION
AND COUNTRY BY COUNTRY REPORTING

Introduction

1. IATA is the trade association for the world’s airlines, representing some 240 airlines or 84% of total air traffic. Our member companies are based in over 125 countries and engage in air transport operations in virtually every country around the globe.
2. Our member companies’ ability to conduct their air transport operations without facing crippling compliance burdens and multiple taxation risks depends almost entirely upon the consensus in favor of exclusively residence-based taxation of airlines’ income from international traffic, as reflected in Article 8 (Shipping, inland waterways transport and air transport) of the UN Model Tax Convention and in the identical language of Article 8 of the OECD Model Tax Convention.
3. Many of the countries, in which our member companies have their effective management or residence, have concluded income tax treaties which reflect the terms of the abovementioned Article 8.
4. Action 13 in the OECD’s BEPS Action Plan calls on the OECD to develop requirements for taxpayers to report income, taxes paid and indicators of economic activity to governments according to a common template.
5. The Memorandum highlights important implementation issues to be addressed in developing a credible reporting system, specifically:
 - 1) what information should be required; and
 - 2) what mechanisms should be developed for reporting and sharing the information.

The main elements of the first issue are identifying the relevant income earned in a country that should be reported (and consequently the source of this information) and the taxes paid by country.

6. The Memorandum acknowledges that there is a need to balance the usefulness of the information reported to tax administrators for risk assessment purposes and the compliance burden placed on taxpayers. Specifically, the Memorandum notes that it would be preferable for any template to limit the required information to “data readily available to corporate management so that companies will not need to go through a time consuming and expensive process of constructing new data”.
7. Given the basis of taxation of airlines’ income from international traffic is generally residence-based, IATA has accordingly a strong interest in the manner in which the proposed reporting requirements apply to the airline industry, so as to minimize the compliance burden placed on airlines operating in multiple jurisdictions.

Tax treaties

8. The policy of including in treaties a reciprocal exemption for income from the operation of aircraft in international traffic dates back as far as the 1928 League of Nations Model Tax Convention. The rationale then was the same as it is today, namely a recognition that for businesses operating in this sector, “lack of implementation of this rule of reciprocal exemption involves either multiple taxation or considerable difficulties of income allocation in a very large number of taxing jurisdictions.”¹
9. In jurisdictions where there is no applicable tax treaty, airlines generally have to use a complicated calculation formula (either Maritime, Calcutta or Massachusetts formulas) to allocate income (and expenses) to the particular non-treaty jurisdiction. This involves time consuming administrative work and compliance costs and is the basis for why Article 8 was inserted into the Model Tax Convention.
10. As the UN’s International Civil Aviation Organization (ICAO) has further noted, decisions in favor of reciprocal exemptions were made because “multiple taxation on the ... income of international air transport, as well as taxes on its sale and use, were considered as major obstacles to further development of international air transport. Non-observance of the principle of reciprocal exemption envisaged in these policies was also seen as risking retaliatory action with adverse repercussions on international air transport, which plays a major role in the development and expansion of international trade and travel.”
11. In light of the extensive tax treaty network and the protections they afford in revenue preservation, and the regulatory requirements that airlines must meet simply in order to conduct flight operations, it is submitted that the airline industry does not produce detailed profit and loss information by country and is not generally susceptible to engaging in BEPS activity such as transfer pricing manipulation.

Transfer Pricing

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

¹ ICAO’s Policies on Taxation in the Field of International Air Transport (Third Edition – 2000), Doc 8632.
<http://www.icao.int/publications/pages/publication.aspx?docnum=8632>

Compliance costs

13. The Memorandum has highlighted the difficulty of reporting income for multinational groups. This difficulty is also exacerbated for airlines, as in most instances the preparation of financial statements in non-home jurisdictions is not statutorily required or produced. The industry generally operates through an overseas local branch structure because of the regulatory requirements in order to conduct flight operations. There is often no requirement under the branch structure operated by airlines for local books and records to support statutory filings. Therefore information is not available to provide the country by country suggested reports.
14. For airlines to comply with country by country reporting requirements to disclose income and taxes will require substantial and very costly system changes. These changes to the way airlines currently operate will add another layer of administration costs and burden to an industry already operating on very narrow margins.

Usefulness of reporting

15. As highlighted above the reporting of no or little corporate income tax paid in a particular country will be due to both the relevant income tax treaties and genuine economic conditions and not any BEPS activity.
16. The majority of taxes paid by airlines are ticket based departure taxes. As such the allocation of profit is not a relevant indicator of the airlines' contributions to individual countries.
17. The taxes paid by airlines are also not entirely comparable by country. In some jurisdictions, tax is levied on a gross receipts basis (for example, Philippines gross billings tax) and in others, such as where the income calculation formulas mentioned above are used, the starting point for the tax calculation may be worldwide profits with applicable adjustments. Certain tax treaties may also apply reduced tax rates based on the particular airline's place of management.
18. There may also be inconsistency between the various jurisdictions in determining the tax base in terms of defining the local jurisdiction income (for example, potential bases could be sales made in a country, sales with a leg starting in a country, or 50% of the round trip income sold for the country) and thereby further contributing to the difficulty of reporting in a particular jurisdiction. This is further complicated with the majority of sales now being online.
19. In light of the above and as a result of the treaty network, there must be a very big question mark over the value of information provided in the same format as other industries as it might serve to confuse instead of enlighten.

Other reporting suggestions

20. Further, some of the additional information suggestions to capture measures of economic activity other than income and taxes (such as revenue by location of customers, research expenditure, marketing expenditure and location of intangibles by country) are unlikely to be readily accessible from airlines' existing business systems.

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

Conclusion

22. In conclusion, it is our view that the airline industry should be exempt from country by country reporting in relation to Article 8 income as long as the tax treaties continue to allocate taxing rights to the country of residence and/or effective management of airlines.
23. Presently, due largely to Article 8, it is not appropriate or possible for airlines to provide the information outlined in the Memorandum without a substantial increase in compliance, administrative and system costs.
24. It is considered that provision of the information in the format proposed will confuse instead of providing transparency.
25. Should airlines not be exempt from such reporting, we do support a uniform (and if possible airline industry tailor-made) approach across jurisdictions as being far preferable to every country developing its own reporting requirements. However, even then, a clear framework that takes account of the peculiarities of the airline industry is imperative.

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26. IATA appreciates the opportunity to provide these comments and looks forward to working with the OECD on this development including possible exemption to address our concerns.