

April 10, 2002

**Memorandum**

Re: Aircraft Impoundment Pursuant to EU Customs and VAT Rules

*Executive Summary*

Several recent articles have focused attention on European Union (EU) customs and VAT rules governing operation of non-EU registered aircraft into and within the EU. These articles have recited instances of US aircraft being detained by French customs authorities and suggested that importation of an aircraft into the EU would eliminate the risk of detainment. This approach was also suggested at a panel seminar at the 2000 NBAA conference in New Orleans.

VATAmerica has reviewed these sources and several applicable customs and VAT rules. Although formal importation of an aircraft into the EU can reduce, but not eliminate, the potential of detainment for EU customs and VAT violations, current rules granting "temporary importation" status provide identical protection for aircraft which do not stay in the EU for extended periods. Further, formal importation does *not* license "cabotage" operations between two points within the EU (which is defined very narrowly), and formal importation may impose additional administrative VAT obligations.

Finally, depending on the nature of an aircraft's usage in the EU, income tax and regular VAT issues may be presented regardless of the aircraft's importation status.

Based on these rules, a "Do's and Don'ts" section is presented below.

*(This memorandum address EU issues. However, importation, cabotage and VAT issues discussed here are applicable in many other countries of the world.)*

*Introduction*

Articles entitled "Bizjets impounded in EU for tax violation" published in the February, 2002 issue of *Aviation International News* and "Cabotage, Customs and VAT in the European Union" in the *Business and Commercial Aviation* issue

## Memorandum Re: Aircraft Impoundment

of March, 2002 have rekindled questions about the EU customs, VAT and “cabotage” rules as applicable to US-registered aircraft.

At the NBAA Annual Conference in September, 2000, a UK-based customs advisor, Mr. Martyn Fiddler, reported that there had been some enforcement activity in France involving aircraft not registered in or “imported” into the EU. In the August, 2001 issue of NBAA’s *BAMJ*, Mr. James Cooling, an aviation lawyer and partner of Cooling & Herbers, Kansas City, discussed the EU customs and related cabotage rules and specific changes to those rules effective in May, 2001.

We have been unable to uncover any further instances of aircraft impounded or detained in the EU other than the two instances cited in the articles mentioned above. Contacts have included four US aviation lawyers, the author of the *A/N* article and a large fractional ownership management company based in the US. (We are aware of at least one instance in which a manufacturer was fined for failing to obtain a required permit to engage in a demonstration flight in France, but this does not appear to involve the importation or cabotage rules.)

The cited articles and the September, 2000 speaker suggest that the impoundment possibility can be mitigated by “importing” an aircraft into the EU, preferably through a country such as the United Kingdom imposing no VAT upon importation of an aircraft.

### *Applicable EU Customs and VAT Rules in General*

Although separate legal frameworks, the EU *Customs Code* and the EU *VAT Directives* each contain provisions allowing goods, such as an aircraft, to be imported into the EU on a temporary basis free of customs duties and local VAT, subject to certain conditions. The Customs Code is applicable to the EU customs territory generally, but the VAT Directives are implemented by local legislation in each of the 15 Member States, thus requiring inquiry into the separate States’ specific VAT rules.

If conditions for temporary importation are not satisfied, the customs authorities may consider that the goods (aircraft) have been imported without customs clearance requiring customs duties and VAT levied at the border. In such a

## Memorandum Re: Aircraft Impoundment

case, the customs authorities may detain, or impound, the goods pending satisfaction of the regular import duties and VAT. This was apparently the determination made in the two cases cited in the recent articles.

*(NB: Such exemptions apply only to the aircraft, not the passengers or their personal belongings. Individuals are always required to comply with local customs clearance and immigration procedures regardless of their mode of arrival. Personal effects required for travel are exempt from customs duties and VAT.)*

### *Temporary Importation under the EU Customs Code*

Articles 558 - 562 of the EU Customs Code, as amended by Commission Regulation 993/2001 as of 4 May, 2001, provide “total relief” from customs duties for specified uses of means of transport including aircraft. Customs Code Articles establish additional conditions when the aircraft is used only by persons “established” in the EU. There has been essentially no litigation concerning these provisions, so their exact meanings are unclear in some circumstances.

To qualify for “temporary importation” relief from customs duties, two sets of conditions must generally be satisfied, one relating to use of the aircraft and one relating to the duration of stay within the EU. When applicable, initial “temporary importation” status is conferred automatically through EuroControl clearance or the flight plan with an EU destination.

First, the “use” condition provided by Article 558 is satisfied for an aircraft that is:

- registered outside the EU by a person or company whose fiscal residence is outside the EU,
- used by a person “established” outside the EU, and
- used exclusively for transport that begins or ends outside the EU.

The first two conditions apply to both commercial and private use, and the third condition applies only to “commercial” use. For Customs Code purposes, “commercial” means charter or normal business use, and “private” means all non-commercial uses (what we’d call “personal” in the US).

## Memorandum Re: Aircraft Impoundment

Second, Article 562 contains the duration of stay conditions: six months for private use, and “the time required for carrying out the transport operations” for commercial flights. This duration of stay condition was the culprit in the reported French impoundment cases.

Because of the second “use” condition, the general exemption under Article 558 for both business and personal-use aircraft would apparently not apply if there were only EU people aboard. However, even if there are only EU persons aboard, total relief from import duties is still available under Articles 560 and 561. (It appears that the nationality determination is applied at the passenger level without regard to crew nationalities, although this is unclear.) As clarified in a letter dated August, 2000 to Air Routing International from the Director General of French Customs, as reported in Mr. Cooling’s *BAMJ* article and further discussed below, the existence of a single non-EU passenger, and probably a single non-EU crew member, satisfies this condition, notwithstanding there are EU persons aboard.

For aircraft carrying only EU persons, Article 560 provides total relief from import duties for private use of an aircraft by an EU person if the use is “occasional” and authorized by the aircraft registrant, and the aircraft registrant happens to be in the EU, though not necessarily aboard the aircraft, at the time of the flight. This exemption would appear to cover the case where the aircraft is used to ferry around the non-EU registrant’s EU friends and family.

Further, Article 561 grants total relief from customs duties when an EU person uses the aircraft for commercial or private purposes if the user is either (1) employed by the non-EU resident aircraft owner, or (2) otherwise authorized by such an owner to be aboard the aircraft. Application of (1) to employees of EU subsidiaries of a US corporate owner is unclear.

Although there has been much discussion about having non-EU persons aboard flights within the EU, there appears to be no basis in current law for denying temporary importation status based on the nationalities of the crew or passengers, IF: (1) at least one person from outside the EU is using the aircraft for any purpose, OR (2) only EU persons are aboard and at least one of the relief provisions of Articles 560 or 561 apply to every person.

This conclusion is generally supported by Mr. Cooling’s excellent article. In

## Memorandum Re: Aircraft Impoundment

addition to citing the relevant Articles of the Customs Code, he further cites correspondence to Air Routing International from the French Customs Director dated August, 2000 for the proposition that “ ... the presence onboard of passengers, whether residents or non-residents of the EU, does not affect the temporary duty-free entry” of an aircraft into the EU. He does caution, however, that it is “extremely” important either for the owner to be aboard or for the owner to provide a letter authorizing use of the aircraft by the passengers. We note that the cited French Customs Director letter indicates that business aircraft are always accompanied by “a responsible authorized person or senior employee of the (owner), (which person) is the de facto beneficiary of the aircraft’s temporary duty-free entry authorization ....”

Finally, Mr. Cooling is personally familiar with both of the French “impoundment” cases cited in the recent articles. As his article states clearly, *he does not believe that the nationality or residence of the passengers had any effect on the two impoundments*. Rather, he believes that the aircraft’s presence on the ground for extended periods of time caused the French customs authorities to find that the aircraft had been imported without proper authority, and he notes that these situations were resolved by formal importation of these aircraft into the EU through the UK. This is consistent with “use” and duration provisions under Article 558 and 562 discussed above.

### *Temporary Importation for VAT Purposes*

The 6th EU VAT Directive, as implemented by legislation in the 15 EU Member States, permits VAT-free importation of goods, such as an aircraft, on a temporary basis. Article 7 (3) of the 6th Directive states that this exemption is available for goods which qualify “under arrangements for temporary importation with total exemption from import duty”. Accordingly, the EU VAT rules, normally applied independently of the customs rules, defer for this definitional purpose to the Customs Code, and a violation of the customs conditions for temporary importation becomes a *per se* violation of the VAT rule. This is why assessment of an import VAT could be a remedy available to customs inspectors for a customs violation.

### *Importation*

## Memorandum Re: Aircraft Impoundment

Various EU countries, notably the UK, grant exemptions from customs and VAT charges upon importation of aircraft weighing more than 8,000 kg, or about 17,600 lbs. There are no similar relief provisions in France, and we have not studied the relevant law in other EU States. While formal importation prevents subsequent violations of the temporary importation customs conditions, importation does not confer local registration status and does not mitigate potential cabotage, income tax and regular VAT issues incident to EU operations.

In certain instances, formal importation may require the non-EU “importer” to register for local VAT or to appoint a local tax representative to act as the importer of record.

### *Cabotage*

“Cabotage” means the carrying of passengers or cargo within a country by a foreign carrier. Derived from the French verb “caboter”, meaning to sail along a coast, cabotage is actually a centuries-old term implying that cheaper foreign labor would disrupt or destroy local commercial carriers.

In the US, our principal cabotage law is the Jones Act, which generally requires any commercial transport between US points to be US-owned, US-crewed, US-registered and US-built. Similar restrictions are not contained in the EU Customs Code, which addresses the carriage of EU persons and cargo through the Articles cited above.

To reiterate the situation concerning carriage of EU persons, no import duties or VAT are assessed if:

- (1) the non-EU registered aircraft is operating in compliance with the general temporary importation conditions with at least one non-EU person aboard,
- (2) the non-EU aircraft is operating under the temporary import conditions with no non-EU people aboard but the EU persons each satisfy the conditions of Articles 560 or 561, or

## Memorandum Re: Aircraft Impoundment

(3) the non-EU aircraft has been formally imported into the EU, in which case carriage of passengers and cargo is subject only to local VAT and income tax rules concerning operation of a business as discussed below.

### *Further Issues*

Consideration of using the importation provisions should include a review of applicable EU income tax and VAT provisions. Companies deciding to base an aircraft in the EU would necessarily wish to take VAT and local income tax into account in planning the new operation.

Under general VAT rules, providing air transport services for compensation from a point within a VAT country constitutes the making of a VAT-taxable supply, regardless of the nationality of the passengers or cargo. When the annual value of such supplies exceeds established threshold amounts, local VAT registration is required, together with liability to charge and collect local VAT on services provided. The *de minimis* threshold amounts vary upward from about US\$ 15,000. Carriage of employees of the owner or operator for business purposes would not normally be considered taxable supplies for this purpose, but carriage of customers or prospective business partners might. There are no known instances of a customs authority asserting liability of this type against a non-EU aircraft.

An income tax issue could arise if the customs authorities determined that the aircraft, although properly imported or subject to the temporary importation exemption, was in operation between two points in the host country. US income tax treaties, including those with France, Germany and most other countries, provide that profits from operation in international traffic may only be taxed in the aircraft's home country. However, "international traffic" is usually defined in US tax treaties to exclude operations between two points in a foreign country. We are not aware of any instances in which a foreign income tax liability was asserted against the owner or operator of a US-registered aircraft.

### *Summary*

## Memorandum Re: Aircraft Impoundment

Here's a matrix that may be helpful in condensing all these rules as relate to non-EU registered aircraft.

### *Commercial-Use (Business) Aircraft (Non-Imported):*

- **OK** to fly into EU destination, then out of EU on next leg after business completed. No customs, VAT or cabotage issues, regardless of who's onboard. **DO NOT** hold out plane as available for charter. **DO NOT DALLY.**
- **OK** to fly into EU, then on to other EU destinations before concluding business and leaving EU. No customs issues unless aircraft in EU for longer than necessary to conduct the business transport. Remote possibility of VAT and income tax issues if paying customers are aboard.
- **OK** for EU person(s) if person employed by non-EU owner or otherwise authorized (writing best) by owner, regardless of travel points.
- **DO NOT** stay in EU beyond time required to carry out transport operation.
- **DO NOT** carry EU persons for compensation between two points in EU.

### *Private-Use (Personal) Aircraft (Non-Imported):*

- **OK** to fly into EU destination, then out of EU on next leg. No customs, VAT or income tax issues, regardless of who's onboard. If non-EU passengers, no restrictions as to owner or registration holder being aboard or in EU.
- **OK** to fly into EU, then on to other EU destinations while carrying **non-EU** passengers. No customs issues unless in EU longer than 6 months.
- **OK** for EU person(s) if: (1) occasional use pursuant to "instructions" (written is best) of registration holder, who may or may not also be the owner, or (2) person employed by non-EU owner or otherwise authorized (writing best) by owner.
- **DO NOT** to stay in EU longer than 6 months. Unclear what period of time must elapse between successive 6-month stays so trips can't be combined



Memorandum Re: Aircraft Impoundment

to violate 6-month rule.

- **DO NOT** hold out plane as available for charter or other business use.

*Commercial-Use (Business) Aircraft (Imported):*

- **OK** to fly into EU destination, then out of EU on next leg. No customs, VAT or income tax issues, regardless of who's onboard. **OK TO DALLY** (at least up to six months per year, then start thinking registration in the country of dalliance).
- **OK** to fly into EU, then on to other EU destinations with some dallying (see above). No customs issues. Remote possibility of VAT and income tax issues if paying customers are aboard.
- **DO NOT** hold out plane as available for charter.

*Private-Use (Personal) Aircraft (Imported):*

- **OK** to fly into EU destination, then out of EU on next leg. No customs, VAT or cabotage issues, regardless of who's onboard. **OK TO DALLY** (at least up to six months per year, then start thinking registration in the country of dalliance).
- **OK** to fly into EU, then on to other EU destinations with some dallying (see above). No customs, VAT or income tax issues.
- **OK** to take on EU persons as passengers if not paying customers.
- **DO NOT** hold out plane as available for charter or other business use.

*Further Advice and Comment*

VATAmerica is not qualified to, and does not, render legal advice. For advice concerning specific situations, we recommend that advice be sought from a lawyer qualified to practice in the area of EU law. VATAmerica would be pleased to refer EU counsel in any of the principal EU countries. In addition, there are

Memorandum Re: Aircraft Impoundment

several qualified US lawyers active in NBAA Tax Committee activities. To comment on this subject (very welcome) or to request subsequent updates of this memorandum, please contact Greg Jackson , Tax Issues Manager at NBAA, 202.783.9254 (GJackson@nbaa.org), or Jim Walker, VATAmerica, LP, 14 Washington Road, Suite 523, Princeton Junction, NJ 08550, Tel. 609.750.9060 (jdw@vatamerica.com).