# Working Draft:

## Airlines Revenue Recognition Implementation Issue

**Issue #2-10 –** Accounting for Passenger Taxes & Related Fees

**Expected Overall Level of Impact to Industry Accounting:** Minimal

## Wording to be Included in the Revenue Recognition Guide:

***Taxes and Fees***

1. Airlines are required to collect and remit a number of federal and local taxes and fees for each passenger ticket sold. In addition, airlines that fly to foreign countries likely have additional taxes imposed by the foreign government on tickets sold to passengers traveling to and from their countries.

2. In Step 3 of the revenue recognition model, an entity determines the transaction price of the contract. According to FASB ASC 606-10-32-2, “[t]he transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes).” To determine whether amounts are collected on behalf of third parties, an entity would need to identify and analyze taxes on a jurisdiction-by-jurisdiction basis to determine which amounts should be reported gross and which should be reported net. However, guidance in FASB ASC 606-10-32-2A permits an entity, as an accounting policy election, to exclude amounts collected from customers for sales (and other similar) taxes that meet certain criteria from the transaction price. An entity that makes this election should exclude from the transaction price all taxes in the scope of the election and should disclose it as a significant accounting policy in accordance with the disclosure requirements in paragraphs 1-6 of FASB ASC 235-10-50.

3. As indicated in paragraph BC34 in the “Background Information and Basis for Conclusions” section of FASB ASU 2016-12, *Revenue from Contracts with Customers (Topic 606) - Narrow-Scope Improvements and Practical Expedients,*[1] if an entity elects not to present all taxes within the scope of the policy election on a net basis, then the entity applies the guidance on determining the transaction price in paragraph FASB ASC 606-10-32-2 and considers the principal versus agent guidance in paragraphs 36-40 of FASB ASC 606-10-55 to determine whether amounts collected from customers for those taxes should be included in the transaction price.

[1] Paragraph BC34 and other paragraphs from the "Background Information and Basis for Conclusions " section of FASB ASU 2016-12, *Revenue from Contracts with Customers (Topic 606) - Narrow-Scope Improvements and Practical Expedients*, were not codified in FASB ASC; however, FinREC believes this and other paragraphs referenced in this paper provide helpful guidance and, therefore, decided to incorporate them in this paper.

4. FASB ASC 606-10-32-2A defines a tax that is subject to this election as "taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction and collected by the entity from a customer (for example, sales, use, value added, and some excise taxes)." In addition, paragraph BC33 of FASB ASU 2016-12, *Revenue from Contracts with Customers (Topic 606) - Narrow-Scope Improvements and Practical Expedients,* provides the following guidance to support identification of taxes that meet this definition and, therefore, may be excluded from the evaluation by policy:

    The Board decided that the scope of the election for taxes is the same scope as existing guidance in Subtopic 605-45, Revenue Recognition—Principal Agent Considerations, because the scope of that existing guidance is well established in practice. That scope does not include taxes imposed on an entity's gross receipts or the inventory procurement process.

5. The EITF issue summary[2] that was prepared when establishing the guidance in FASB ASC 605-45 specified the airline taxes as follows:

    **17.** Airline industry—The airline industry is subject to a number of different taxes at different points in the delivery of the service to the end-customer and specific taxes on the sale of the airline ticket to the end-customer. For example, the airline is subject to an excise tax on every gallon of jet fuel used. **The taxes that are assessed on the delivery of the service to the end customer are presented on a gross basis.** An airline is assessed a number of taxes on the sale of the airline ticket to the end-customer including the Air Transportation Taxes (AT tax), Federal Security Surcharge (flat fee per passenger), and Airport Passenger Facility Charge (flat fee per passenger). The AT tax includes, but is not limited to, the Federal Ticket Tax (7.5 percent of the ticket price), and the Federal Flight Segment Tax (flat fee per segment). All of the taxes assessed on the sale of the ticket to the end-customer are federally imposed taxes. The airlines are required to remit the taxes when the taxes are collected, but do not recognize revenue until the ticket is used by the end-customer. There can be a several month lag between the time the taxes are remitted and the revenue is recognized by the airline. The AT tax is a trust fund taxes which means that the seller is holding the money in trust for the government until the taxes are remitted. **The taxes assessed on the sale of a ticket to an end-customer are presented on a net basis.**

6. Based on the definition in FASB ASC 606-10-32-2A, taxes assessed by a governmental authority have to meet both of the following criteria in order to be subject to the policy election: 1) they have to be "imposed on and concurrent with a specific revenue-producing transaction" and 2) they have to be "collected by the entity from a customer." Taxes listed in the following table are the primary taxes that are collected by the airlines; they are added directly to the price of the ticket charged to the customer and listed separately on the ticket contract. Airline taxes are either imposed at the time of sale or at the time of departure of the flight. As a ticket is the principal contract airlines use for revenue producing activities, FinREC believes these taxes meet the definition in FASB ASC 606 as they are imposed on and concurrent with revenue-producing activities, irrespective of whether they are imposed on sale or at departure.

7. The following table presents the major taxes in the United States that FinREC believes meet the definition in FASB ASC 606-10-32-2A. In addition, most foreign taxes imposed by foreign governments on airline passengers and collected in a similar fashion by the airline as an agent would generally meet the definition in FASB ASC 606-10-32-2A. The airline should perform an evaluation of the facts and circumstances of those foreign taxes to determine if they would also be eligible for the policy election.

[2] Source: Issue Summary No. 1 prepared on February 28, 2006 in connection with EITF Issue No. 06-3, "How Sales Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross Versus Net Presentation)," which can be accessed at http://www.fasb.org/jsp/FASB/Document_C/DocumentPage&cid=1218220168047.

| TAXES AND FEES ON PASSENGERS | | |
|---|---|---|
| ***Type of Tax*** | ***Percentage or Flat*** | ***Unit of Taxation*** |
| Federal Ticket Tax (1) | Percentage of ticket price | Domestic Airfare |
| Federal Flight Segment Tax (1) | Flat Fee per passenger | Domestic Enplanement |
| Federal Security Surcharge (2) | Flat Fee per passenger | Enplanement at U.S. Airport |
| Airport Passenger Facility Charge (PFC) (3) | Flat Fee per passenger | Passenger Enplanement at Eligible U.S. Airport |
| International Departure Tax (1, 4) | Flat Fee per passenger | International Passenger Departure |
| International Arrival Tax (1, 4) | Flat Fee per passenger at Fee | International Passenger Arrival |
| Immigration and Naturalization Service (INS) User Fee (5) | Flat Fee per passenger | International Passenger Arrival |
| Customs User Fee (6) | Flat Fee per passenger | International Passenger Arrival |
| Animal and Plant Health Inspection Service (APHIS) Passenger Fee (7) | Flat Fee per passenger | International Passenger Arrival |
| Frequent Flyer Tax (8) | Percentage | Sale of Frequent Flyer Miles |

**NOTES**

1. Deposited to the Federal Airport and Airway Trust Fund, which funds the majority of the Federal Aviation Administration annual budget.
2. Funds screeners, equipment, and other costs of the Transportation Security Administration.
3. PFCs are federally authorized but levied by local airport operators, which set the amounts (up to $4.50 per enplanement, to a maximum of 2 PFCs per 1-way trip and 4 per journey).
4. Does not apply to those simply transiting through the United States between two foreign points.
5. Funds inspections conducted by the U.S. INS.
6. Funds inspections conducted by the U.S. Customs Service. Passengers arriving from Canada, Mexico, U.S. territories and possessions, and adjacent islands are exempt.
7. Funds U.S. Department of Agriculture agricultural inspections, conducted by the U.S. APHIS. Arrivals from Canada are exempt.
8. A form of federal ticket tax, deposited with the federal Airport and Airway Trust Fund, imposed on proceeds from the sale of the right to award (frequent flyer) miles to third parties (for example, credit card issuers, car rental companies, restaurants, and hotels); became effective October 1, 1997.

8. All of these taxes are authorized by the United States government via its principal agency that oversees aviation in the United States - the Federal Aviation Administration (FAA). Rules governing these taxes require the airline to collect the tax, on behalf of the FAA, for each passenger and remit it directly to the government. Of the taxes listed in the preceding table, only PFCs are collected and remitted to individual airport authorities, which are not necessarily a governmental entity (although most airports in the U.S. are currently legally established as governmental entities, this is not a required attribute). However, as the overall airport PFC tax was authorized by the U.S. government and each participating airport has to obtain authorization from the FAA both to participate in the program and to support the level of the PFC charged, it appears PFCs also meet the definition in FASB ASC 606-10-32-2A of "assessed by a governmental authority." Therefore, FinREC believes PFCs are within the scope of the policy election and can be excluded from the transaction price.

Comments should be received by September 1, 2016, and sent by electronic mail to Yelena Mishkevich at ymishkevich@aicpa.org, or you can send them by mail to Yelena Mishkevich, Accounting Standards, AICPA, 1211 Avenue of the Americas, NY 10036.