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## **Reform – maybe this time**

Somewhat lost in the clamour of the IATA AGM, and the very understandable clamour surrounding fuel price, Giovanni Bisignani made an extremely interesting call on world governments to reform and liberalise the world's aviation system. Interesting because as well as making the standard plea for action, he actually invited them to do something. Specifically, he invited them to meet in Istanbul, before the end of the year.

It is understood that a number of governments have already indicated a willingness to consider such a meeting. The more interesting question is what will be discussed. The big issues are the continuation of the bilateral exchange of 'freedoms' and the ownership and control restrictions.

What is interesting is that neither of these issues are actually in the Chicago Convention. Both concepts are defined in the International Transit Agreement, which multi-laterally exchanges what we now call first and second freedoms (overflight and technical stops) and the International Transport Agreement, which would have exchanged third and fourth freedoms mutually to all signatories. That treaty languishes on a shelf with only nine signatories. It was in fact the resurrection of the Transport Agreement that the US proposed in the recent round of negotiations on Phase II of the EU-US Open Skies bilateral.

Whilst generally thought of together, unlimited rights ('open skies') and ownership and control are not the same at all, and do not have to go together; as the Transport Agreement, and the US offer in Slovenia, showed. What IATA is calling for is not specified, but doing away with all bilateral reciprocal rights exchanges whilst a good start, may not be enough. Being able to invest and raise capital around the world must be the ultimate goal of this push for reform. It is politically difficult, but should not be abandoned for that reason alone.

Being able to invest and raise capital as needed, without restriction, would make aviation the same as most every other international industry in the world. That is why the IATA push is so important, and why we wish them luck.

## **The environment, ETS and the art of the possible – when greenhouse gases meet political reality**

When the European Council and the European Parliament cannot agree on the final terms of a proposed piece of legislation, the co-decision process calls for a 'trialogue' in which the Council and the Parliament meet with the Commission to attempt to resolve the outstanding issues. A triologue is an informal meeting of the three institutions to find common ground. The triologue is chaired by a representative of the then current Presidency of the Union (currently, but only until the end of June, Slovenia). After three meetings – naturally – of the triologue to resolve the outstanding issues (and several more of the Council's permanent representatives) on the proposal to introduce aviation into the European Emission Trading Scheme (ETS), a deal was done. For all sides, the alternative would have been very difficult – the cumbersome conciliation procedure.

So after all the screaming and shouting, a political agreement is on the table. And all sides acknowledge that it is the best that can be done. If one takes the cynical view that if no-one is happy it must be a good compromise, then this must be a good compromise. The greens call it an enormous lost opportunity, the airlines label it the End of the World as We Know It. It will increase costs, at a time when the price of oil alone means that we cannot afford to increase costs, say the airlines; it doesn't increase them enough, say the greens.

That dichotomy perhaps explains the dialogue of the deaf that has been the debate about aviation being part of the ETS in Europe. Airlines assume that people do not want to ban flying outright. Indeed, even if it were to be banned outright, it would not solve the greenhouse gas issues for Europe, or the world. Consequently, they approach the debate with the assumption that there must be a way to keep the world flying. The doctrinaire green advocates are not so sure.

The final agreement, which still needs to be approved by the Parliament in plenary to become final, (that is scheduled for 9 July) is as follows:

- The scheme will start from 2012
- It will apply to all civil flights into and from the European Union
- Except for scientific research flights
- The scheme assumes a baseline of average annual emissions based on operations between 2004-2006.
- It then takes that baseline and applies a reduction of 3% in year one, and 5% the year after
- 85% of the certificates necessary for the emissions from operations (as reduced by the calculations above) will be allocated free to airlines
- 15% of certificates will be available by auction
- The proceeds of the auctions will be directed towards
  - research on low-emission aircraft and other transport
  - climate change mitigation schemes
  - anti-deforestation projects
- There is an exemption for small operators with a threshold of up to 10,000 tonnes of CO<sub>2</sub> per annum and up to 243 flights per period of four months

Nearly as important as what is in the scheme is what was finally left on the cutting room floor. There is no NOX multiplier for example, no ring-fencing of certificates (which would have not allowed the purchase or sale of certificates to other industry sectors) and there is some earmarking of auction proceeds (although some, for example, may also be spent in developing competing transport systems). These are all good concessions, from the point of view of the airlines which had feared the worst.

Given too the savings available in Europe should the Single European Sky finally be made a reality (regularly calculated at 12% of flying – and thus emissions) it would seem that making these savings will be a flight in clear weather. Easy to say, of course, but from the point of view of the airlines, the savings from obtaining the SES are so clear, and so large, that this is where they should perhaps now be focusing their energy. That is what made this month so very important. Days before the ETS compromise was reached, the Commission unveiled Phase II of the Single European Sky. This is discussed below.

The day-to-day details of the ETS and much of the mechanics of how it will be put into place have been under discussion for some time. The final details of the monitoring, reporting and verification procedure guidelines are expected in the autumn. This is of particular concern for non-European airlines. They will need to nominate a European country with which they will liaise to both confirm their 2004-2006 baseline and to obtain their certificates (or perhaps their exemption). For details of what airlines need to do and for assistance in determining baseline emissions and other details please contact us.

All of the above is not to say that this file can now be gently filed away. Given that this is a political compromise, and that the environmental lobby is not happy, one should not assume that as far as they are concerned the game is over. Helping them in their cause are three interesting, albeit disparate, items that came to light this month. First, the European Environment Agency annual report on greenhouse gas emissions noted that whilst overall there was a small reduction in emissions (due in part to the increased cost of fuel) aviation emissions rose 'sharply' by 4.1%. Secondly, the Commission itself chipped into the debate by noting that the best solution to the rise in fuel prices is to find increasingly fuel efficient solutions. Finally, the UN Aarhus Treaty celebrated its tenth anniversary.

In case that celebration was not marked on your calendar, it might be worth going back and retrospectively putting a small black mark on the date (13 June, in case you have forgotten). One hundred NGOs, from 33 countries celebrated the date by having a two day workshop on strategies to further strengthen the Treaty and to take action in accordance with it. Be very afraid.

The Aarhus Treaty is the UN International Environmental Democracy Treaty. It gives NGOs and other civil society members standing to demand environmental information of companies they claim to have committed an environmental foul if that company does business in a signatory country. If that company refuses to provide that information, and even if the NGO would otherwise have no standing to commence litigation in that country, it can commence an action pursuant to the Aarhus Convention for the information. That is what is meant by environmental democracy. If the information is not provided, the fact that there was no actual environmental foul committed is not relevant. Failure to produce the documents is of itself a breach of an international obligation. European countries are all signatories to Aarhus. It is hard not to get the feeling that the NGOs and others are not simply biding their time on this one.

The Aarhus Treaty might not be the only chance the lawyers get to make money out of the European ETS. The United States airlines' trade association, the ATA, and others have also noted that in their opinion the ETS is a breach of international law. Picking up on the text of a State letter sent to the Commission by the governments of the US, Australia, China, Canada and others more than a year ago (and reported by us in our Aviation Intelligence Reporter of April last year [www.aviationadvocacy.aero](http://www.aviationadvocacy.aero)) the ATA notes that the ETS cannot be applied to non-European airlines. That State letter is explicit, and the ATA implicit in noting that the courts may yet get involved.

The risk of litigation will be basis for airlines not complying with their obligations. Carriers must now start to make their plans. Aviation Advocacy can help.

## **A Single European Sky – and this time the Commission means it**

Not to be outdone by their colleagues in the Environment Directorate General, the DG Transport team has perhaps done more for the environment than all of the hot air, ink and pulped paper that has gone into the debate about the ETS with their announcement on the second attempt to introduce a Single European Sky (SES) into Europe. Because they are polite they called it 'Phase 2', implying that this is building on from Phase 1, but really it should be called 'take 2'. This time, they hope to get it right.

You will recall that the first effort saw an attempt at the 'bottom up' building of functional airspace blocks (FABs) which would be organically agreed between the respective air navigation service providers, and by means of which the patchwork quilt that is the controlling of Europe's skies would coalesce into a few larger, cooperatively working together, non-national air traffic control centres. Presumably, flying pigs need to be controlled too, after all.

Hardly surprisingly to anyone that has read even a modicum of European history, that did not happen as planned. There are some commendable exceptions to that general, sweeping statement. The Scandinavians have agreed to a number of joint operations, including a joint training centre and a number of high altitude rationalisations and joint operations. And they will jointly host the AGM of CANSO in a couple of year's time, too. That may prove to be the sternest test of all. There has been real progress involving Switzerland, France and others, and Austria and its neighbours are making some progress too. But given the five years all of that has taken, it is easy to understand the Commission's frustration.

It should also be remembered that the Commission was keen to impose a 'top down' solution from the start, but were convinced that they should give each of the Member States, and their ANSPs an opportunity to find an inherent solution. Five years later, that has not happened, and thus, the Commission has stepped in.

If you accept that air traffic control is a long term, painstaking task (and the alternative is not all that attractive), then the Commission plan of Phase I, and only now Phase II, are good strategic steps. Maybe they had read their European history after all, as well as their Machiavelli. It is unlikely that progress could have been made much more quickly with a top down approach, even with full bodied Member State support and backing. In the meantime, SESAR (the cooperative plan for an interconnected technology base for air traffic management across Europe) is now past planning and into acceptance, there are clear understandings between SESAR in Europe and NextGen in the US, and only now has EASA had the time to build its staff, and find its feet. All these things needed to happen before any real progress could be made, so it might be argued that the necessary building blocks would only now in place in any event. Now, the Commission can step in with a plan of attack and no stain on its credibility.

The new SES Mark II, announced at the end of June by the brand new European Commissioner for Transport, Antonio Tajani from Italy is in fact a package of measures. It should be noted that this is a subject of co-decision between the three arms of Europe (the Commission, the Council and the Parliament), so the opportunities for 'creative

assistance' to steer the package through the process cannot be discounted. However, until that occurs, the Commission proposes a four pillar approach:

- The SES legislation will set out binding performance targets
- EASA will get extra powers to deal with ATM (and airports and environment)
- SESAR will be the basis for upgrading technology and airport capacity
- There will be clearer coordination between air and ground bottlenecks

The details are fascinating. The Commission is proposing binding targets that each Member state will enforce, requiring their national air navigation service provider (ANSP) to meet certain performance targets in the areas of safety, cost efficiency, environment, capacity and network planning. There will also be a requirement that new technology installed be in line with the SESAR requirements.

Clearly, what is missing is a single management system. Binding targets can bring together national monopoly providers, but they will still need to be held accountable against agreed target aims. Bringing these national targets together is at best a second best solution. The performance targets will also need to be published, so that user airlines can know what they can expect. The Commission says that it will do that.

A single management system is a long term solution. It is going to have to find a way to resolve two big issues. The insistence that States have sovereignty not only over their own airspace (Article 1 of the Chicago Convention makes that clear) but that in accordance with the terms of Article 28, they are also required to provide the air traffic control necessary. Even the Commission in setting out these proposals noted that the proposals are not replacing national networks. Instead, the Commission's current vision is that functional airspace blocks smooth traffic flows that proceed by means of adhering to national borders instead of using more logical and efficient air traffic control patterns. On this issue, help is at hand from a most unexpected quarter – see the next article.

The second issue is the role of Eurocontrol. The SES package has a very strong implied criticism of Eurocontrol's central flow management unit, and the fact that it is not connected to airports. Consequently, it cannot be expected to deliver gate to gate control, with all of the savings that arise from that. It does not do that because of an early airing of the time honoured sovereignty argument.

What has not been said in the SES II but is there between the lines, is that the Commission is determined to take control of air traffic control, undoing the maze of bilateral treaties that make up Eurocontrol. In our view, that is part of a long, long, term vision to create a European Aviation Agency, to mirror the Federal Aviation Agency (the FAA) in the US, and as a sister organisation to the European Maritime and Space Agencies.

Gently tucked away in this package of proposed legislation is a strengthening of EASA – giving it responsibility for air traffic management, as well as airports and the environment. Coming on top of its recent increased responsibility for pilot licensing, third party country operator licensing and certification, as well as the granting of enforcement powers (all contained in the very recent regulation 318/2008), it has been a very good half year for EASA. It should be remembered that EASA is not an international organisation, it is an executive arm of the European Commission. On a strict reading of

the Chicago Convention, it is illegal, in that each State is responsible for the discharge of these duties. But much of what EASA does is hard, and it is not glamorous, so no-one talks about sovereignty. Air traffic management is different.

## **Sovereignty – Help from an unexpected quarter**

Sovereignty is dead: long live the King. For a very long time now, ‘sovereignty’ has been the killer argument against any proposal for change in the ANSP industry. Anything that risks bringing new thinking or commercial thinking into the ANSP debate can be guaranteed a good bashing-about by those opposed to the idea. And almost always, that opposition will use the blunt instrument of sovereignty. And a very blunt instrument it is indeed.

That is why the comments made by the Director of the ICAO Legal Department at the ICAO sponsored symposium on the transition from AIS to AIM in Montreal this month were so very significant. Article 28, according to M Wibaux, is no impediment to outsourcing or delegation of air traffic control services.

You may recall that Art 28 notes that each State is responsible for the provision of air navigation services in its air space. But, ‘responsible’ does not mean there is an absolute obligation to also manage the day-to-day provision of the service. According to Wibaux, and according to a recent CANSO Legal and Policy Committee white paper ([www.canso.org](http://www.canso.org)), Art 28 needs to be read intelligently, not dogmatically. Hooray! If it was not so rare in the ATM debate such a comment might not be so earth shattering.

But it is rare, and thus earth shattering.

The CANSO paper is very good: well argued, logical and practical. In the interests of full disclosure, it should be noted that we participated in the drafting committee. But neither CANSO nor Aviation Advocacy had any input whatsoever into Wibaux’s remarks. It just so happens that we agree with them. And he would agree with the CANSO paper.

So now we know – don’t expect support from the very centre of governmental thinking if you want to use sovereignty as a reason why ANSPs cannot merge, outsource services or look outside their own walls. Or put into place the reforms the Commission has set out in SES II.

Given the growing pressure on ANSPs (and their owners) to reform and restructure – the pressures from the environment issues alone are growing daily and the ever more strident calls from the airlines for something to be done by ANSPs – this means that again the ANSPs must look at their options and start to think strategically.

## **Low Cost Airports and State Aid – the Commission looks at Hahn**

The paths for airports never seem to run smooth. On one hand, they are attacked for behaving like monopolies. Next thing you know, the Commission comes knocking on the door complaining that the airport is behaving ‘like a private market investor’. It gets even

more confusing when the airport in particular is owned by a listed company, or what might be called a private market investor in other parts of the globe. To be fair to the Commission, the basis of their complaint in this case is that airports must follow market based principles when giving assistance to airlines and there is concern that this is not the case at Hahn.

The Commission announced this month that it had decided to launch a formal investigation into public financing which Frankfurt Hahn airport has received from the Hessen and Rheinland-Pfalz regional authorities, as well as from its publicly owned parent company, Fraport AG. The Commission has also decided to scrutinize the airport charges applicable at Frankfurt Hahn. They are also going to look at the individual contracts the airport has concluded with Ryanair.

Ominously, the Commission noted that the investigation follows complaints from a competing airline and from an association of airlines. It did not specify which association, or airline.

Frankfurt Hahn airport has received and continues to receive public funding in different forms. The Commission investigation concerns mainly two capital increases, which took place in 2002 and 2004, as well as a profit-and-loss transfer agreement, between the airport and its mother company, Fraport AG.

In 1999, the airport concluded a first individual agreement with Ryanair. This initial agreement was followed by further agreements in 2002 and 2005. Subsequently, the airport has also modified its published list of charges, making available to other airlines terms and conditions similar or identical to those offered initially to Ryanair. The Commission has concluded that Flughafen Frankfurt Hahn GmbH might have acted like a private market investor, rather than following market based principles.

The Commission now needs to show this beyond reasonable doubt. Hence the call for interested parties and the German authorities the chance to present their views, before it takes a final decision on whether or not state aid has been granted to Flughafen Frankfurt Hahn GmbH and/or the airlines operating from it.

If the airport only received funds from its parent, there would be no basis for complaint. The Commission concedes that the funding by the regional authorities has helped the airport grow, and accepts that has been good for the region. Nevertheless, it is difficult to get away from the thought that with a large number of high profile State aid issues coming up, the Commission wants to be seen to be drawing a hard line on this point.

## **State Aid to Alitalia? Never – or perhaps not in 1996, anyway**

In the meantime, on July 9, the European Court of Justice will bring down a decision on State aid for Alitalia – State aid from 1996. In 1996 Alitalia adopted a restructuring plan for 1996-2000 which provided for an injection of capital to the amount of 2750 billion Lira by its majority shareholder l'Istituto per la ricostruzione industriale SpA, an Italian State body. At the time, the Commission's examination of the aid found it to be compatible with the common market, provided that (quite strict) ten conditions were met.

Alitalia challenged that decision before the CFI. The Court annulled the Commission's decision finding that it had failed to state reasons and had made certain errors in its assessment. The Commission subsequently adopted a new decision to rectify these mistakes, again declaring the aid to be compatible but attaching a number of conditions to it. Alitalia have challenged that new decision.

Given the current stakes for Alitalia, more may turn on this decision than might otherwise be the case. We may also see the Commission itself playing the role of grim reaper, demanding the repayment of funds that breaks the camel's back.

In his confirmation hearing for the Transport Commissioner post, Antonio Trajani was pressed repeatedly on how he would react if Alitalia's fate were to fall into his hands. He assured the Parliament that he would not be swayed by nationality issues. It is, however, ironic that the two people with more fundamental decision making power over the fate of Alitalia than most are both Italian. The second person of course being Giovanni Bisignani, of IATA, who one day might be called upon to remove Alitalia from the clearing house – meaning that Alitalia will be unable to rely on interline revenue.

It remains to be seen when Alitalia has its Swissair moment, but on current reports, it cannot be far away.

## **A tale of two trade associations**

IATA has been dispatching emissaries to various aviation industry trade associations' meetings this month, putting the case that airlines are hurting and looking for support from their suppliers to address the issues. Jeff Poole was dispatched to the CANSO AGM, Patricio Sepulveda to the Latin American meeting of the ACI.

CANSO released a declaration at the conclusion of the AGM offering support and urging members to do what they could to defer expenditure and review charges. ACI-LAM was less accommodating. It released a statement noting the issues that IATA had raised, but suggesting that they had businesses to run, and airlines were but one of their customers. So there.