

## **Regulatory Affairs Newsletter October 2007**

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## The regulation of international air transport – vale Chicago?

This week, the vice-chairman of Emirates Airlines said what a lot of people have been thinking – that it was time there was a considered review of the regulation of international air transport. It is one of the most deeply held and incorrect notions in aviation that the road to aviation regulation starts and stops with the Chicago Convention, and ICAO; but now, from a number of quarters comes calls for a review of what is necessary for the industry in the 21st century. Those calls are arguably a decade later than they should have been, but they are now loud and clear.

Reality has mugged the view that ICAO was the font of all aviation regulation. Competition law, regional trading blocks, the WTO, environmental regulations and even labour law have meant that ICAO has no claim to covering the gamut of regulations. ICAO gave up on commercial matters from the very start, of course, delegating to IATA (in the role of Sancho Panza) much of the commercial regulation of air transport (including famously tariffs and sandwich thickness). IATA was able to move with the times much more adroitly than ICAO and it now, on behalf of its members, is well aware of the array of sources governing aviation.

ICAO has been less adroit. In part it is a victim of its history: a permanently sitting governing Council, triennial Assemblies and a requirement for consensual, multi-lingual procedures make it difficult for ICAO to act in a timely manner. At the recent ICAO triennial Assembly, Canada and seventeen other countries tabled a very cautious proposal to look at a review of ICAO and its processes which was slapped down.

To give ICAO credit, ICAO has since September moved pretty fast on the process of setting up a group on international aviation and climate change. Whether this group will be able to produce results in the time frame that the environmental regulators and NGOs want (the next major meeting in Bali is late this year) remains to be seen.

In the meantime, we are seeing the EU and the US take over much of the regulation of commercial aviation: witness security requirements and the environment. Each of these governments are acting without regard of the multilateral framework put in place in 1944, and are unlikely to do so again, unless it is to their perceived benefit.

And, to add salt to the wound, the fastest growing aviation sector (the Low Cost Carriers) is wholly independent from IATA's regulatory gravitational pull. As the LCCs expand into long haul, it will be increasingly apparent that there will be a new world order.

Ironically, the very week after the ICAO Assembly finished, the WTO held a meeting in Geneva to consider the regulation of air transport. In the WTO's favour, some of the current huge issues that ICAO seems incapable of resolving – environment, security and overflight disputes for example, might well be better resolved and more quickly resolved, in the WTO framework (or in the case of overflights, would be, if only Russia were a member of the WTO). The WTO has a limited remit in aviation even now. Maintenance, CRS and ground handling are items included in the WTO services annex. That means that for nations signatory to the WTO there can be no 'nationality' exception or restriction imposed to stop cross border trade. No dispute has ever been brought to the WTO for resolution, either meaning that no service supplier feels that there are restrictions on its doing business, or that the prospect of taking a claim through the WTO process is too daunting.

That is not the case for Airbus and Boeing, who are at each other's throats over a state aid dispute (state aid being 'genetically hard-wired' into the entire aviation industry's DNA according to a senior Airbus official this week) that huge as it is, is nowhere near setting records for length of proceeding or complexity in the WTO roll-call of fame (step forward the banana dispute of the

nineties – a dispute that in one of the 14,000 pages of decision and deliberation comes forward with the tellingly deep observation that ‘only a banana is like a banana’).

Speaking at the WTO seminar on the regulation of aviation, a number of air transport delegates praised the fact that within the ICAO structure regional blocks were developing. It is not clear that the regional blocks are actually within the ICAO structure, or despite the ICAO structure, but in any event, WTO research shows that in fact, only one in six international passengers actually flies on an international sector that is actually liberalised, although to be fair, this excludes passengers which from next year fly between the EU and the US. At that point the number will certainly increase. The WTO is also not equipped to handle the complex technical work that IACO addresses, and it is certainly true that such work needs to go on in a multi-lateral framework.

But it might be time to look at the development of technical standards and procedures in a different light to the on-going regulation of what must now be considered to be a mature industry. Perhaps a good starting point might be to ask: if there wasn't an ICAO, would we invent one, and if so, would it look like this?

## **Emission trading – soon the hot air expended will need its own off-set program**

And still the debating and lobbying goes on in Brussels. The most important developments this month include the Working Group of the European Council (the third arm of the European Union governance – representing the Member States) rejected a Portuguese Presidency of the EU proposal for a triologue that would have effectively put onto the fast track any decisions on inclusion of aviation in Europe's Emissions Trading System (ETS).

This is a major set back for the rapporteur Dr Peter Liese, the German Christian Democrat with the legislative lead on the issue. It has also set the stage for further Parliamentary confrontation with the Council. In technical terms, the working group of the Council voted against providing a mandate to the Portuguese Presidency of the EU to negotiate a First Reading agreement with the European Parliament. The Commission proposes legislation, the European Parliament has the authority to amend it, and the Council of Ministers of the Member States reaches agreement with the Parliament and then approves it. A triologue would have short circuited that process.

Instead, the decision of the Council means that we are back to the standard full co-decision process in the Parliament with both a First and Second Reading on the report and amendments. At the end of that process there will be a process of conciliation between the Parliament and the Council. This is a formal system like the U.S. House and Senate meeting to reconcile different versions of bills. If Conciliation fails, then there is no agreement at all and no inclusion for aviation. This is not at all likely.

The current deadline for new amendments in the European Parliament is 7 November. Formal plenary vote in the European Parliament on the Liese Report and amendments is set for the November 13 plenary in Strasbourg as originally scheduled.

In the meantime, Dr Liese, lead rapporteur from the Environment Committee, and Georg Jarzembowski, rapporteur in the Transport Committee have met over the last two weeks to try to negotiate compromises on different positions held by the two European Parliament committees that have had carriage of the debate to date. There are a number of those differences to reconcile. This includes whether or not to include business aviation in the ETS. The Transport Committee draft excludes aircraft up to 20 tonnes, the Environment Committee draft includes all aircraft above 5.7 tonnes. For business aviation operators that makes a considerable difference.

Liese and Jarzembowski (both members of the EPP (and both German Christian Democrats)

have reached a common EPP position on many issues. This is likely to see the deletion of the 20 tonne threshold. On the other hand, the EPP appears likely to table an amendment which would exempt business aviation from the EU ETS provided business aviation operators join a voluntary carbon offset scheme covering all their carbon emissions. Another party, the ALDE (Liberals) is expected to support this amendment which has a fair chance of being voted in plenary in Strasbourg on 13 November.

The Presidency also will try to achieve internal agreement in the Council for the December 20 Ministerial Meeting. This is seen as “very ambitious” by a majority of Member States. The outcome for meeting that date is uncertain. The overall timetable now may be a Second Reading late in the first quarter 2008 or sometime in the second quarter of 2008. If so, final passage can be expected late in 2008 or even in 2009.

The Council appears to be hesitant to move forward with the current drafts on four issues: Member States would prefer a starting date 2012 or 2013 for both EU and intercontinental flights; a disagreement over a cap setting, with many smaller states concerned over limits that may be too strict; there was also some concern at the currently proposed level of ETS certificates that carriers could obtain by auction. Several Member States do not want anything higher than 10% available by way of auction. The UK is the leading proponent of a higher level. Generally, new Member States want a higher allowance for growth, as their aviation industry started from a very low base; finally, there was concern over the allocation of revenues derived from the ETS scheme. On this point the UK leads opposition to earmarking revenues solely for environmental purposes.

In short, substantial differences remain. The European Parliament Environment Committee had previously voted for cap setting of 75%, from a baseline of the years 2004-2006, a start date for all carriers of 2010, both EU and non EU, auctioning of 50% of allowances and a multiplier effect for NOx emissions unless checks on NOx are forthcoming too.

In other words, there are still a number of debates to be had on this issue. It is a good thing that the heat and hot air generated of themselves are not a threat to the climate.

## **AIS to AIM – Commercialising ATC Data**

Be careful what you ask for, as the saying goes. The airlines have been hammering away at the air navigation service providers (ANSPs) for several years, asking them to take a more commercial view of life. So they are, and the law of unintended consequences comes knocking. A number of ANSPs are looking at the possibility of commercialising the provision of data. That data has been provided for many years free of charge to chart makers and to others involved in flight planning, weather planning and so forth. Those chart makers then provide their service to the airlines and others. If they have to pay for the raw data they use, there is inevitably going to be an increase in the cost to the airlines that use the services.

Two things have moved together to make this possible. First, as mentioned above, there is a move to commercialise services provided by ANSPs. This is part of a process known as ‘unbundling’ whereby those services that can be provided by ANSPs without concern of any breach of sovereignty can be provided (see our September newsletter LINK for more details on this issue).

Secondly, the technology has moved on. The data is increasingly now in a digital form, allowing it to be processed and transferred more readily. ICAO has been working towards the arrival of the digital age for information – it has even worked out a new acronym. What used to be called AIS

(Aeronautical Information Systems) will now be called AIM (Aeronautical Information Management).

There are a number of good arguments as to why this information should be delivered free: first, and perhaps most compellingly, because under the terms of Annex 15 of the Chicago Convention, it is information that is vital for efficient and safe air transport, and thus there is an obligation to provide it free of charge, (with the possible exception of a strictly cost recovery fee, uniformly applied and not inimical to free access and competition). Secondly, for there to be safe air transport, there can only be one set of 'official' information, which once made available to all, on a non-discriminatory basis can then be open to competitive forces, as vendors provide value adding products based on that information.

Annex 15 defines how a State's AIS will receive and/or originate, collate or assemble, edit, format, publish/store and distribute specified aeronautical information/data. The goal is to satisfy the need for uniformity and consistency in the provision of aeronautical information/data that is required for the operational use by international civil aviation. Annex 15 has its origins in Article 37 of the Chicago Convention. The operator of any type of aircraft, be it small private aircraft or large transport aircraft, must have available a variety of information concerning the air navigation facilities and services that may be expected to be used.

Against this argument based on the Chicago Convention is one based on another body of international treaties: copyright. ANSPs for example are of the view that they create the information, they are entitled to capitalise on the money that can be made from it. They might make money from the information in two ways; first, by selling the data to the value adding companies (which are clearly profiting from this data). Data, which, they argue, they created in the first place, and thus are entitled to sell; and secondly, can an ANSP join in the value adding services market by selling such services in competition with the other existing suppliers?

The first half of this issue is harder than the second. Copyright is a statutory monopoly, created to allow the makers of original material to gain from their work. On the other hand, if the governments of the world want to ensure that safety data is available, it is possible for governments to over-ride such copyright rights. It is indeed arguable that Annex 15 does that now. The second part of the equation comes down to competition law. The answer is yes, of course they can, but only if they do so that is not likely to prevent, hinder or lessen competition. That is a structuring issue and for that, the ANSPs need advice.

## **OECD Agreement on limiting export credits for aircraft – what it could mean for the industry**

Tucked away in a news item in the middle of the summer holiday season, the OECD announced that Brazil had joined with OECD club members, including Australia, Canada, Japan, the United States and the EU, to agree to limit the export credit support available for aircraft. This will have an intriguing paradoxical effect on the industry following the coming into force of the 2001 Cape Town Convention on International Interests in Mobile Equipment and the Aviation Protocol 18 months ago and the gradual adoption of this Treaty by many countries.

The paradox is that one of the first successes of the Treaty was to persuade Ex-Im Bank to lower its risk premium in relation to loans into countries which had adopted the Treaty. This OECD pact could now actually limit the scope of export credit agencies to provide favourable finance conditions otherwise promised due to the implementation of the Treaty. On the other hand, this move amplifies the overall benefits of the Treaty in creating a secure structure for private sector lenders when they are financing aircraft and to replace the financing role traditionally played by Ex-Im, Hermes and others.

Of course, the losers are those in countries that have not yet ratified the Treaty. In particular, the failure of the EU to resolve its Gibraltar problem, thereby blocking the ratification of the Treaty across Europe, means that European industry will gradually be placed at more of a disadvantage with public sector financial support being carefully restricted and private sector financing at a competitive disadvantage to air financiers in countries which have adopted the Treaty. This taking of hostages in Europe on the Treaty is truly an own goal; if the goal is for operators to own aircraft without dedicated finance, no problem; if finance is needed, the OECD Agreement will disproportionately damage the European side of the industry.

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