

Mid-term evaluation of Regulation
785/2004 on insurance
requirements of air carriers and
aircraft operators

Final Report

Report

July 2012

Prepared for:
European Commission
DG Move,
DM 28,
B1049 Brussels

Prepared by:
Steer Davies Gleave
28-32 Upper Ground
London SE1 9PD

+44 (0)20 7910 5000
www.steerdaviesgleave.com

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Executive Summary

Background

1. Regulation 785/2004 (hereafter ‘the Regulation’) defines insurance requirements for air carriers operating in the EU. Article 3(h) of Regulation 1008/2008 defines that, for EU air carriers, compliance with these requirements is a condition for obtaining an operating license. The objective of the Regulation is to establish minimum insurance requirements for air carriers and aircraft operators in respect of passengers, baggage, cargo and third parties. Insurance for mail is regulated by Article 11 of Regulation 1008/2008 and in the national laws of the Member States. This Regulation was introduced in the aftermath of 9/11, partly to address the reduced insurance supply for the risks of war and terrorism.
2. The Regulation applies to all air carriers and to all aircraft operators flying within, into, out of, or over the territory of a Member State, with certain exceptions, principally for State aircraft, model aircraft and other small aircraft. The Regulation thus establishes a level playing field for all European and third-country aircraft operators in respect of insurance to cover of liabilities for passengers, baggage, cargo and third parties.
3. In the framework of the fitness check on the internal aviation market¹, the European Commission wishes to evaluate whether the Regulation is still fit for purpose. In order to do this, this study analyses whether the Regulation achieves its objective, namely the definition of common minimum insurance requirements which contribute to the effective operation of the internal market for aviation, by ensuring appropriate protection for users and third parties, and minimising distortion of competition.
4. The study assesses whether there are gaps, inconsistencies, overlaps, excessive administrative burden, and whether any measures have become obsolete over time. It also updates information previously published by the Commission in 2008 in its Communication on insurance requirements for aircraft operators in the EU - a Report on the operation of Regulation 785/2004². The study has been informed by interviews with industry stakeholders, including national authorities, air carrier representatives, and the insurance industry, as well as by desk research.

Factual conclusions

5. Regulation 785/2004 has largely achieved the objective of harmonising insurance requirements within the EU, by establishing minimum requirements for all operators, regardless of nationality. The definition of relatively high minimum thresholds for coverage has contributed to the objective of consumer protection and may also have contributed to the development of safer air travel.
6. The large majority of industry stakeholders interviewed for the study supported Regulation 785/2004 and thought it addressed the issues it was meant to address.

¹ Roadmap Fitness check - internal aviation market

² COM(2008)216 final

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However, some issues were raised; we describe these issues, and recommendations for how they could be addressed, further below.

7. No stakeholders suggested that minimum requirements for insurance should be removed, and in any case, this would result in:
 - A conflict with the Montreal Convention which requires all signatory States to establish minimum requirements of liability insurance.
 - A risk that some airlines operating into the EU might not have appropriate liability coverage in place and therefore a risk that potential EU and non-EU victims of accidents would not receive adequate compensation.
 - EU Member States having to establish their own minimum liability insurance requirements, which would distort the single market for air transport and increase the administrative workload for insurers and operators. Although commercial airlines might already exceed any national requirements, this could create barriers to cross-border movement of light aircraft.
8. Most stakeholders considered that the definition of harmonised insurance requirements in the European Union is proportionate to the issue under consideration and that this has a useful impact. Therefore, we conclude that there is still a need to retain these requirements at EU level.

Key issues and recommendations

9. Most stakeholders consider that the Regulation is working well and there is no urgent need to change it. However, some (mostly relatively minor) issues have been identified in the course of our research, and there could be some benefits from addressing these. In accordance with the Commission's normal practice, an impact assessment would be required before any such changes could be made.

Third-party liability

10. Although the Regulation harmonises requirements on insurance for liability to third parties, the level and nature of this liability varies between Member States. Various attempts have been made through ICAO to agree a harmonised framework for third party liability, comparable to the framework for liability with respect to passengers, baggage and cargo defined in the Montreal Convention, but these have not been successful. Therefore, we discussed with stakeholders whether this should be harmonised.
11. We have not identified any significant benefits from harmonisation of rules on third party liability. The level of fragmentation is not considered by either Member States or the industry to pose a problem and, although strictly not relevant to this evaluation, we have been advised it is likely to be very difficult to get Member States to agree a common position.
12. The Regulation defines requirements for insurance to cover third party liability on the basis of bands for aircraft weight. We recommend that the Commission should consider the creation of additional weight bands, mostly to reflect increased use of very light unmanned aircraft. At the time the Regulation was drafted, the possibility of unmanned aircraft being used for civil purposes was not considered, and the current lowest weight band (which covers all aircraft of less than 500kg)

may be considered to create a disproportionate and unnecessary burden for very light unmanned aircraft. However, any addition of lower bands to accommodate very light UAs would need to be carefully weighted against the risk of damage caused by unmanned aircraft in the case of accidents. The addition of lower weight bands would not necessarily mean a reduction in insurance requirements at any level; although no issues with this were raised by stakeholders, the minimum insurance for small aircraft already appears quite low given the damage these could potentially cause (for example if an aircraft crashed into a group of people).

13. Additionally, there is a particularly steep change between two of the weight band categories (bands 5 and 6). This rationale for this differential is not clear. This could be softened by the addition of a middle band to make levels of third party cover required more proportionate. Again, this does not necessarily mean that there should be a reduction in the minimum level of coverage at any level - it could either be achieved by increasing the coverage required for aircraft at the upper end of band 5, or reducing the coverage required for aircraft at the lower end of band 6.
14. Any changes to the weight bands should take into account the potential damage that aircraft of different sizes could cause to third parties in the event of an accident.

Certificate of insurance

15. At present, some Member States require air carriers to obtain insurance certificates in specific formats, which creates an unnecessary additional administrative burden for both carriers and the industry. We recommend that a standard-format insurance certificate should be defined; if an air carrier or an aircraft operator were to provide a CAA with such a certificate a different format could not be requested.
16. Although the standard certificate could be implemented by the Commission providing guidance, there is then a risk that some regulatory authorities would not use it (and would not have to). Therefore we recommend that acceptance of a standard certificate should be a binding requirement. However, if a certificate was to be defined, this should not be within the main text of the Regulation, as flexibility would be needed to revise this quickly to adapt to market circumstances. This could be achieved through the Regulation delegating power to the Commission, using the mechanism in Article 290 TFEU, to define the certificate.
17. Insurance certificates are usually issued by the broker but some national authorities will not accept this from their own national carriers. We see no reason why certificates from insurance brokers are not allowed at domestic level whereas they are for international carriers. Therefore we would recommend that the Commission clarifies that certificates from brokers can be used for both international and national carriers.

Exchange rate fluctuations

18. The Regulation defines minimum insurance requirements in Special Drawing Rights (SDR). However, insurance can only be contracted in hard currencies, and in practice is almost always contracted in US dollars. Therefore, there is a risk that

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where operators contract the minimum specified insurance, they end up being under-insured due to exchange rate fluctuations.

19. However, the administrative burden that this generates for regulatory authorities and the insurance industry is not excessive (limited to occasional checks that insurance is still sufficient), and we believe there is not much that can be done on this issue. Therefore we recommend not changing the Regulation on this matter.

Mail

20. Regulation 1008/2008 requires carriers to have insurance covering mail but the current Regulation 785/2004 does not specify what amount of insurance is required. We discussed with stakeholders whether there was a need to harmonise insurance for mail, but we have not identified any need or benefits from doing so. The legislative framework is in place and well known by the stakeholders, so there is a risk that the disruption created by an amendment to Regulations 785/2004 and 1008/2008 would be greater than any benefits of harmonisation.

Unmanned aircraft

21. In the short-term, as explained above, we recommend that the Commission should consider the definition of one or two lower weight bands for third-party liability, to avoid creating a disproportionate and unnecessary burden for very light (usually unmanned) aircraft. We would also recommend clarifying the definition of model aircraft in Article 2, to make clear whether unmanned aircraft of less than 20kg are within the scope of the Regulation. This could be based on the distinction between recreational and commercial use.
22. In the longer term, the Commission should consider a specific legislative instrument on unmanned aircraft, and this could include consideration of whether the standard approach to third party liability insurance in the Regulation is appropriate for these aircraft.

Heritage aircraft

23. The requirements for third party liability insurance defined in the Regulation may impose a relatively significant cost on operators of heritage aircraft. It is important that third parties are protected from potential damage from these aircraft and therefore they cannot be excluded altogether from the scope of the Regulation. However, due to the nature of their operations, the minimum requirements may be excessive in specific circumstances, for example if the aircraft would only ever operate at well below their maximum takeoff mass.
24. Therefore we recommend that the Commission should consider granting Member States the flexibility to reduce third party insurance requirements for these aircraft on a case-by-case basis where this is appropriate in the specific operational circumstances and other measures are taken by the State to ensure third parties are adequately protected.
25. An impact assessment would be necessary before any such proposal could be implemented, and as discussed in more detail within section 4 of the report, there are some risks and issues with this proposal which would need to be considered. Another option which could be considered by operators and national authorities is

re-certification to operate at reduced MTOW, to correctly reflect the size and kinetic energy of the aircraft.

Other aviation provider third-party liability

26. We have discussed with stakeholders whether there is a need for harmonised minimum insurance requirements for other aviation service providers. With respect to ANSPs, we do not believe this is necessary, as most ANSPs are State entities and therefore are in effect insured by the State. On the matter of airport insurance levels we do not believe there is an issue at EU level and recommend no further action. The issue of insurance for ground handlers has been addressed by the Commission's recent proposal for a new Regulation on ground handling.
27. The most significant potential issue relates to insurance requirements for security service providers, who may find it difficult to obtain insurance against third party liability arising from terrorism. We would recommend that there is more research done at EU level on the impact of a lack of harmonisation on third-party liability in the case of terrorism.

Other issues

28. If the Regulation was revised, we would also suggest:
- There are certain terms within the Regulation which national authorities have found to be unclear, for example relating to joint operations such as codeshares; these could be clarified.
 - It should be clarified whether deductibles are permitted. We recommend they should be, as they are normal insurance industry practice, but this should be subject to safeguards to protect passengers and third parties in the event an accident led to the insolvency of the carrier concerned.
 - A provision could be inserted to ensure that prescribed limits in Regulation 785/2004 are automatically increased in line with the Montreal Convention rather than later on through a new Regulation.

1 Introduction

Background

- 1.1 Civil aviation makes a significant contribution to the European economy: research on behalf of the aviation industry indicates that it employs 1.9 million people in Europe, and contributes around €230 billion directly to EU GDP³. The civil aviation sector has grown rapidly since the 1990s, partly as a result of the liberalisation of the sector, which has resulted in a wider choice of air services and lower fares.
- 1.2 The internal aviation market gives every EU air carrier the freedom to perform services anywhere within the EU (to carry out flights within an EU Member State and between Member States). It also gives them complete freedom to set prices, subject only to provisions on transparency and non-discrimination. The role of regulatory authorities is limited to defining and enforcing minimum standards with respect to safety, security, competition and consumer protection. Member States are also permitted, subject to a number of conditions, to define public service obligations to allow certain routes/areas to be served which are not economically viable, but have to be served for reasons of territorial cohesion.
- 1.3 Regulation 785/2004 (hereafter ‘the Regulation’) defines insurance requirements for air carriers operating in the EU, and Article 3(h) of Regulation 1008/2008 defines that, for EU air carriers, compliance with these requirements is a condition for obtaining an operating license. The objective of the Regulation is to establish minimum insurance requirements for air carriers and aircraft operators in respect of passengers, baggage, cargo and third parties. Insurance for mail is regulated by Article 11 of Regulation 1008/2008 and in the national laws of the Member States.
- 1.4 The Regulation implements Article 50 of the Montreal Convention for the Unification of Certain Rules for International Carriage by Air from 1999. The EU and all its Member States are party to this Convention.
- 1.5 The Regulation applies to all air carriers and to all aircraft operators flying within, into, out of, or over the territory of a Member State, with certain exceptions, principally for State aircraft, model aircraft and other small aircraft. The Regulation thus establishes a level playing field for all European and third-country aircraft operators in respect of insurance to cover liabilities for passengers, baggage, cargo and third parties.
- 1.6 In April 2008 the Commission published a Communication on insurance requirements for aircraft operators in the EU - a Report on the operation of Regulation 785/2004⁴.

The need for this study

- 1.7 In the framework of the fitness check on the internal aviation market⁵, DG MOVE wishes to evaluate whether the Regulation is still fit for purpose. In order to do

³ Air Transport Action Group, March 2012

⁴ COM(2008)216 final

this, this study analyses whether the Regulation achieves its objective, namely the definition of common minimum insurance requirements which contribute to the effective operation of the internal market for aviation, by ensuring appropriate protection for users and third parties, and minimising distortion of competition. The study assesses whether there are gaps, inconsistencies, overlaps, excessive administrative burden, and whether any measures have become obsolete over time.

- 1.8 This study also updates the information collected by the Commission for the 2008 Report on the operation of the Regulation.

This report

- 1.9 This report is the Final Report for the study. It sets out the work undertaken over the course of the study, and draws conclusions on the current functioning of the legislation.

- 1.10 This report does not contain information which was provided in confidence, and therefore this report can be published without the need to redact information.

Structure of this document

- 1.11 The rest of this report is structured as follows:

- Chapter 2 summarises the methodology used for the study;
- Chapter 3 explains the legislative background and shows the legal review of the Regulation;
- Chapter 4 presents the recent development of the aviation insurance market;
- Chapter 5 reports on issues that have arisen with the operation of the Regulation; and
- Chapter 6 summarises our conclusions and recommendations.

- 1.12 We also provide one appendix:

- Appendix A: examples of insurance certificates;

⁵ Roadmap Fitness check - internal aviation market

2 Methodology

Introduction

2.1 This section provides a summary of the research methodology. The research phase was comprised of two main parts:

- **Desk-based research;** and
- **Stakeholder consultation** to evaluate the enforcement and effectiveness of the legislation.

2.2 These tasks are described in turn below.

Desk-based research

2.3 We have carried out a desk research to collect relevant information. This was started immediately after the kick-off meeting. The desk research identified data sources, as well as issues raised in previous studies and their associated recommendations.

2.4 The desk research was conducted with the following objectives:

- To identify any possible data sources;
- To review the key issues highlighted by other studies as well as common themes in the insurance legislation in order to be able to identify gaps and areas with a lack of clarity; and
- To understand the earlier views and opinions of the stakeholders.

2.5 The data we collected for the study, its sources and current status is provided in Table 2.1.

TABLE 2.1 DATA SOURCES

Source	Data description
Montreal Convention	Convention for the Unification of Certain Rules for International Carriage by Air
Regulation 785/2004	Legislative text
Regulation 285/2010	Legislative text
Regulation 2407/92	Legislative text
Regulation 1008/2008	Legislative text
2008 European Commission Report	Insurance Requirements for Aircraft Operators in the EU - A report on the Operation of Regulation 785/2004
Consultative document	Summary of the contributions received by the Commission following the open consultation on the operation of Regulation 785/2004 on insurance requirements for air carriers and aircraft operators

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Airline annual reports	Cost allocated to liability insurance
Aon Market outlook 2011	Size of the market, recent trends, cost of premiums, consensus opinion on likely future developments
Willis Insight Nov 2011	Insurance market overview and trends
Marsh Insight Nov 2011	Insurance market overview and trends
Airline Business Jan 2012	Insurance market overview and trends
Aviation Insurance Clauses Group (AICG) Minutes and publications	Proposed changes to insurance clauses, recent developments in the industry
CoESS	White Paper
BH AviNews	May 2009 newsletter
Australian Government	Review of Carriers' Liability and Insurance
US DoT CFR Part 205	Legislative text
US DoT Form OST-6410	Insurance certificate for US carriers
UAS Yearbook 2011	ICAO Unmanned Aircraft Systems, Circular 328

Stakeholder consultation

2.6 In order to gain an understanding of any issues that had arisen with the Regulation, in agreement with the Commission we defined a programme of stakeholder consultation, involving the following organisations:

- National enforcement authorities;
- Air carriers and their representative associations;
- Aircraft operators and their representative associations;
- Insurers and representative bodies;
- Insurance brokers and representative bodies; and
- Other organisations.

2.7 The subsequent section explains the choice of stakeholders within each category, and is followed by a summary of the process adopted in engaging with each organisation.

Stakeholder selection process

2.8 For each of the States surveyed we approached the civil aviation authorities or equivalent. Six of the eight States were selected as the largest aviation markets in Europe (the United Kingdom, Germany, Spain, France, Italy and the Netherlands), together with two central European states (Poland and Romania) to improve the geographical spread of the sample.

2.9 We approached a number of individual aircraft carriers and operators, selected to cover a mix of different business models and geographic locations. We also

approached the main insurers and insurance brokers specialising in the aviation sector, and all of the key EU-wide industry representative organisations.

2.10 We also received a number of unsolicited responses from organisations which had taken an interest in the study. These comprised:

- Historic aircraft operators in the UK: Sally B, Vulcan to the Sky, and Plane Sailings Air Display Ltd; and
- The International Air Pilot Association.

Approach

2.11 We conducted face-to-face interview with the national enforcement authority of the United Kingdom. We also held face-to-face meetings with:

- LIIBA (London & International Insurance Brokers' Association);
- Insurance brokers from United Insurance Brokers, AON, Willis and JLT Specialty Limited;
- LMA (Lloyd's Market Association);
- IUA (International Underwriting Association); and
- IUAL (International Union of Aerospace Insurers).

2.12 The remaining stakeholders contributed in writing and/or by telephone. Telephone interviews were conducted with chairs and presidents of the smaller aircraft operators association. This approach was important to ensure that the correct stakeholders were contacted and that they were given the opportunity to contribute despite the lack of organisational resources and, often, time to complete the questionnaire.

2.13 The approach adopted in making initial contact with the stakeholders was as follows:

- Contact the organisation to invite them to participate in the study;
- Send a question list to the organisation; and
- Either arrange a face-to-face meeting or agree a timescale for their written response, indicating that this may be followed by a subsequent telephone interview to clarify any outstanding issues.

2.14 Question lists were developed for each of the five types of stakeholder identified at the start of this section. These were designed to both assess compliance with key aspects of the legislation, and to investigate the issues highlighted by the Commission in the Terms of Reference.

2.15 A full list of all stakeholders involved in the study, and the status of each contact is given in Table 2.2. Many of the individual airlines that were approached stated that they did not wish to respond; this reflects the fact that (as discussed further below) many do not see there being any significant issues or problems with this Regulation.

TABLE 2.2 STAKEHOLDERS TO BE APPROACHED

Stakeholder Group	Specific organisation(s)	Status
Air carriers and representative bodies	Association of European Airlines	Forwarded the questionnaire to their members. Responses received from two members.
	European Regions Airlines Association	Forwarded the questionnaire to their members. Responses received from one member.
	IATA	Responses received
	IACA	Responses received
	European Low Fares Airline Association	Forwarded the questionnaire to their members. No responses received.
	Lufthansa	Responses received
	EasyJet	Declined to participate
	Thomas Cook	Responses received
	Virgin Atlantic	Declined to participate
	Ryanair	Declined to participate
	Norwegian	Declined to participate
	Air Baltic	Declined to participate
Aircraft operators and representative bodies	British Air Display Association	Responses received from their members
	Europe Air Sports	Declined to participate
	Finnish Aeronautical Association - Suomi Ilmailuliitto	Declined to participate
	General Aviation Alliance	Responses received as Light Aircraft Association
	Historic Aircraft Association	Responses received
	Light Aircraft Association of the Czech Republic	Responses received
	Nationale Federatie Historische Luchtvaart	Declined to participate
	Light Aircraft Association	Responses received
	Réseau du Sport de l'Air	No response received, assume declined to participate
	Royal Belgian Aero Club	Responses received

	Union des Fédérations Gestionnaires des Assurances ⁶	No response received, assume declined to participate
	International Council of Aircraft Owners and Pilot Association	Responses received
Insurers and representative bodies	ANIA - Associazione Nazionale fra le Imprese Assicuratrici	Responses received
	CEA - European Insurance and Reinsurance Federation	Responses received
	Fédération Française des Sociétés d'Assurances (FFSA)	Responses received
	Gesamtverband der Deutschen Versicherungswirtschaft - German Insurance Association (GDV)	Responses received
	International Underwriting Association of London (IUA)	Responses received, face-to-face interview held
	Global Aerospace Underwriting Managers	Declined to participate
	Mapfre Empresas	Declined to participate
	Mitsui Sumitomo Insurance Underwriting at Lloyd's	Responses received as part of Lloyd's
	QBE Nordic Aviation Insurance	Declined to participate
	International Union of Aerospace Insurers (IUAI)	Responses received, face-to-face interview held
	Lloyds Market Association	Responses received, face-to-face interview held
	London and International Insurance Brokers' Association (LIIBA)	Responses received, face-to-face interview held
Insurance brokers	Marsh Ltd., Aviation & Aerospace Practice	Responses received
	Willis	Responses received as part of the LIIBA response
	Haywards	Responses received
National enforcement authorities	France: Direction Générale de l'Aviation Civile	Responses received
	Germany: Bundesministerium der Justiz	Responses received

⁶ In spite of their name, this organisation is a grouping of air sport federations (microlights, paragliding, etc)

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	Ireland: Commission for Aviation Regulation	Declined to participate
	Italy: Ente Nazionale per l'Aviazione Civile (ENAC)	Responses received
	Latvia: Ministry of Transport; Aviation Department	Responses received
	Netherlands: Ministerie van Verkeer en Waterstaat	Responses received
	Poland: Civil Aviation Office	Responses received
	Romania: Civil Aeronautic Authority	Responses received
	Spain: Ministerio de Fomento; Dirección General de Aviación Civil	Responses received
	United Kingdom: Department for Transport; Civil Aviation Division	Responses received and face-to-face interview
UAV stakeholders	Global Aerospace	Responses received and telephone interview
	UVS International	Telephone interview
Other stakeholders	Airports Council International Europe (ACI)	Responses received
	Schiphol Group	Declined to participate
	Polish Airports State Enterprise	Declined to participate
	Confederation of European Security Services (CoESS)	Responses received (joint CoESS-ASSA response)
	Aviation Security Services Association	Responses received (joint CoESS-ASSA response)
	Irish Aviation Authority	Declined to participate

Stakeholders not participating

- 2.16 Three of the airline associations, the Association of European Airlines (AEA), European Regions Airlines Association (ERAA) and the European Low Fares Airline Association (ELFAA), preferred to forward the question list to their members rather than to reply directly. Three responses were received from their members.
- 2.17 There have been some changes to the organisation of the associations of small aircraft operators, and in addition, the same individuals tend to be members of multiple associations. In the UK, this resulted in the General Aviation Alliance (GAA) and the Light Aircraft Association (LAA) providing joint answers. The British

Air Display Association (BADA) forwarded the questionnaire to individual members, three of whom submitted a response.

- 2.18 Other stakeholders, such as Ryanair, Easyjet, QBE and the Irish Aviation Authority, decided not to participate in the study after having examined the questionnaire.

Stakeholders which have not yet provided a written submission

- 2.19 At the time of writing, we have not received any responses from the Finnish Aeronautical Association and Polish Airports State Enterprise despite soliciting answers from them on several occasions. We therefore take it that these stakeholders did not wish to participate.

Stakeholder engagement

- 2.20 All stakeholders who participated in the study or were invited to participate but declined to were provided with a copy of the Draft Final Report and the opportunity to comment on the study findings. All comments received were provided to the Commission. Comments that clarified or corrected the text were incorporated, and other comments were considered on their individual merit. This report presents the views of Steer Davies Gleave, not necessarily those of the stakeholders.

3 Legislative background and legal review

Introduction

- 3.1 This section provides an overview of the requirements of the Regulation, and how this falls within the international legislative framework on insurance and liability. It also provides a review of national legislation on liability towards third parties, and a comparison with legislation on liability and insurance in other countries.
- 3.2 In this context it is important to understand the difference between insurance requirements and liability. If an incident happens and the airline is found liable, then it must indemnify the parties concerned. Depending on the circumstances, liability may either be capped or unlimited, and either strict or fault-based. Regulation 785/2004 sets minimum levels of insurance that airlines and aircraft operators must carry, but does not impact their liability. If the airline is liable for less than the minimum amount it is insured for, then its insurance covers the liabilities. If the liability is greater than the minimum amounts of insurance purchased, then the airline would have to pay the difference out of its reserves or assets. Where liability is unlimited, this difference could be substantial.

Aviation insurance and aviation liability

- 3.3 Regulation 785/2004 on insurance requirements for air carriers and aircraft operators came into effect on 30 April 2005. This Regulation was introduced in the aftermath of 9/11, partly to address the reduced insurance supply for the risks of war and terrorism. It followed from several related Regulations or Conventions that had already established the notion of minimum insurance requirements:

- **Regulation 2407/92 (subsequently replaced by Regulation 1008/2008)** required that air carriers contract insurance to cover their liability with respect to passengers, baggage, cargo and third parties in the event of an air disaster. However, it did not indicate minimum insurance requirements or the terms and conditions of insurance. The basic EU position is now enshrined in Article 4(h) of Regulation 1008/2008, which requires compliance with the requirements of Regulation 785/2004.
- **Article 50 of the Montreal Convention (1999)** requires signatory States to ensure that air carriers contract adequate insurance to cover their liability.
- The European Civil Aviation Conference (ECAC) adopted **resolution ECAC/25-1 on 13 December 2000** (amended on 27 November 2002), pertaining to minimum insurance requirements for passenger and third party liability.

Scope of the Regulation (Article 2)

- 3.4 The Regulation applies to all air carriers and to all aircraft operators flying within, into, out of, or over the territory of a Member State to which the Treaty applies. Article 2(2) defines exemptions for State aircraft, captive balloons, parachutes and

kites, foot-launched flying machines and model aircraft with a MTOM⁷ of less than 20kg.

3.5 In addition, Article 2(2)(g) defines that aircraft (including gliders) with a MTOM of less than 500kg, and microlights, are exempt from the war and terrorism insurance obligations if they are:

- used for non-commercial purposes; or
- used for local flight instruction which does not entail the crossing of international borders.

Principles of the Regulation (Article 4)

3.6 The Regulation defines insurance requirements for air carriers and aircraft operators in respect of their liabilities for passengers, baggage, cargo and third parties. In this context third party means any legal or natural person, excluding passengers and on-duty members of flight and cabin crew. The insured risks must include at least acts of war, terrorism, hijacking, acts of sabotage, unlawful seizure of aircraft and civil commotion. All flights must be covered, whether the flight is operated through code-share, franchise, any form of lease, etc.

3.7 The Regulation applies without prejudice to the rules on liability arising from other Conventions and laws. This means that the Regulation does not change the existing rules on liability as arising from the Montreal Conventions or any other relevant laws.

Minimum coverage requirements (Articles 6 and 7)

3.8 For air carriers and operators of aircraft within its scope, the Regulation sets minimum insurance requirements that vary depending on the type of liability:

- For liability in respect of passengers, the minimum insurance cover is 250,000 SDRs⁸ per passenger. However, for non-commercial operations by aircraft with a MTOM of 2,700 kg or less, Member States may allow a lower minimum insurance cover of at least 100,000 SDRs per passenger.
- For liability in respect of baggage, the minimum insurance cover is 1,000 SDRs per passenger.
- For liability in respect of cargo, the minimum insurance cover is 17 SDRs per kilogram in commercial operations.
- For overflights (without a take-off or landing in the EU) by non-EU carriers or operators using aircraft registered outside the EU, the minimum insurance requirements for passengers, baggage and cargo shall not apply. These flights are only required to comply with the requirements for insurance against liability to third parties.
- In respect of liability for third parties, the minimum insurance cover per accident varies depending on the maximum takeoff mass (MTOM) of the aircraft, from 0.75 million SDRs for aircraft with an MTOM of less than 500kg, to 700 million SDRs for aircraft with an MTOM of 500,000kg or more. The minimum applies per accident for each and every aircraft.

⁷ MTOM = Maximum Take-Off Mass corresponds to the certified amount specific to all aircraft types.

⁸ SDR = Special Drawing Right as defined by the International Monetary Fund. 1 euro = 0.82854 SDR (03/07/2012).

- 3.9 Insurance requirements for aircraft with an MTOM of less than 2,700kg are shown below.

TABLE 3.1 ARTICLE 6 REQUIREMENTS FOR MTOM < 2,700 KG

Member States who responded	Minimum insurance coverage per passenger
France	100,000 SDR
Germany	100,000 SDR
Italy	250,000 SDR
Netherlands	100,000 SDR
Poland	100,000 SDR
Romania	100,000 SDR
Spain	250,000 SDR
UK	100,000 SDR

Source: SDG analysis.

Insurance certificates (Article 5)

- 3.10 Air carriers and, when required, aircraft operators, must demonstrate compliance with the insurance requirements set out in the Regulation by providing the competent authorities of the Member State concerned with a deposit of an insurance certificate or other evidence of valid insurance. Member States that are overflowed may require that the aforementioned air carriers and aircraft operators produce evidence of valid insurance.

Enforcement and sanctions (Article 8)

- 3.11 Article 8 of the Regulation stipulates that sanctions for infringement shall be “effective, proportional and dissuasive”.
- 3.12 With regard to Community air carriers, these sanctions may include the withdrawal of the operating license - and compliance with insurance requirements is defined as a condition of an operating license under Article 4(h) of Regulation 1008/2008. For non-European Union carriers and aircraft operators using aircraft registered outside the European Union, the sanctions may include refusal of the right to land on the territory of a Member State.
- 3.13 In the event a Member State is not satisfied that the conditions of the Regulation are met, it has the power under Article 8(7) to prevent an aircraft from taking off until the air carrier or aircraft operator concerned has produced evidence of adequate insurance cover. Article 8(5) defines that Member States can proceed to withdraw the operating licenses of Community air carriers, subject to the relevant provisions of Community law, and Article 8(6) defines that carriers from third countries can be refused the right to land.

Failure of the insurance market (Articles 5(5) and 9(2))

- 3.14 In exceptional cases of insurance-market failure, the Commission may determine the appropriate measures to ensure that air carriers and aircraft operators are in compliance with the insurance requirements set forth under the Regulation. The Regulation does not specify what these measures could be, but they could take the form of assistance from governments, the formation of mutual funds, etc.

The carriage of mail

- 3.15 Regulation 785/2004 does not specify insurance requirements for mail. Recital 11 simply states that “insurance for mail liability is sufficiently regulated by Article 7 of Regulation 2407/92”.
- 3.16 Regulation 2407/92 has now been replaced by Regulation 1008/2008. Article 11 requires insurance with respect to mail, but does not set any limits or minimum levels, only stating that “notwithstanding Regulation (EC) No 785/2004, an air carrier shall be insured to cover liability in case of accidents with respect to mail”.
- 3.17 Therefore, with regard to insurance for the carriage of mail, Member States set the minimum insurance requirements in value for the carriage of mail by air carriers or aircraft operators; provided there is no discrimination on grounds of nationality or identity, there are no further requirements.

Aviation liability and the Montreal Convention

- 3.18 All Member States, and the European Community, have ratified the Montréal Convention. However, the minimum insurance requirements that are fixed in Regulation 785/2004 are in some respects higher than the liability levels specified in the Convention.
- 3.19 The Montreal Convention has a two tier system of liability for the death of, or bodily injury to, an aircraft passenger:
- Up to 113,100 SDR, there is strict liability, which can be reduced or excluded only in the case of contributory negligence of the passenger or person claiming the compensation.
 - For claims in excess of 113,100 SDR, liability is fault-based. However, the plaintiff is not required to prove fault: the carrier is liable unless it proves that either the damage was not due to negligence or any other wrongful act or omission, or the damage was solely due to the negligence or the wrongful act or omission of a third party. There is no limit to carriers’ liability.
- 3.20 Under the Montreal Convention, airlines are liable for up to 1,131 SDR per passenger for damage to cabin and checked baggage. This limit can be increased if the passenger makes a ‘special declaration’ at check-in regarding the value of the baggage - although the airline could consequently refuse to carry the baggage or charge a higher fee to carry the baggage. The caps do not apply if it is shown the damage was caused by the carrier's intent or recklessness.
- 3.21 In relation to checked baggage, passengers are not required to prove that the carrier was at fault in causing the damage. However, carriers will not be liable for damage to goods caused by any “inherent defect, quality or vice” of the baggage. For cabin baggage, carriers are only liable for damage if it is shown that the

damage was due to the fault of the carrier or its agents. Additionally, passengers have to prove the amount of damage sustained (i.e. passengers are required to prove that the bag was worth 1,131 SDR if claiming for 1,131 SDR).

- 3.22 The Montreal Convention does not define liability for mail or in respect of third parties.
- 3.23 The Montreal Convention does not automatically apply to domestic flights, but States may opt to apply this international regime to their domestic operations, and Regulation 889/2002 extends it to all flights by EU carriers including domestic flights. In comparison, Regulation 785/2004 applies to all flights within and out of the EU, and to all EU carriers and air operators.
- 3.24 The table below provides a summarized comparison of the requirements of both texts. It shows that there are no significant differences in the liability levels for cargo and mail. However, for passengers, Regulation 785/2004 has significantly higher requirements which are nonetheless below the average indemnity in case of airline accidents in Europe.

TABLE 3.2 COMPARISON OF MONTRÉAL CONVENTION AND REGULATION 785/2004

	Montréal Convention	Regulation 785/2004
Passenger	113,100 SDR strict liability No maximum limitation of liability	Minimum insurance requirement: 250,000 SDR No maximum limitation of liability
Baggage	Limits the liability in relation to baggage to 1,131 SDRs per passenger	Minimum insurance requirement of 1,131 SDRs per passenger
Cargo	Limits the liability in relation to cargo to 19 SDRs per kg	Minimum insurance requirement of 19 SDRs per kg
Third-party	Third-party is not covered	Minimum insurance cover per accident, for each aircraft vary from 0.75 million SDRs when MTOM < 500 kg, to 700 million SDRs when MTOM >= 500,000 kg
Mail	Mail is not covered	Mail is not covered

Note that the liability amounts specified in the table above include the reviews of limits of liability conducted by ICAO in December 2009 and following by the EU in April 2010 (Regulation 285/2010). The passenger insurance requirement in Regulation 785/2004 have not been increased, but are in any case set at a level significantly exceeding the revised limits of liability under the Montreal Convention.

Third-party liability

Liability provisions in international law

- 3.25 Since the Warsaw Conference in 1929, several attempts have been made to introduce regimes defining the liability of an aircraft owner or operator to third parties who suffer damage on the surface, but with limited success.
- 3.26 The 1933 Rome Convention Relating to Damage Caused by Aircraft to Third Parties on the Surface (from which flowed the Brussels Insurance Protocol 1938) never came into force and was superseded by a new convention in 1952, amended by a

protocol in 1978. The 1952 Rome Convention is in force and contains (in Article 15) a provision permitting a contracting state to require an operator to procure insurance against the limits of liability determined by the weight of an aircraft.

- 3.27 However, the Rome Convention is not well supported with only 49 parties (out of 190 countries) having ratified it. Although several EU Member States have signed the Convention, many of these (including UK, France and Netherlands) have not ratified it, and Germany has not signed it at all. Only 12 parties have ratified the 1978 protocol and these do not include any EU Member States or any of the other largest aviation markets, such the United States, China or Japan.
- 3.28 The Montreal Convention 1999 was the first international instrument with recognised general support (currently, 103 countries) to provide for compulsory insurance against the liability of an air carrier for damage sustained by passengers, baggage or cargo. However, the requirement was only to maintain “adequate insurance” with respect to liability under the Convention, and the Convention does not deal with an operator’s liability to third parties.
- 3.29 In the aftermath of 11 September 2001 and the activation by war risks insurers of the clause providing seven days notice before cancellation of the policies, ICAO undertook an initiative to reconsider the Rome Convention. The working groups understandably gave much attention to the introduction of a regime to deal with terrorism, ultimately producing two separate Conventions, known as the General Risks Convention and the Unlawful Interference Convention. The latter included a scheme to develop a permanent fund managed for the purpose of compensating loss caused by terrorist activity. However, these Conventions were opened for signature in 2009 and have not yet come into force on account of lack of sufficient support - and it seems unlikely that they ever will. No EU Member States, or any of the other countries with the largest aviation markets, have signed either Convention.

Liability provisions in national law of Member States

- 3.30 Liability can be strict or based on fault of the operator. Under strict liability, no negligence of the operator needs to be proven, whereas with fault-based liability, an operator will only be found liable if some form of negligence is established. Liability can be limited with a cap on the potential level of compensation, or unlimited, in which case there is no theoretical cap on the amount of damages for which defendants are potentially liable (although compensation will in practice be limited to the value of an airlines’ insurance policy combined with its total liquidated assets).
- 3.31 The table below provides an overview of the different third-party liability regimes that exist in the Member States for aviation matters. There are some important differences between the regimes of the Member States surveyed and we would expect the same to be the case for the remaining EU Member States.

TABLE 3.3 THIRD-PARTY LIABILITY REGIME IN SELECTED EU MEMBER STATES

Member States	Strict or fault based	Applicable limits	As defined in
France	Strict	Unlimited	Civil Code
Germany	Strict	Limited except where the carrier is negligent	-
Italy	Strict	Limited except where the carrier is negligent	Italian Navigation Code, Article 971
Netherlands	No detail provided	No detail provided	Civil Code
Poland	Both	Unclear (see note below)	-
Romania	Strict	Limited except where the carrier is negligent	Civil Code
Spain	Strict	Unclear	-
UK	Strict	Unlimited	Section 76(2) of the Civil Aviation Act 1982

Source: SDG analysis

Note: In the case of Poland, the CAA indicated that it is difficult to summarize the Polish third party liability regime in a one-word expression as the system is unique, complex and every case is individually investigated (among others it can be fault-based or risk-based liability). Similarly, whether the liability is limited or unlimited cannot be determined in general terms.

- 3.32 The comparison of third-party regimes shows that EU Member States apply different rules which are not necessarily comparable to the rules that apply regarding liability vis-à-vis passengers. We understand that there is also no consistent framework in the rest of the world.
- 3.33 Other than the 1952 Rome Convention (discussed above) and the ICAO Convention on Compensation for Damage Caused by Aircraft to Third Parties, signed at Montreal in 2009 (and not yet in force), we are not aware of other international rules regarding air carriers' liability to third parties applied in other world regions.
- 3.34 However, the desk research and stakeholder interviews undertaken for this study have not identified any problems arising from the lack of a commonly-defined regime on third party liability. The civil aviation authorities interviewed for the study considered that the different regimes were a 'non-issue', and did not recommend harmonisation. This view was also shared by the insurers and brokers, as well as the airlines and aircraft operators. Some national authorities also noted that due to the different positions that had been taken in discussions on this issue by different Member States, it was likely to be very difficult to achieve agreement on a common regime.
- Legal review**
- 3.35 Our legal advisors, Clyde & Co, have undertaken an independent legal review of the Regulation and issues with it. This section provides this review.

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- 3.36 Overall, our legal advisors consider that the regime set down in the Regulation appears effective and sufficient, and no amendment is currently necessary. However, they have raised some issues, set out below.
- 3.37 Article 1 excludes the carriage of mail from the insurance requirements set out in the Regulation. Recital 11 states that this is because the position is adequately dealt with by virtue of existing rules applicable to the relationship between the carrier and postal administrations per Article 2 of the Montreal Convention and, within the Community under Article 7 of Regulation 2407/92, providing that “*An air carrier shall be insured to cover liability in case of accidents, in particular in respect of passengers, luggage, cargo, mail and third parties*”. However, Article 11 of Regulation 1008/2008 (which replaces Regulation 2407/92) states that “*Notwithstanding Regulation (EC) No 785/2004, an air carrier shall be insured to cover liability in case of accidents with respect to mail*”. To ensure that this insurance obligation includes the minimum requirements of the Regulation, an express extension of the Regulation to cover the carriage of mail could be considered.
- 3.38 The Regulation distinguishes between “air carriers” and “aircraft operators” which separates those operators with a valid operating licence from those persons or entities without. To a large extent, the Regulation applies equally to both. The exception is found in Article 5(1) where the requirement to demonstrate compliance with the insurance obligations to “the Member State concerned” is mandatory for those with a valid operating licence and subject to Member State discretion for those operators without. Such different treatment could be incorporated within Article 5 itself, with an all-embracing single definition to cover both carriers and operators, which would simplify the drafting of the Regulation. (In this review ‘operators’ means both ‘air carriers’ and ‘aircraft operators’.)
- 3.39 The operation of Unmanned Aerial Vehicles (UAVs) was minimal, if not non-existent, at the time of adoption of the Regulation, and they were thus probably not considered. However, their use has grown significantly in recent years and they pose a very real risk of surface damage. While it is not entirely clear, the current scope provisions in Article 2 probably mean that many if not most UAVs are not within scope, because they fall within either Art 2(2)(b) or (g). Consideration could therefore be given to making the application of the Regulation to UAVs clearer.
- 3.40 Insofar as the Regulation is concerned to ensure that there is cover for war and related risks, the types of risk stated in Article 4(1) are relatively limited when compared with the cover available from the insurance market. The stated risks are war, terrorism, hijacking, acts of sabotage, unlawful seizure of aircraft and civil commotion. It is not clear why certain other risks covered under model form policies are not also risks that require insurance cover. If, for example, a policy covered only ‘war’, it would likely cover war of every type so that civil war would be included. However, that does not mean that it would be given such a wide definition so that the term would also include hostile attempts to overthrow a ruling body, which then might be covered by the term ‘hostilities’ and/or ‘attempts at usurpation of power’ cover is not. A formal extension to the scope of war and

related risk would mean that any scheme designed to help provide required cover in the face a failure of the insurance market would also improve the prospect of operators continuing to comply with the insurance provisions in any finance/leasing contracts.

- 3.41 The current form commonly used by the market is AVN52E, which operates as write back (i.e. reinstatement) to a model form of exclusion clause - AVN48B. AVN52E provides for the insurer and insured to agree which elements of the exclusion will be reinstated. The provision relating to war cover, for example, also deals with “*invasion, acts of foreign enemies, hostilities (whether war be declared or not), civil war, rebellion, revolution, insurrection, martial law, military or usurped power or attempts at usurpation of power*”. It may be that the Regulation - construed differently from an insurance contract - would be interpreted to include this extra cover but there is no explicit requirement for an operator to obtain it and no real reason it should be expressly required, from a consumer/third party protection perspective.
- 3.42 Article 5(5) deals with measures to respond to “insurance market failure”. This contemplates the activation of cancellation provisions, as occurred in the immediate aftermath of the 11 September 2001 incident. The Regulation does not provide for any procedure nor any time frame for measures to be adopted. In that context it is to be noted that those aircraft operating under leases will typically contain contractual requirements for such insurance to be obtained as is set down in the Regulation. The absence of sufficient cover will therefore effectively ground aircraft.
- 3.43 The operation of the Regulation is predicated upon sufficient capacity in the insurance market. In the event that the insurance market did not provide cover sufficient to meet the requirements of the Regulation, it is assumed that those affected by the Regulation would look to their governments as a fall-back position. Since the Regulation seeks to foster consumer protection, it is noted that an equilibrium would need to be sought to ensure that the primary risks were protected without excessive cost for that cover. Any such cost would likely be passed on to consumers. While it would be difficult to prescribe within the Regulation what solution might be adopted to the possible withdrawal of sufficient insurance market capacity, this debate already has some history stemming from various government-backed schemes considered post 11 September 2001, such as the scheme known as Globaltime.
- 3.44 The cancellation and review provisions contained within war risk policies are well established and are well understood by policyholders. These operate prior to the expiry of a policy and effectively withdraw cover from an insured. There is a range of views within the insurance market as to what level or kind of loss might precipitate a mass withdrawal of capital or a fundamental reassessment of the perceived risks involved. From comments by leading insurers (who do not wish to be quoted), it is thought, at the time of writing, that a US\$1 billion loss would not trigger either the cancellation or review (i.e. terms and/or pricing) provisions or otherwise significantly alter an insurer’s perception of the risk environment. Therefore, currently the risk of cancellation or review of these policies is considered low.

- 3.45 The limits set out in Article 6 were amended by EC Regulation 285/2010 to increase the liability in respect of baggage to 1,131 SDRs per passenger (Article 6(2)) and in respect of cargo to 19 SDRs per kilogram (Article 6(3)). These increases help to ensure that minimum limits are kept in line with the ICAO review of the Montreal Convention (per Article 24), which determined that inflation has exceeded the relevant 10% threshold. Article 6(5) could potentially be amended to include a provision automatically increasing the value/limits in line with updates to the Montreal Convention and EC Regulation 2027/97.
- 3.46 The minima set out in Article 7 in respect of liability for third parties appear to be well within the insurance capacity limits available in the market. Accordingly, any threat or challenge to available insurance capacity could be considered to be minimal. These minima reflect the figures that appear in the Montreal Conventions dealing with third party liability. Should these Conventions come into force, which does not appear likely in the near future, the Regulation would be consistent.
- 3.47 The concern in the last paragraph of Article 7(1) as to aggregation of war and related risks does not appear to be significant at the moment. Most policies are written on 'per occurrence' or 'per accident' basis, without a cap on the number of occurrences/accidents that the policy will respond to. Accordingly, so long as the combined single limit (capping exposure to passenger, baggage and third party liability) per accident is sufficiently high, the insurance requirements should be met notwithstanding a sub-limit in relation war and related risks. Other than for small general aviation operators war and other perils, coverage is subject to an aggregate limit for third party liability.

The chain of liability for aviation service providers

- 3.48 Our legal advisors, Clyde & Co, have addressed the subject of the potential for airlines to recover what has been paid to passengers arising from incidents caused by third party service providers, such as ground handling agents, airport operators and air navigation service providers. This section provides this review.

The liability chain

- 3.49 The basic chain with which we are concerned is as follows:
29. Incident affecting passenger/damaging cargo;
 30. Passenger or cargo interests claim against Carrier and claim paid by Carrier and/or Insurers;
 31. Carrier and/or its insurers identify third party's breach (of contract, tort or public duty) as having caused incident; and
 32. Potential (subrogation) claim against third party.
- 3.50 For the purposes of this advice in relation to an action against a third party, parts 1 and 2 of the chain are assumed. Many, but not all, claims giving rise to carrier liability will arise under the Warsaw/Montreal system (Regulation 261/2004 provides an example of an alternative basis for a claim); the Warsaw/Montreal system enjoys wide international support. The principles of liability are effectively the same between the Conventions and so it will suffice for the purposes of background to look at the provisions in the Montreal Convention 1999 (which in any

case will generally be the relevant regime for EU air carriers). The Convention applies to the international carriage of persons, baggage or cargo performed by aircraft for reward. It applies equally to gratuitous carriage by aircraft performed by an air transport undertaking.

- 3.51 There are important limitations to the scope of a carrier's liability under the Convention, which provide potential defences in the event of a claim. Perhaps, the most well-known example is the meaning the term 'accident' as it applies to personal injury and death claims. The term is given a meaning specific to Article 17, which was defined by the United States Supreme Court in *Air France v Saks (1985)*: a passenger's injury must be 'caused by an unexpected or unusual event or happening that is external to the passenger'.

Basis for third-party liability

- 3.52 As discussed above, the law creating obligations between private individuals is split into two branches - contract and tort (or delict) - a division recognised in most jurisdictions. Liability arises where a duty owed to one person is breached by another causing damage or a loss.
- 3.53 While every claim must be considered upon its own merits, contractual relations will greatly impact the liability of third parties to carriers. One of the principal reasons for this is that the basis of most relationships with third parties will be contractual, whether or not impacted by other rules. A contract will apportion to one of the contracting parties the risk of certain events happening, either by agreement (which may be express or implied) or by operation of law. Accordingly, the terms of the relevant contract must be considered as well as the applicable law and the jurisdiction (for matters of public policy) in which the contract is considered. In addition to the law of contract, standard principles of negligence generally apply to the potential liability of the third party service providers.
- 3.54 However, product liability - based on negligence principles - deserves special mention because it is treated as a discrete area, at least by practitioners of common law, and because it is a fertile area for the liability of aircraft and/or component manufacturers. A complaint may be made regarding a defective or dangerous product where (1) it has caused injury to persons or property (other than itself) or (2) otherwise causes loss because it cannot be properly used due to a malfunction or because it may cause damage.
- 3.55 The extent of a manufacturer's exposure to such losses will depend upon whether a carrier has a contractual link to the manufacturer. However, in tort, it is necessary to prove that the product is dangerous and there is not normally recovery for pure economic loss. The implications for the failure of a product or component are very wide, and hence the financial consequences are likely to be high. This means that such cases are likely to be strongly disputed by manufacturers.
- 3.56 A breach of a duty by a third party may result in a civil and/or criminal liability towards the affected person. Civil law jurisdictions are known for including criminal liability in relation to accidents. A famous example is the Air France Concorde crash shortly after take-off from Paris CDG on 25 July 2000. After a criminal investigation, on 12 March 2008 a French public prosecutor asked judges to bring charges against Continental Airlines in relation to debris on the runway

left by the Continental flight preceding Concorde. We understand that the court found Continental criminally liable and ruled that it would have to pay 70% of any compensation claims such that Air France could recover payments it made to victims (although we do not know precise details).

- 3.57 Subrogation adds an additional dimension. In effect this means that the insurer takes over the claim from the carrier and exercises the rights the carrier would have had against the third party which is allegedly responsible for the damage. Therefore, although an action to pursue a third party in relation to liability incurred to a carrier's customer may well be a commercial decision taken by the carrier, it may simply appear that way, since it is just as likely that the carrier's insurer or reinsurer exercising claims control or subrogation rights will be the actual party seeking to pursue a recovery of claims paid.

Air Traffic Management

- 3.58 Air traffic management encompasses a broad range of activities including preventing collisions. The complexity of aircraft operations arises from the nature of air travel and the number of potential parties involved. Under Article 28 Chicago Convention⁹ a Contracting State must provide suitable air traffic management facilities. To flesh out the principles set out in the Chicago Convention, a suite of annexes was produced containing detailed sets of rules on various aspects of the administration of civil aviation. Annex 2 provides rules for air navigation and under Article 12, Member States agree as far as possible to keep their own rules of the air uniform with Annex 2.
- 3.59 In light of the fact that the structure of the governing bodies is relatively complex, identifying a decision maker represents a principle difficulty for a carrier in deciding who to pursue for a recovery of payments to passenger - for example, the closure of airspace to due the ash cloud in April 2010 where Member States, the EU Commission, Eurocontrol and national air traffic service providers were all involved. Where an accident is caused by a failure of an air traffic management system, such as an error by an air traffic controller, the persons who may be liable include the State, and/or the air traffic control organisation and/or the air traffic controller.

Airport operators

- 3.60 An airport operator is responsible for managing take-off and landing and for managing any obstruction to the landing areas (runways), aprons, stands and the approaches/air corridors. Where there is potential hazard of engine ingestion for example, airport operators may be liable if there is no appropriate system to discover and control the problem. For example, this applies to bird strikes and ice ingestion on the runway. However, it is unlikely that such systems have to eliminate the risk of ingestion at the airport entirely.
- 3.61 Some incidents take place inside or on the ground, some examples of which include lost luggage and falls within an airport or when approaching an aircraft. Where a person is moving within the airport grounds, the airport operator will be subject to premises liability.

⁹ Air navigation facilities and standard systems

Ground handling

- 3.62 Ground handling addresses the many service requirements of aircraft from arrival at a terminal gate to departure, among them baggage handling, ramp handling, refueling, oil, freight and mail services. Where an airline does not provide such services itself, they are subcontracted to a handling agent. The basis of the relationship is frequently governed by IATA's SGHA, which forms the basis of most ground handling contracts under which the carrier has very limited protection.
- 3.63 A hurdle to recovery by the carrier regarding losses incurred to passenger interests, and a common feature of all versions of the SGHA under Article 8, is the need to prove that a handling company's act causing damage was carried out with intent or recklessly with knowledge that damage, death, delay, injury or loss would probably result. These concepts are well known to English courts (and, as a historical feature of the Warsaw system, to many jurisdictions) but are difficult to prove because they incorporate a subjective test, requiring a carrier to show not only that the handler knew that the act was risky or did not care whether or not it was risky but also was aware that damage would probably result.
- 3.64 A detailed discussion on IATA's SGHA provisions is provided in Chapter 5 ("Operation of the Regulation"), between paragraphs 5.52 and 5.63.

International comparison of insurance and liability outside Europe

- 3.65 The largest EU aviation partners such as the USA, Canada, Japan, China, the UAE, Australia and New Zealand have all ratified the Montreal Convention. As of February 2012, there were over 100 countries that were Parties to the Convention, including most large aviation markets. Countries that have not signed the Convention include Algeria, Angola, Antigua, Azerbaijan, Belarus, Brunei, Burma, Chad, Djibouti, Ethiopia, Guatemala, Indonesia, Iran, Iraq, Kazakhstan, Kyrgyzstan, Laos, Lesotho, Nepal, Philippines, Russia, Sri Lanka, Thailand, Tunisia, Venezuela, Vietnam and Yemen.
- 3.66 The Montreal Convention applies to commercial international carriage of persons, baggage and cargo performed by aircraft for reward, between countries who have implemented the Convention. It does not apply to domestic travel (unless countries decide to extend it to domestic travel, as the EU has) or to journeys where the origin or destination points are countries who have not implemented the Convention. In this case, it is the 1929 Warsaw Convention together with the subsequent amending Conventions and Protocols (The Hague Protocol of 1955, the Guadalajara Convention of 1961, the 1971 Guatemala City Protocol, the 1975 Additional Protocols Nos 1,2,3 and the Montreal Protocol No 4 of 1975) that apply.
- 3.67 However, there is also a series of voluntary agreements, which were developed by the International Air Transport Association (IATA) prior to the negotiation of the Montreal Convention, called IATA Inter-carrier Agreements. These Agreements sought to redress the inadequate compensation levels offered under the Warsaw system, and were developed from the 1960s with the most recent set of agreements being negotiated by IATA in the 1990s. Airlines that are signatories of the IATA Inter-carrier Agreements waive the Warsaw caps, and waive the Warsaw defences up to a threshold of 100,000 SDR, which in practice creates a liability regime similar to the one of the Montreal Convention.

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- 3.68 It appears that the coverage of the agreements has declined in recent years, as the Montreal Convention has been gaining wide acceptance. However, some airlines implement the agreements in their Conditions of Carriage, even though they are not formal signatories to the agreements. As the coverage of the Montreal Convention expands, the agreements will decline in relevance, however, they will still be important for travel from countries which are only signatories to the Warsaw Convention.

The USA

Passenger, baggage and cargo liability

- 3.69 The USA is a signatory to the 1999 Montreal Convention and a Party to the Warsaw Convention, including The Hague Protocol and the Montreal Protocol No 4. The Montreal Convention therefore applies for passenger, baggage and cargo liability of international flights to/from the USA.

Third-party liability

- 3.70 For third party, the USA has a system of unlimited fault-based liability.

Insurance requirements

- 3.71 Insurance requirements in the USA are specified in CFR Part 205¹⁰. For domestic and international travel, the US requires minimum insurance coverage for bodily injury or death of US\$300,000 for any one passenger, and a total per involved aircraft for each occurrence of US\$300,000 multiplied by 75% the number of seats installed in the aircraft. Less stringent requirements apply to small capacity aircraft (such as air taxi operators registered under Part 298), with minimum insurance coverage of US\$75,000 per passenger and a total per involved aircraft for each occurrence of US\$75,000 times 75% the number of seats installed in the aircraft.
- 3.72 For domestic and international travel, the USA requires minimum insurance for third-party of US\$20 million for damage to property per involved aircraft for each occurrence and a minimum limit of US\$300,000 for bodily injury or death to any one person for each occurrence. Less stringent requirements apply to small aircraft with less than 60 seats or 18,000 pounds of MTOW where the third-party insurance minimum limit is set at US\$2 million per occurrence and at US\$300,000 for air taxi operators.
- 3.73 In 1966, the United States indicated its intent to denounce the Warsaw Convention because of its dissatisfaction with the Convention's limit of 125,000 French gold francs or around 8,300 SDRs on air carriers' liability to passengers. The United States withdrew its denunciation when all air carriers serving the US entered into the "Montreal Agreement" discussed above. The Agreement also provides that a carrier is strictly liable for a passenger's bodily injury or death up to the liability limit even if the carrier can prove that it was not negligent in causing the accident. The USA still requires all airlines to become signatories to the Montreal

¹⁰ Available at <http://www.air-compliance.com/Downloadable%20Files/FAA%20Information/DOT%20Applicable%20Department%20of%20Transportation%20Regulations.pdf>

Agreement to ensure that passengers are covered by the higher limits of liability provided by that Agreement.

War risk insurance

- 3.74 After 9/11, the FAA began issuing premium third party liability war risk insurance to US air carriers. The Homeland Security Act of 2002 (HSA), Public Law 112-7 and subsequent legislation mandated the expansion of war risk insurance coverage to include hull loss and passenger liability, and required continued provision of this insurance.
- 3.75 The Federal Aviation Administration (FAA) Aviation Insurance Program Office currently provides war risk hull loss, and passenger, and third party liability insurance to regular scheduled US air carriers. The Program authority is effective until 31 December 2013.

Australia¹¹

Passenger, baggage and cargo liability

- 3.76 Australia is a party to the Warsaw Convention, including the Hague protocol, the Montreal Protocol No 4, the Guadalajara Convention, and the 1999 Montreal Convention, which would apply for passenger, baggage and cargo liability of international flights to/from Australia.
- 3.77 For domestic travel within Australia, the Warsaw System, the Montreal Convention and the IATA agreements do not apply for passenger liability. Instead there is a separate system of liability, which covers carriage between States and Territories¹². It essentially adopts the Warsaw rules, subject to the following important modifications:
- Limits of liability are set at A\$500,000 (€406,000). The liability limits are unbreakable and there is no capacity for a person to receive compensation in excess of the limits by establishing intentional or reckless conduct, wilful misconduct or gross negligence etc.
 - Liability is strict and the carrier has no ‘all necessary measures’ defence.
 - While application of the Montreal Convention is limited to bodily injury, the domestic framework extends to personal injury. Personal injury can include bodily injury, sickness, disease, fright, shock or mental anguish, and psychiatric injury.
- 3.78 Australia has a strict cap on liability for cabin baggage (A\$160 or €130) and checked baggage (A\$1,600 or €1,300). For checked baggage, the carrier is considered liable unless the carrier proves that all necessary measures were taken to avoid the damage. For cabin baggage, passengers are required to prove that they were not responsible for causing the damage. Unlike the Montreal Convention, it is not possible for the passenger to claim in excess of the caps by proving that the damage was caused by the carriers’ intent or recklessness. In all circumstances, passengers have to prove the amount of damage sustained.

¹¹ Source: Review of Carriers’ Liability and Insurance, Government of Australia (2009)

¹² Established in Part IV of the Civil Aviation Carriers’ Liability Act of 1959

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- 3.79 There is currently no regulation regarding the liability of air carriers for damages to cargo on domestic transport within Australia.

Third-party liability

- 3.80 In Australia, the *Damage by Aircraft Act (DBA) 1999* imposes strict and unlimited liability. Both the owner and the operator of the aircraft are potentially liable under the Act.
- 3.81 The Act does not apply to unincorporated intra-state operations. State Government legislation, which mostly predates the DBA Act, creates similar liability frameworks which cover these operations.
- 3.82 Prior to the DBA Act, Australia was a Party to the Rome Convention (see paragraph 3.26 above). However, Australia denounced the Convention in 1999 because the caps on liability were not consistent with its expectations.

Insurance requirements

- 3.83 In Australia, mandatory insurance for carriers against liabilities for death or injury caused to passengers commenced in early 1996. Part IVA of the CACL Act imposes mandatory non-voidable insurance requirements on air carriers flying to, from or within Australia. No operator is allowed to carry passengers for hire or reward without appropriate insurance cover.
- 3.84 In the case of domestic carriage, the minimum insurance level is A\$500,000 per passenger. International carriers, including foreign carriers serving Australia, are required to provide evidence that they are insured to a level of 260,000 SDRs per passenger. Carriers must have these levels of insurance irrespective of their potential liabilities under the Warsaw System or the Montreal Convention.
- 3.85 An important feature of Australia's mandatory insurance scheme is that it makes insurance contracts 'non-voidable': part IVA of the CACL Act nullifies any clause which would relieve the insurer of its obligations to meet the carrier's liabilities. It is a standard condition in most insurance contracts that an insurer is not liable to pay compensation to a policy holder who breaches the law. However, due to the non-voidable nature of Australia's insurance scheme, insurers cannot avoid paying compensation in respect of passengers who are killed or injured because of a breach of a legal aviation safety requirement by an operator.
- 3.86 There are no provisions in the DBA Act which require carriers to obtain insurance against third-party risks.
- 3.87 It has been estimated that around 10% of all aircraft in Australia are not insured at all, for either aircraft hull risks, or liability risks. It is understood that nearly all of these aircraft are privately owned recreational aircraft, who are not covered by the mandatory passenger insurance scheme which applies to commercial operators.

War risk insurance

- 3.88 The Australian Government does not require carriers operating in Australia to have war risk insurance, but many airlines consider it a commercial imperative in order to offset potential liabilities. It is also a mandatory requirement for the carriers operating to/from the European Union (currently Qantas only).

4 The aviation insurance market

Introduction

- 4.1 This chapter provides a review of the aviation insurance market in the context of the Regulation. It examines the price of insurance for airlines and aircraft operators, and discusses the impact of terrorism and war risks on the market.

Exclusions from insurance policies

- 4.2 Airline insurance and reinsurance contracts are subject to exclusion clauses which specify risks that insurers will not cover (as per AVS104B clause). The most significant exclusions include:

- Bodily injury or death of an employee in the course of his employment;
- Damage to property owned/rented/leased/occupied by the insured;
- Illegal/criminal/dishonest acts with the knowledge and consent of the management/Directors of the insured;
- Failure to perform (in the context of the Airport Owner and Operators Liability Insurance);
- Noise and pollution hazards;
- War and allied perils (discussed below in paragraph 4.11);
- Nuclear risks (discussed below in paragraph 4.15);

- 4.3 However, brokers are in most cases able to procure insurance for their airline or air carrier client that partially ‘writes back’ a significant number of these exclusions. The extent to which the broker is able to do this will, of course, depends on the profile of the individual airline concerned (based on its safety records and culture, fleet value and age, areas of operation, etc) and the receptiveness of the leading underwriter. However, the majority of these ‘write backs’ have become standard and are usually provided by the market.

- 4.4 However, there is always the possibility that insurers will seek to deny coverage in some circumstances. This would depend on the individual circumstances of the loss in question, and other factors (for instance did senior management of the airline have prior knowledge that safety violations were routinely occurring and had done nothing to address them).

Terrorism and war risks

- 4.5 Air transportation is particularly vulnerable to terrorism. Examples include the September 11th, 2001 events, as well as in-flight explosions such as that of a Boeing 747 in December 1988 over Lockerbie (UK).
- 4.6 Insurance representatives interviewed for the study emphasised that a risk is only insurable to the extent that it can be measured and is diversified, and re-insured for a reasonable cost, so that it can be shared between the largest numbers of insurers. Therefore, the scope of cover must be limited, which explains why occurrences such as damages caused by war, terrorism, or nuclear accidents are usually either not covered (or covered but subject to cancellation at short notice

(or automatic termination). However the Regulation explicitly includes war and terrorism risks in the minimum insurance requirements.

- 4.7 On September 11, 2001 (9/11), terrorism took on a new dimension:
- The costliest disaster in the history of insurance (3,100 people died and 2,250 were injured);
 - Claims falling on airline all-risk policies during 2001 totaled almost US\$5 billion, three times the originally expected total premium for the year¹³;
 - Civil aircraft were used as weapons of mass destruction; and
 - The level of uncertainty grew as to the possible means of terrorism which could be used (ground-to-air missiles, biological and chemical materials, etc.) and this meant that insurers felt unable to assess the risks.
- 4.8 After 9/11, aviation insurers limited their liability with respect to non-flying third parties (injury to persons or property on the ground) for war risks, including acts of terrorism. Liability cover for terrorist acts in respect of third parties on the ground was limited to US\$50 million which would have resulted in many airlines being grounded as they would not have had adequate insurance.
- 4.9 The absence of a European backstop mechanism and the inadequacy of the global supply led air carriers in 2002 to ask European governments to set up Eurotime, a European mutual terrorism insurance fund. This was not actually set up - individual Member State governments provided guarantees, and the European Commission decided to put an end to all such measures in effect throughout the European Union with effect from 1 November 2002. At about the same time, the US government decided to maintain its backstop, via the FAA (Federal Aviation Administration).
- 4.10 Although insurers limited the level of coverage available for third party damage caused by war or terrorism, coverage continued to be available for loss or damage to passengers and aircraft hulls in the event of a terrorist attack.

Aviation Insurance Clauses Group (AICG)

- 4.11 Aviation insurance contracts exclude so-called war risks under the standard War, Hijacking and Other Perils Exclusion Clause (AVN48B). The AVN48B clause is broad in its scope, excluding coverage for damage caused by a wide range of military and terrorist actions, hijacking, as well as strikes, riots, labour disturbances, any “malicious act or act of sabotage” or hostile use of atomic or radioactive device. However, payment of an additional premium will allow most excluded risks to be written back under separate extension clauses (AVN52C), thereby allowing airlines to purchase cover for those risks.
- 4.12 After agreement with the European Commission in March 2005, the Aviation Committee of the Lloyd's Market Association (LMA) and the Aviation Technical Committee of the International Underwriting Association of London (IUA) set up the Aviation Insurance Clauses Group (AICG). The purpose of the AICG is to consider, and where appropriate, draft, non-binding standard wordings and clauses which command support from insurers and re-insurers, brokers and clients of

¹³ Airline Business, Feb 2012

aviation insurance underwritten in the London market and which comply with legal and regulatory requirements.

- 4.13 After 9/11, some insurers considered that the standard exclusion clause AVN48B was no longer adequate, given the potential risks threatening the airline industry, and in particular “new perils” such as hostile use of electromagnetic pulses, or chemical or biological agents. In August 2006, the Aviation Insurance Clauses Group published two proposals for new exclusion clauses: AVN48C and AVN48D.
- AVN48C included the same exclusions to AVN48B, as well as an exclusion of so-called “new perils”. It also proposed a complementary ‘write back’ clause (AVN52H).
 - AVN48D is an alternative to AVN48C and comes with a write-back clause (AVN52K). It is intended to provide limited insurance cover against some of the “new perils” under certain circumstances.
- 4.14 In practice, these new clauses are still not used, and the market still uses AVN48B. The European Commission advised that AVN48D if combined with the AVN52K write-back would be acceptable, but that use of AVN48C and AVN52H would be a breach of the Regulation. However the Regulation imposes obligations on airlines, not insurers, and more generally, it is usually not possible to compel insurers to offer coverage under particular terms. Therefore, it is possible that in the future insurers could insist on use of AVN48C, with all its negative consequences for the air transport market.
- 4.15 At present, the only universal exclusion for which no ‘write-back’ is available, when purchasing third party war and allied perils liability coverage, is nuclear risks (per AVN38B) and hostile use of nuclear devices (as defined in paragraph (b) of AVN48B). Carriers currently operate without insurance for these risks.
- 4.16 All cover under AVN52 is automatically terminated (not voided) if war breaks out between any of the 5 major powers (defined as France, People’s Republic of China, Russian Federation, UK and USA), whether or not there is a declaration of war. However, coverage remains in effect until the aircraft lands for the first time after war commences. All cover is also automatically terminated from requisition by the government of the country in which the aircraft is registered.

Force majeure

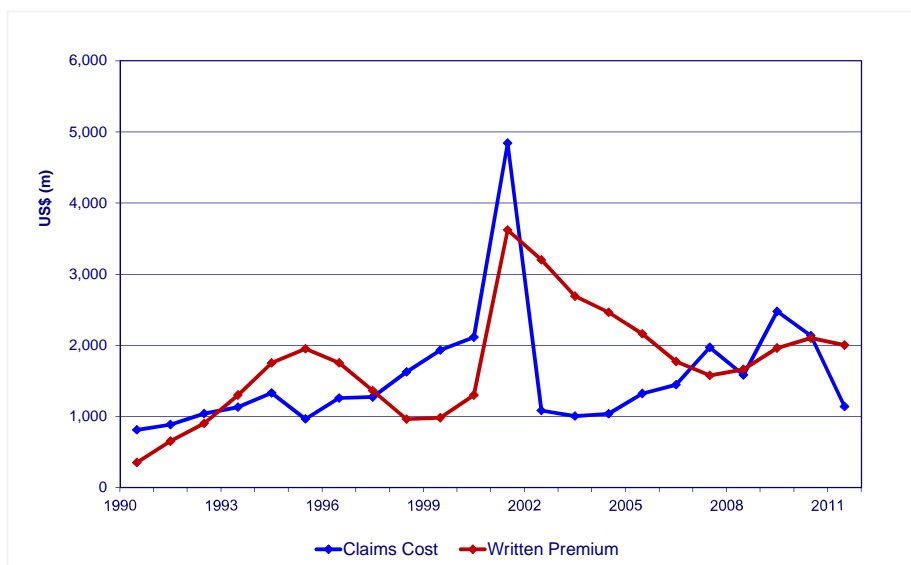
- 4.17 The term ‘force majeure’ is used in aviation policies mainly with respect to circumstances in which the aircraft is outside the geographical limits covered by the policy for reasons outside the control of the air carrier. This would happen in cases such as engine failure or other mechanical breakdown to the aircraft or as a result of hijacking or theft of the aircraft which would result in the aircraft landing in a place outside geographical limits of the policy.
- 4.18 In other respects, there is no ‘force majeure’ exclusion in aviation insurance policies. Perils that are not covered are specifically excluded, and generally aviation policies do not exclude ‘acts of God’ because aviation insurance is by definition an accident product.

Development of the aviation insurance market

Total insurance costs

4.19 The airline insurance industry operates in a very volatile environment, as illustrated in the graphic below. This is because there is a small premium base and occasional catastrophic losses. This seems to have been the norm for 20 years with a succession of cycles where premiums exceed claims (such as between 2002 and 2006) and years where claims exceed premiums (such as between 2009 and 2010). AON also states that “hull and liability premium has swung from 84% increases and 24% declines between 2000 and 2010”. Note figures in this section are reported in US dollars as this is the currency used by the aviation insurance industry.

FIGURE 4.1 AIRLINE HULL AND LIABILITY COSTS AND PREMIUM



Source: Ascend. Note that the amount of premium written in an “underwriting year” and the cost of claims incurred in a calendar year are not directly comparable. The data displayed excludes hull war and excess third party losses.

4.20 The increase in insurance claim costs in 2009 and 2010 comes from a number of catastrophic losses with expensive passenger liability loss in 2009 and an increase in hull losses in 2010 compared to previous years.

4.21 Despite price volatility and its compulsory nature, airline insurance remains a small percentage of the total operating costs of airlines. Ascend estimates that overall the world airlines paid an estimated US\$2.3 billion for basic airline insurances in 2011, which is the equivalent of about 80c (US cents) per passenger carried or US\$60 per flight.

4.22 We have also checked insurance costs incurred by major EU airlines. Unfortunately, many do not specify what insurance costs they have incurred, but Lufthansa and easyJet provide figures in their annual reports:

- **Lufthansa:** Lufthansa’s Annual Report indicates a 2010 premium of €64 million, for traffic of 91 million passengers, and slightly more than 1 million flights performed. This is equivalent to about €0.70 per passenger or €63 per flight. Although this is higher than the average worldwide insurance cost per flight,

this is due to Lufthansa's relatively long average flight length, as well as Lufthansa's fleet structure including high value long-haul aircraft; German insurance tax of 19% being included in this amount; and Lufthansa's passenger profile including a large number of premium class travellers and US passengers who represent a high liability exposure. Lufthansa also commented that they "purchase the most comprehensive coverage available in the insurance market".

- **easyJet:** Insurance costs were equivalent to about €0.21 per passenger or €29 per flight in 2010. These figures are lower than for Lufthansa, probably due to the shorter average sector length, and the fact that easyJet does not fly to/from the US.

Costs by type of insurance

- 4.23 Airlines purchase a number of insurance products in order to meet the requirements of Regulation 785/2004, as well as other insurance requirements not specifically required by the Regulation, such as hull cover. Liability and hull risk are typically covered in a single policy with the same insurers covering both¹⁴ (referred to as the "all-risk hull and legal liability to passengers and third-parties" product, which is purchased in the all-risk market).
- 4.24 The cost of all-risk hull and legal liability to passengers and third-parties is estimated to be US\$2 billion in 2011, and therefore this accounts for the large majority of total airline insurance costs.
- 4.25 The airline hull war market has remained fairly static in 2010 with forecasted premium increases of a single-digit percentage for 2011. Over the longer term, the increase in insurance premia is below the increase in fleet size and traffic: the underlying trend is therefore a decrease in premia of around 8%¹⁵ p.a. The total value of the airline hull market for 2011 (premia paid by the airlines for this product) is estimated to be of US\$100 million¹⁶.
- 4.26 The airline excess third party war and allied perils liability market is estimated to have generated premia of US\$200 million in 2011¹⁷. When the AVN52E clause first became available it generated around US\$1.5 billion. However, no losses have been incurred since its inception, and there has been an increase in interest in this market by underwriters, who see it as an attractive risk. As a result, there has been a steady decline in premiums¹⁸. AON estimates that premia for this product decreased by more than 10% in 2010 compared to 2009.
- 4.27 We understand that no claims have ever been made against the excess third party war liability.
- 4.28 Whilst the market provides coverage for war, acts of terrorism, Weapons of Mass Destruction (WMD) and other perils, the policies covering such perils also include

¹⁴ Aviation Insurance - A Plane Man's Guide. P.J. Viccars (2001)

¹⁵ AON Market outlook, 2011.

¹⁶ Ascend, "insuring the risk", Airline Business, February 2012.

¹⁷ Ascend, "insuring the risk", Airline Business, February 2012.

¹⁸ AON Market Outlook, 2011.

automatic termination in certain circumstances and short notice cancellation clauses. We understand from the insurance brokers and insurers that if there was a major incident such as 9/11, this type of coverage might again be unavailable in the commercial market place, because insurers could take the view that the risks are too high.

- 4.29 The price of insurance varies significantly from airline to airline. Insurers take into account a number of factors when establishing premiums, including the location of the airline and geographic spread of the network; airline size; track record of safety; fleet age; fleet manufacturers; fleet maintenance, etc. The price of insurance is also influenced by the level of deductible (the amount that is covered by the policy-holder before the insurer pays any expenses) taken by the airline. If an airline is prepared to accept a high deductible, such as the first US\$1 million of any claim, then the cost of insurance can fall significantly.

Other operators

- 4.30 On the basis of the stakeholder submissions, there does not seem to be significant issues with the current capacity of the insurance market for air carriers, for whom the market is competitive. However, for those operators that have more specialist needs we were informed that there can be difficulties obtaining insurance for General Aviation products (including historic aircraft). For instance in the UK the market is dominated by one insurer (Munich Re) through one broker (Hayward) which insures 70% of the General Aviation aircraft and 90% of the helicopter fleet.

Conclusion on the insurance market

- 4.31 The insurance market delivers the required insurance products to the airlines and the aircraft operators, including for hull war and excess third party war risks, at prices that appear to be reasonably related to the costs incurred. However we cannot be certain that in the case of a major terrorist incident this would still be the case. Depending on the circumstances, insurers and re-insurers may withdraw from their contracts at short notice (48 hours).

Economic impact on air carriers and aircraft operators

- 4.32 Although the Regulation harmonised rules on air carrier insurance, carriers already had significant insurance to cover these risks, and therefore it did not have a significant economic impact on them. However, it did increase the level of insurance required for heritage aircraft and also for some other aircraft operators.
- 4.33 The 2008 report on the operations of the Regulation stated that, after the Regulation entered into force in April 2005, the increased cost in insurance led to a number of heritage aircraft not being able to fly. For the heaviest historic aircraft, falling in the highest MTOM bands, aircraft insurance costs commonly increased by 500-1,000%. After fuel costs, insurance is the largest cost for these operators.
- 4.34 The Regulation defines minimum insurance requirements for third-party liability on the sole basis of the MTOM of the aircraft. However, the capacity to cause damage is determined by the kinetic energy that the aircraft possesses because of its motion, not by the MTOM. The kinetic energy of an aircraft is a function of the actual (not maximum) mass of the aircraft and its velocity (squared). MTOM is in

effect used as a proxy for the potential damage that the aircraft could cause, and whilst it is probably the best and most convenient proxy available, it is not a perfect one: in particular, it does not take into account that some aircraft may operate at lower speeds and typically at a mass well below their MTOM.

- 4.35 Historic aircraft on display flights operate at low altitudes and with low average speeds. In most cases, they do not operate near their certified masses, because:
- they usually carry a lot less fuel than their capacity, due to short flight lengths for these operations (such as local air shows);
 - they do not carry passengers, baggage or cargo; and
 - in the case of ex-military aircraft, the MTOM may be determined by the capability to carry heavy weapons, but these would no longer be carried.
- 4.36 There has been at least one example in the UK of a heritage aircraft (a PBY Catalina) that was re-certificated to a lower weight, in order to reduce insurance costs for the aircraft. The insurer was satisfied that it provided the operator with a realistic level of third party liability for the type of flights undertaken and authorised by the UK CAA that are to be taking place outside controlled airspace and away from major conurbations. The re-certification of the aircraft resulted in the premium falling by £10,000 (€12,000).
- 4.37 Another issue for the heritage aircraft market has been the lack of insurance capacity and the resulting lack of competition between brokers/insurers. This is because there are only a very limited number of underwriters interested in this line of business in Europe.

Conclusion on heritage aircraft

- 4.38 The Regulation has had a relatively significant impact on heritage aircraft operators. However, third-parties need to be protected from the risk of damage from heritage aircraft. Unlike airlines, heritage aircraft operators would not take out substantial third party insurance without a regulatory requirement to do so, and also do not have significant other assets that could be claimed against. Therefore, it is important that these operators are adequately insured.
- 4.39 In some cases it may be possible for heritage operators to decrease insurance costs through re-certification of their aircraft with a lower MTOM, although we are unclear what the costs this process may incur. We were also advised by insurance industry representatives that they take into account the lower speeds, lower mass, and limited hours of operation of these aircraft when establishing the premium. However, given the regulations imposed on historic aircraft operations by the aviation authorities of the Member States including for example the restriction to day VFR (Visual Flight Rules) operation only, or the prohibition of flight over populated areas¹⁹, in some cases it might be considered that the legal liability coverage demanded could be disproportionate.
- 4.40 As noted above it is important that third parties are adequately protected, and for this reason a general exemption from minimum insurance requirements is unlikely

¹⁹ Note this is not a recommendation of this study but given as an example of the type of alternative measures national authorities could take

to be appropriate. However, in some cases it may be possible to protect third parties partly through other measures. Therefore we recommend that the Commission should consider allowing national authorities to reduce the requirement for third-party liability insurance for specific non-commercial operations by heritage aircraft on a case-by-case basis, in limited defined circumstances that reflect their operational environment, limited utilisation, low-inertia and actual operational weights (as against their certificated weights). We have been advised that this should only concern 25-30 aircraft at EU level, mostly in Benelux, Scandinavia, Germany, France and the UK.

4.41 However, any analysis of such a proposal would have to take into account potential negative impacts. One national authority, in its comments on this study, expressed concern about allowing any potential for an exemption, for the following reasons:

- **Clarity and transparency:** The national authority was concerned that if an exemption was granted to one type of operator, others might seek it as well, and considered setting common insurance minima across the EU was a significant step forward in developing a level competitive playing field.
- **Definition:** There is no accepted definition of historic aircraft and for this reason it is not clear how many aircraft could be exempted.
- **Potential impact on third parties:** Although other measures could be taken to protect third parties, such as limiting fuel carried, the authority considered that these measures would all be hard to monitor and some could have other impacts.

5 The operation of the Regulation

Introduction

- 5.1 This section summarises our analysis of issues that have arisen with the operation of the Regulation. It updates the discussion in the Commission's 2008 Report and addresses some specific questions which were raised about the operation of the Regulation in the Terms of Reference for the study. Where possible, it suggests changes which could be made to address the issues which have been identified.

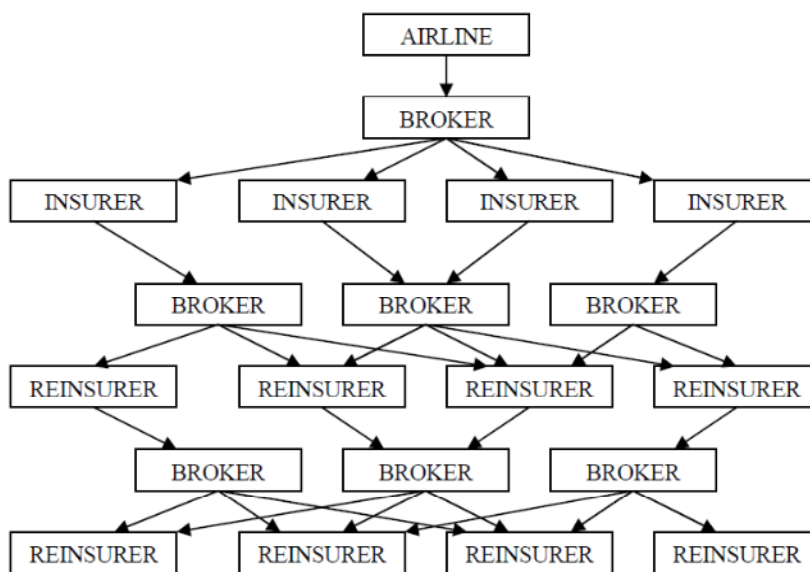
Passenger liability minimum requirement level

- 5.2 The minimum level required for passenger liability (SDR 250,000) is significantly below the actual average indemnification amount for passenger fatalities, so it may be felt that the minimum limit required by Regulation 785/2004 is not appropriate. On the other hand, we have been told by both the insurance industry and the airlines that commercial airlines operating in the EU usually purchase insurance limits significantly in excess of SDR 250,000 per passenger anyway. These stakeholders were not willing to discuss actual amounts. Consequently, we do not believe there is a significant problem here that needs addressing.

Impact of currency fluctuations

- 5.3 The Regulation defines insurance requirements in SDRs (Special Drawing Rights). SDRs are also used in the Montreal Convention to define liability levels. The SDR is the unit of account of the International Monetary Fund and the SDR value is defined by a weighted currency basket made of the US Dollar, the Euro, the British pound and the Japanese Yen. This means that there are daily fluctuations between SDR and the currency in which insurance is purchased (which we were informed is usually US\$).
- 5.4 Insurance brokers try to make sure that their clients purchase and maintain adequate insurance to comply with the minimum limits imposed by the Regulation. As noted above, most commercial airlines purchase insurance for amounts significantly higher than the minima stipulated in the Regulation and therefore would not fail to meet the minimum insurance requirements as a result of currency fluctuations. However, many small commercial operators or general aviation operators instruct brokers to purchase insurance with limits that are equivalent to or close to the stipulated limits. Consequently, when the Regulation came into force, LIIBA recommended to their broking members that, for those risks with low limits, they should recommend to their clients that they add at least a 10% margin when converting the SDR limits to the policy currency, to cater for exchange movements.
- 5.5 An enforcement authority suggested that, to resolve this issue, insurance contracts should be written in SDR rather than in national currencies. However this may prove very difficult in practice: insurance purchased by an airline from an insurer in a given currency is then broken down into parts which are sold by the insurer to the re-insurers in the same currency. The graphic below illustrates how this is done in practice:

FIGURE 5.1 THE INSURANCE “CHAIN” FOR AVIATION RISK



Source: Recent developments in the Aviation Insurance Industry paper, P. Hayes, T. Flouris and T. Walker, 2004

- 5.6 Using the SDR, which is made of four hard currencies, each with their variable exchange rate, would be very unappealing to the insurance market. At present, the US dollar is used for most aviation insurance contracts, partly because aircraft purchases and leases are contracted in dollars and therefore the amount necessary to cover hull insurance will be in dollars.
- 5.7 On the other hand, brokers suggested that the Regulation should state that, if an insurance policy provides sufficient coverage with the exchange rate at inception to meet the SDR minimum amounts, the limit should not require further adjustments until renewal or 12 months, whichever is sooner. This seems to us difficult to accommodate as, at certain times, there have been significant currency movements within 12 month periods, and therefore it could leave the air carriers and aircraft operators under-insured.
- 5.8 We have been told that this issue does not generate a significant administrative burden for regulatory authorities or the insurance industry. Therefore we believe that nothing can be done to address this minor issue and that regulatory authorities and brokers will have to keep checking that insurance policies meet the minimum limits from time to time.

Insurance certificate

- 5.9 There is already a standard-format insurance agreed by the industry and produced by the brokers or insurers (shown in Appendix A). However, brokers indicated that a number of States are requesting their own versions of insurance certificates for domestic and foreign aircraft. This adds a considerable administrative burden, as airlines must obtain insurance certificates in multiple different formats. Brokers informed us that some States also insist on very particular phraseology or special terms which increases the burden, although once the forms are “set up” on brokers’ systems, this becomes less difficult.

- 5.10 All the regulatory authorities stated that they accept insurance certificates from both insurers and brokers, but in the case of Italy at least, we understand that the certificates for national carriers must be issued by insurance companies, not brokers²⁰. However this view was disputed by an insurance broker who mentioned that they have issued certificates for Italian airlines which have been accepted by Italian authorities.
- 5.11 Another issue is that some Member States require evidence of insurance for delay to passengers. This is not a requirement of Regulation 785/2004 and is not covered by standard aviation liability insurance policies, which cover legal liability for bodily injury or property damage caused by an accident. A requirement for insurance for delay appears to be rather pointless in any case, as airlines are very rarely held liable under the Montreal Convention for damages due to delay to passengers.
- 5.12 Stakeholders interviewed for this study repeatedly raised the requirement for a specific format insurance certificate imposed by the German civil aviation authority, LBA, as being particularly onerous. In addition, Lloyds of London informed us that LBA does not share the widely accepted view that it is an insurance “operator” which regulates its own members, and has rather insisted that each managing agency within Lloyd’s (which can amount to 50 or more) to be registered with LBA. This issue affects all airlines flying to/from and over Germany.
- 5.13 Most stakeholders who contributed to this study considered that a standard insurance certificate would be beneficial. The advantage of a standard insurance certificate would be to ensure the simplification of procedures for oversight for the regulatory authorities. It would also reduce the regulatory burden for air carriers, insurance brokers and insurers. It would also allow comparisons in terms of coverage (depending of course on the operators, the operations, aircraft and insurers).
- 5.14 However, our legal advisors Clyde & Co commented on the issue of insurance certificates that “we support the idea of not prescribing a standard format. This will ensure that insurers are capable of responding to new circumstances and should prevent any model wordings from being inconsistent with policy terms”. It is clear that any certificate would need to be flexible enough to meet changing circumstances but it may still be possible to achieve this whilst defining a standard certificate (see discussion below).
- 5.15 There is a consensus among almost all stakeholders (regulatory authorities, insurers and brokers, airlines, aircraft operators) that all would benefit from definition of a standard insurance certificate. All CAAs interviewed for the study, including LBA, concurred. However, some of them thought that it was important to retain a level of flexibility and would favour this being implemented through guidance rather than as a binding requirement. The Dutch CAA mentioned that a

²⁰ As per Article 109, comma 2, lett. b) of the Italian Private Insurance Code (CAP) which states that “the insurance or reinsurance brokers act on behalf of the customer and do not have any power of representing the insurance/reinsurance Company. Therefore the insurance certification that a broker might issue could not be considered legitimate, valid and binding upon the insurer, who would not be held to cover of the risks so certified”.

compliance statement with Regulation 785/2004 on the current insurance certificates could be sufficient.

Which instrument?

- 5.16 The main problem with the Regulation itself specifying the format for the insurance certificate is that it would be difficult and time consuming to change, and therefore it would be inflexible. It would also be harder to consult with the industry about the detailed provisions if these had to be defined through the legislative process. However, this could be avoided if the detailed requirements for the insurance certificates were defined outside the main text of the Regulation, with the Regulation itself defining general principles to be followed.
- 5.17 For some other legislation in the transport sector, detailed provisions are defined in implementing rules. For example, the Single European Sky II (SESII) programme was introduced through Regulation 1070/2009 amending the initial SES Regulations, but important elements of the programme are defined in implementing rules, such as Commission Regulation 691/2010 defining the performance scheme. These Regulations are approved by the (specialist) Single Sky Committee through a comitology procedure.
- 5.18 Alternatively, as the design for the certificate is a relatively technical matter, it might be possible for the Regulation to state that the Commission should be delegated powers to define the certificate itself. Article 290 TFEU allows powers to be delegated to the Commission in specific circumstances and this mechanism may be appropriate in this case.

Administrative burden

- 5.19 As national authorities all may check the insurance certificates for each air carrier and aircraft operator operating to/from their airports, and in some cases also through their national airspace, this means that multiple authorities check the same certificate. In effect, there is no mutual recognition of the validity of the controls undertaken by other Member States. Although this is a thorough approach which minimises the risk of an inadequately-insured operation, arguably it creates an unnecessary administrative burden for both air carriers and enforcement bodies. This could be addressed if, at least for Community air carriers, national authorities agreed to accept that a carrier was adequately insured if it had a valid operating license, as the licensing authority would have been obliged to check this already.

Mail insurance requirements

- 5.20 Article 1 excludes the carriage of mail from the insurance requirements set out in the Regulation. Recital 11 states that this is because the position is adequately dealt with by virtue of existing rules applicable to the relationship between the carrier and postal administrations per Article 2 of the Montreal Convention and, within the Community under Article 7 of Regulation 2407/92, providing that "*An air carrier shall be insured to cover liability in case of accidents, in particular in respect of passengers, luggage, cargo, mail and third parties*". However, Article 11 of Regulation 1008/2008 (which replaces Regulation 2407/92) states that

"Notwithstanding Regulation (EC) No 785/2004, an air carrier shall be insured to cover liability in case of accidents with respect to mail".

- 5.21 The air carriers and insurers who contributed to this study were not aware of any problems with regards to mail insurance requirements. Coverage for carriage of mail liabilities appears to be largely available in the market.
- 5.22 Article 11 of Regulation 1008/2008 does not set any minimum levels of insurance regarding carriage of mail. Only one of the eight regulatory authorities which responded to the study thought that this should be harmonised. The French DGAC thought it would not be helpful to set specific minimum requirements in this area, since the airline's liability for mail is subject to special international conventions within the Universal Postal Union.
- 5.23 Although the omission of mail appears to be inconsistent given that the Regulation defines requirements for insurance for cargo, there is no obvious need for regulation of minimum insurance requirements for mail other than for simplicity purposes - in contrast to passengers, for which there is a clear consumer protection interest. We believe that on balance there is no need to extend the Regulation to cover the carriage of mail.

Non-commercial operations of aircraft with a MTOM of less than 2,700kg

- 5.24 The Terms of Reference for the study ask us to comment on whether the differentiation of minimum insurance cover for passengers for non-commercial operations of aircraft with a MTOM of less than 2,700kg in the EU results in impediments to the free movement of persons.
- 5.25 Since this flexibility only applies to non-commercial operations, the only way in which it could impact the free movement of persons is with respect to transport by business aviation operators. However, we have found that very few business aircraft have an MTOM of less than 2,700kg: the most commonly used types are all significantly larger than this²¹. In any case, business aviation users should be in a much stronger position than regular air passengers to negotiate the type and level of insurance that they require without regulatory intervention.
- 5.26 The desk research and the stakeholder consultation did not raise any issues with respect to insurance for non-commercial operations of light aircraft with a MTOM of less than 2,700kg caused by the adoption of the lower limit by some Member States. Therefore we conclude that it should not be necessary to harmonise the passenger insurance requirements for such light aircraft.

Evidence of valid insurance for overflights

- 5.27 We observe that most Member States exercise their option under Article 5(3) of the Regulation to not request evidence of insurance in the case of overflights, unless it is an overflight with dangerous goods. The table below summarises the situation for each Member State that took part in the stakeholder consultation.

²¹ Eurocontrol (2010): Business Aviation in Europe 2009

TABLE 5.1 EVIDENCE REQUEST FOR OVERFLIGHTS

Member State	Request evidence?	Rationale
France	No	Evidence of insurance must always be supplied when operators are required to seek overflight rights under the Chicago Convention of 7 December 1944.
Germany	No	No rationale provided
Italy	No	No rationale provided
Netherlands	No	No rationale provided
Poland	No	Only in cases of overflights with dangerous goods, when exemption or approval should be granted (as regards to commercial air operations).
Romania	No	Only in the case of non- EU air carriers which need, according with the Romanian rules, an overflight permission (i.e. aircraft carrying dangerous goods, military goods and troops).
Spain	Yes	If the origin or destination of the flight is a member state of the European Union, then no evidence is required. In all other cases it is a requirement.
UK	No	It is unenforceable in relation to private aircraft operations. The majority of the air carriers who fly over the UK also operate into it, or indeed other Member States, and have already demonstrated compliance in order to obtain their landing permits. When overflight permission for aircraft operating without an ICAO-compliant Certificate of Airworthiness is sought, evidence of insurance must be supplied.

Enforcement and sanctions

- 5.28 National enforcement authorities have stated that cases of non-compliance with the Regulation have remained extremely limited. The enforcement authorities indicated that they monitor compliance in a number of ways, including unannounced “spot checks” at airports and airfields.
- 5.29 Authorities that have had to enforce sanctions include:
- Netherlands: One Cessna 172 operator was found non-compliant.
 - Spain: Sanctions imposed in a few isolated cases. As soon as the enforcement authority was made aware of it, aircraft take-off was prohibited.
 - UK: Eight sanctions have been imposed since the Regulation came into force.
- 5.30 The table below summarises the legal framework for enforcement and sanctions in each Member State. Member States noted that, in addition to any sanction, carriers or operators found to be without insurance would be banned from

operations in their State; in the case of a Community air carrier the operating license would be withdrawn; and the case of a carrier or operator from a third country, traffic rights would be removed (as per Articles 8(5) and 8(6) of the Regulation).

TABLE 5.2 ENFORCEMENT FRAMEWORK

Member State	Offense type	Possible sanction	Text
France	Administrative	Fines up to €1,500 for a person and up to €7,500 for a business/organisation	Article R160-1 of the French Aviation Code (Code de l'Aviation Civile)
Germany	Administrative	Fines up to €50,000	German Air Traffic Act (Luftverkehrsgesetz), § 58 paragraphs. 1 No. 15 and paragraphs 2
Italy	Unclear	Fine between €50,000 and €100,000 for no insurance. Where insurance does not meet specified minima, fines between €30,000 and €60,000.	Legislative Decree 197/2007
Netherlands	Administrative	Up to €1,000,000.	Article 11.16 of the Air law (Wet Luchtvaart)
Poland	Administrative	Fine of 0.25% of the minimum insurance cover	Article 209o of the Polish Aviation Act
Romania	Administrative	Fines of 20,000-35,000 lei (€4,750-€8,300)	Governmental Decision 912/2010 (Article 13(a) and Article 14(1))
Spain	Administrative	For commercial flights fines between €4,500 and €135,000. Fines up to €60,000 otherwise	Article 33 of Law 21/2003 of 7 July
UK	Criminal	Unlimited fine, up to two years imprisonment, or both	The Civil Aviation (Insurance) Regulations 2005 and Operation of Air Services in the Community Regulations 2009

Unmanned Aircraft: a new development to be considered as part of the review of the Regulation

- 5.31 The use of unmanned aircraft for civil purposes was non-existent at the time of adoption of the Regulation, and they were thus probably not considered. However, their use is expected to increase significantly in the future. Civil applications could include meteorological services; inspections of infrastructure such as bridges, pipelines, electricity grids or runways; monitoring of large events

or traffic; wildlife monitoring; land management; and customs and police surveillance.

- 5.32 Derived from military technology, unmanned aircraft Systems (UAS) usually fall within two categories:
- Remotely Piloted Aircraft Systems (RPAS): there is a pilot in command like in any other aircraft, but the pilot is not on board the aircraft. The RPAS is a system made of an aircraft, a ground control station where the pilot is based and a data link;
 - Fully autonomous systems: where the aircraft operate independently as a system, without being piloted on-board or from the ground; Today civil applications of fully autonomous aircrafts have not happened yet;
- 5.33 Remotely piloted aircraft systems are not necessarily flown within visual distance of the pilot: they can be fitted with cameras and GPSs. Some UAs, albeit for military usage, are flown above conflict areas (such as Afghanistan) but piloted from the USA.
- 5.34 UA for civil use come in a variety of shapes, format, range and weights. Some UA used for land surveying, which carry high-tech equipment, can be as light as 2kg, whereas others under 150kg can nonetheless have a wingspan of around 8 metres. An industry expert estimates that 80-90% of the UAS under 150kg used for civil applications have a mass of less than 15kg with around 90% of these having a mass of less than 7kg. Nonetheless, UAs may have payloads and equipment that are expensive, and can potentially pose a real risk of surface damage to third parties (people and property).
- 5.35 UAs with a maximum take-off weight (MTOM) greater than 150kg are regulated and certified by the European Aviation Safety Agency (EASA), whereas those below 150kg MTOM are regulated by their national authority, such as the Civil Aviation Authority for the UK.

Are Unmanned Aircraft in scope of Regulation 785/2004?

- 5.36 Regulation 785/2004 is not explicit about UAs. Although most other EU air transport legislation, including Regulation 1008/2008, only applies to air carriers, Regulation 785/2004 also applies to aircraft operators, which are defined in Article 3(c) as any person or entity which has effective disposal of the use or operation of an aircraft. Therefore, if UAs are considered 'aircraft', then UAs are likely to be within scope.
- 5.37 ICAO defines an unmanned aircraft (UA) as a "pilotless aircraft, in the sense of Article 8 of the Convention on International Civil Aviation, which is flown without a pilot-in-command on-board and is either remotely and fully controlled from another place (ground, another aircraft, space) or programmed and fully autonomous". Article 8 of the Chicago Convention, as amended by the ICAO Assembly, states that "no aircraft capable of being flown without a pilot shall be flown without a pilot over the territory of a contracting State without special authorisation by that State and in accordance with the terms of such authorisation. Each contracting State undertakes to ensure that the flight of such aircraft without a pilot in regions open to civil aircraft shall be so controlled as to

obviate danger to civil aircraft.” Consequently, all unmanned aircraft, whether remotely-piloted, fully autonomous or a combination of both, are subject to the provisions of Article 8 and have been defined by ICAO as “aircraft”.

5.38 Since ICAO has defined UAs as aircraft, this implies that UAs are within the scope of the Regulation. However, the Regulation explicitly excludes some categories of UAS as follows:

- Article 2(2) of the Regulation excludes State aircraft, and therefore UAs that are used for civil but State use (such as customs or police) are therefore excluded.
- Article 2(2)(a) excludes model aircraft of less than 20kg from the scope of the Regulation. The main characteristic of model aircraft is that they are used for sporting and recreational purposes, not for commercial, scientific or governmental application. Moreover their flights are limited to specific areas under well-defined conditions. Rules and definitions of model aircraft may exist at national level but it is not clear if this is the case in every Member State and if rules are consistent. The UK CAA for instance defines model aircraft as “any small Unmanned Aircraft (0-20kg) used for sporting and recreational purposes” or “any Unmanned Aircraft (over 20kg) used for sporting and recreational purposes”; therefore, according to this definition, UAs used for civil commercial applications cannot be categorised as “model aircraft” and are not excluded from the scope of the Regulation by Article 2(2)(a) even when their MTOM is under 20kg.

Third-party liability of Unmanned Aircraft

5.39 Where UAs are covered by the Regulation, the impact would only be with respect to insurance for third-party liability: they do not transport passenger or baggage, and although the supply of cargo by UAs could occur in the future, it is not a feature of UAs at present.

5.40 The Regulation defines the requirement for third-party liability insurance based on the mass of the aircraft. Accordingly the insurance requirement for UA would fall in the first four mass categories of the Regulation, as per the table below:

TABLE 5.3 UA THIRD-PARTY LIABILITY AS PER REGULATION 785/2004

Category	MTOM (kg)	Minimum insurance (million SDRs)	Minimum insurance (million €s)
1	< 500	0.75	~ 0.91
2	< 1 000	1.5	~ 1.81
3	< 2 700	3	~ 3.62
4	< 6 000	7	~ 8.45

Note: EUR-SDR exchange rate of 03/07/2012 (1 euro = 0.82854 SDR)

5.41 Interviews with stakeholders have shown that there is disagreement among experts as to the availability of insurance products for UAs:

- I One stakeholder said that insurance is only really available through the manufacturer's product liability (which is out of scope of the Regulation), with no or a very small amount of insurance available in the market for physical loss of vehicle (hull), or third-party liability. With only a very limited number of products available, the insurance industry would be reluctant to offer insurance for UAs until they better understand the operating risks and loss rates of UAs, as well as the laws applying to their operation. Moreover, the stakeholder believed that UAs could have a higher rate of loss than manned aircraft because the standards used in engineering are not as stringent as those for manned aircraft. Therefore this expert estimated that, for hull insurance, insurance rates could be 10 times higher than for manned aircraft in similar operating conditions and environments. Insurance rates for third party liability could be of the same order of magnitude higher when these products become available on the market. This would be for a limited period of time (5-10 years) until insurers become more aware of the loss rates and other factors and until the number of commercial operations of UAs expands. However levels of premiums so high would also act as a deterrent to UAs operators and may slow down the growth in this market.
 - I Another stakeholder disagreed with that view and stated that insurance is available for commercial UA operators for approximately €1,875 for €2.5 million third-party coverage. Moreover, this expert said that there are upwards of 80²² registered commercial UA operators in the UK all of whom are required to be insured to meet the UK CAA registration requirements. Therefore, this stakeholder considered that there were not significant financial barriers to entry into this market caused by minimum insurance limits.
- 5.42 In any case, stakeholders said that the level of premium for third-party liability (and hull) insurance would be correlated to the potential third-party exposure as well as than the mass of the UAs: for example, a stakeholder expected that land surveying UAs, which would be used mostly over built up areas, would be more likely to cause damage to third parties than fire-fighting UAs which would generally be used to survey bushfires or similar, which by definition are not in built up areas.

Conclusion on UAs insurance requirements

- 5.43 The industry recommended that the question of UA insurance would be best addressed outside Regulation 785/2004. This Regulation had been drafted based on air carriers' needs and operating models, albeit extended to aircraft operators. Stakeholders suggested a specific set of EU rules for UAs but conceded that in the short-term, before specific rules are prepared for UA insurance requirements, explicitly including UAs in the Regulation would be a safeguard.
- 5.44 At the time the Regulation was drafted, it was not envisaged that significant numbers of aircraft would have very low MTOMs. However, a significant proportion of UAs for civil use are likely to be under 15kg. The current Regulation requires these to have insurance for third party liability of 0.75 million SDR which does not seem to be unaffordable.

²² The UK CAA did not respond to our clarification question to confirm this statement.

- 5.45 The Regulation should also clarify the definition of ‘model aircraft’, to clarify whether UAs of less than 20kg are intended to be in scope. This could be defined based on their usage (recreational or commercial): unmanned aircraft used for recreational activities (including air shows) and under 20kg would then be defined as “model aircraft under 20kg” and therefore excluded from the scope of the Regulation. Where used for commercial activities, even if under 20kg, they would be included in the scope of the Regulation.

Insurance for airports and other service providers

- 5.46 In the EU there is no harmonised framework for third-party liability of airports or other service providers. This means that, in some Member States, there is no legal requirement to have public liability insurance to cover such claims, although prudent operators will nonetheless have such coverage in place. Airports and air carriers generally require ground handlers to have such coverage as a condition of their supply contracts (although ground handlers are protected from most liability if they operate under the IATA Standard Ground Handling Agreement).
- 5.47 There were problems in the immediate aftermath of 9/11, especially for aviation security providers who could not obtain third-party liability insurance. However, the market now provides war, terrorism and other perils cover on a primary and excess basis for all these parties on an annual aggregate limit basis.
- 5.48 This section aims at giving a first analysis based on available data on whether there should be a harmonised EU legal framework for third-party liability of airports or service providers.

Airports

- 5.49 There are differences in airport insurance and liability requirements between Member States. In the UK, for example, there is no legal requirement to have public liability insurance; and in some other States, such as Poland and Italy²³, there is no minimum amount of liability insurance for airport managing entities, so in practice it is left to the insurance broker and the airport risk manager to ensure adequate cover.
- 5.50 Third-party liability of airports covers a wide range of claims, some minor such as passengers slipping and falling in the terminal whilst on the other side of the spectrum airports could potentially be held liable for their contribution to a catastrophic loss. For example an aircraft could crash on take-off after birds are sucked into an engine, and the airport could be held responsible for the crash if it did not have a comprehensive and successful wildlife control programme in place.
- 5.51 ACI Europe, which was consulted for this study, did not raise particular issues regarding the current non-harmonised provisions. We are not aware of the level of liability held by airport authorities and whether or not they would be sufficient in the case of a catastrophic failure.

²³ ENAC has set in 2008 minimum amounts for third party liability insurance for handlers, depending on the activity handled. These minima are also applicable to airport managing entities when they act, totally or in part, as ground handling service providers.

Ground handling

- 5.52 For ground handling activities, most (but not all) Member States require proof of adequate insurance, notably when approving groundhandling operators, but only few States prescribe what the limits are. Poland for instance defines the minimum amount of liability insurance as the equivalent of 10,000 SDR for every 1,000 passengers or tonne of cargo and mail but not more than 5 million SDR or 15 million SDR respectively. The maximum amount depends on the category of groundhandling services.
- 5.53 Most contractual relationships between commercial scheduled aviation operators and ground handlers use the IATA Standard Ground Handling Agreement (SGHA) which is an international recognised document and is primarily used in the commercial aviation world. The SGHA was designed to make it easy to enter and terminate handling agreements between an airline and its groundhandling service provider, but it is not a compulsory standard so there are handling contracts based not on the SGHA but on airline specific forms. SGHA latest version is from 2008 and is expected to be revised with a 2013 version. It is IATA's Aviation Ground Services Working Group which is responsible for the Aviation Ground Services Agreement (SGHA) and is made of representatives from IATA carriers and ground handling companies.
- 5.54 The SGHA consists of three parts:
- The Main Agreement in which the parties agree on the legal and administration clauses including rights and liabilities each party has;
 - Annex A which describes the ground handling activities;
 - Annex B which sets out other issues such as the locations where the services are to be performed and the agreed handling fees.
- 5.55 Article 8 of the SGHA Main Agreement regulates the liability position between airlines and ground handling companies. The SGHA places strong limits on the liability of ground handlers, so that in most circumstances they are only liable for damage which is caused intentionally. It is not sufficient to prove that the ground handler was negligent. Recent versions of the SGHA have extended handlers liability, but only in limited areas.
- 5.56 In the past, airlines indemnified the ground handler against any claims for damage to their aircraft (or other property), or any liability in respect of passengers, employees, baggage or cargo, except where the damage was caused intentionally by the ground handler (SGHA Article 8.1). A ground handler would usually have had to give the airline an indemnity if an employee steals cargo and exposes the airline to liability to the cargo owner.
- 5.57 Since 1996, Article 8.5 of the SGHA has required ground handlers to indemnify airlines where the negligent operation of ground support equipment by them has resulted in damage to aircraft which they are servicing. That indemnity is limited to claims in excess of US\$3,000 but is capped at US\$1.5 million. In 2004, this was extended to cover aircraft damage however caused, whether or not such acts or omissions involved the use of ground support equipment²⁴.

²⁴ Source: QBE Aviation Service Provider liability management

- 5.58 For cargo (excluding mail), Article 8.6 requires ground handling service providers to indemnify airlines for direct loss or damage to cargo caused by negligent acts or omissions in the provision of services and/or the supply of goods by the ground handling business to the airline. However, the liability is limited to the lower of:
- 17 SDR per kilo (the Montreal Convention limit); or
 - The actual amount of compensation paid by the airline.
- 5.59 This indemnity is limited to claims in excess of US\$500 and is capped at US\$1 million. Article 8.6 also mentions that the liability of the ground handling service providers shall never exceed the liability of the carrier: it creates consistency with the terms imposed by the Montreal Convention and Regulation 785/2004 on airlines and the ground handling service providers).
- 5.60 For passengers and baggage, Article 8.1 states that a carrier cannot claim against ground handling service provider for delay/injury/death of passengers or delay/damage/loss of baggage arising from an act or omission of the ground handling service providers unless intent can be established, and that the carrier shall indemnify the ground handler, provided that the indemnity of the carrier to the ground handling service provider is limited to the amount that the carrier would have been liable if it had committed such act or omission.
- 5.61 For third-party liability, there is also very little scope for claims between the carriers and the ground handling service providers as regards to damages caused by the carriers' aircraft: Article 8.2 states that carriers cannot claim against ground handling service providers for third-party damages/delay/injury/death/loss caused by the carrier's aircraft arising from an act or omission of the ground handling service providers unless intent can be established. This means that in most cases third-party damages made by a carrier aircraft resulting from ground handling negligence would have to be indemnified by the airline. It is important to note that third-party damages other than those caused by the carrier's aircraft are not covered by SGHA.
- 5.62 In principle, airlines do not have to use the SGHA. For example, a stakeholder noted that there is an increasing tendency for airlines to impose exceptions to SGHA Article 8.5, resulting in the handler being liable for damages caused by negligence or omissions. However, in some cases, the airline/operator may also be required to accept a ground handler's specific contract terms, particularly if there are a limited number of ground handlers at the airport and therefore limited competition.
- 5.63 Refuelling is a particular activity of ground handling that carries the potential for significant exposure to airline catastrophic losses. If the kerosene becomes contaminated by water or grit or any other agent, it can lead engines to suddenly stop working.
- 5.64 There have been some examples in the past where minimum insurance provisions (or lack of) in the ground handling sector have acted as barriers to entry and did not necessarily ensure a level playing field²⁵. After 9/11, it was found that a number of groundhandlers either did not have sufficient insurance to cover liability

²⁵ Possible revision of Directive 96/67/EC on access to the ground handling market at Community airports

against third party damage, or in some cases did not have any insurance cover at all. Consequently the Commission suggested in its *Proposal for a Regulation on groundhandling services at Union airports and repealing Council Directive 96/67/EC* (COM (2011) 824 final) that “the granting of approval should be subject to minimum insurance requirements”.

- 5.65 The CAAs consulted in the evaluation of Regulation 785/2004 did not appear to have particular views on this issue, although this may be because (despite our requests) it was not necessarily the CAA ground handling expert who was responding.

Air Navigation Service Providers

- 5.66 In most Member States, Air Navigation Service Providers (ANSP) are State entities and any need for insurance is met by the State. However, some States including the UK and Poland do require ANSPs to contract insurance. Currently there are no common levels of insurance for ANSPs, or providers of EGNOS/Galileo satellite air navigation systems.
- 5.67 The UK CAA informed us that “the UK has exercised its right under Article 7 of EC Regulation 2027/2005 to require an ANSP to hold third party insurance as a condition of the grant of its Air Navigation Service Provider Certificate (ANSPC). Although EC Regulation 2096/2005 does not specify minimum levels of insurance, the United Kingdom has therefore based its national levels on the minimum levels set out in Regulation 785/2004”. The minimum insurance levels are based on those defined in Article 7, with the only difference being the definition of the “weight” categories. For each ANSP, the insurance required is based on the size of the largest aircraft that regularly operates to the airports where the ANSP provides services.
- 5.68 The UK CAA has exempted ANSPs with a turnover of less than £1 million (€1.2 million) per year from the requirement to hold war risk and allied perils cover, but not third party cover. This appears adequate, because those ANSPs would generally be terminal area providers of air navigation services for small size airports where the risk of war and other perils should be limited.
- 5.69 In Poland, the minimum amount of liability insurance for ANSPs is the equivalent of 30 million SDR. This is very different from the approach used by the UK CAA where NATS’ minimum amount of liability insurance would be 700 million SDR.
- 5.70 There is a potential for catastrophic losses from ATC errors such as the Uberlingen disaster above Germany where two aircraft collided in flight as a result of conflicting instructions from the ATC provider and the on-board collision avoidance systems. The identification of liability in this case was complicated by the fact that the airspace was controlled by the Swiss ANSP, Skyguide, even though it was over Germany.
- 5.71 ANS is still generally provided on a national basis by State-owned companies. Therefore, it is too early to conclude if there is a need of harmonisation for third-party liability or insurance requirements. However, it is possible that, as Functional Airspace Blocks mature, ANSPs will increasingly provide services within FABs on a cross-border basis; in this context insurance requirements should be monitored to ensure that they do not distort the market.

Other services

- 5.72 The other most important sector to consider is private airport security services. The cost for insurance for third-party liability is estimated by ASSA-I (the trade association of [security services providers]) as being several million euros per year. Most Member States do not regulate the issue of third-party liability for the aviation security sector.
- 5.73 The aviation security services have indicated that insurance and re-insurance for third-party liability is very difficult to obtain for acts of war, weapons of mass destruction or terrorism; and when it can be obtained at all, it is at a very high price. The industry is also very concerned with the current distribution of risks between Member States and security providers: since most States do not address the issue, the third-party liability would be the one of each individual Member State, but there are some exceptions where some kind of protection is being offered:
- France: The French State takes back part of the responsibility - outsourcing security to private security providers is allowed but the liability remains with the State.
 - Spain: There is exist an agreement on the split of risks (“Consortia de Compensación de Seguros”) which was established after the 2004 Madrid bombings.
 - UK: There is a reinsurance pool set up by the insurance industry in co-operation with the UK government so that insurers can cover losses resulting from damage caused by acts of terrorism to commercial property in Great Britain.
- 5.74 Clearly terrorist attacks are in general directed towards States rather than towards private companies or individuals and their impact are both national and international. The security services industry and most stakeholders share the view that this should be reflected in the allocation of liability following a terrorist attack. Therefore the industry advocates a similar EU instrument to Regulation 785/2004 for the security sector in respect of third party liability in the case of an act of terrorism or act of war. This would apply the principle of strict, but capped, liability.
- 5.75 However, any proposals in this respect should only be developed after thorough analysis, including an impact assessment, as any regulation would result in changes to established contractual relationships between airports, airlines and service providers.

Other issues*Other terms requiring clarification*

- 5.76 Some other terms are considered by some stakeholders to be **unclear** and their interpretation may need to be clarified in order to better harmonise the application of the Regulation across Europe:
- Article 2(2): The wording of this article has been found slightly ambiguous by regulatory authorities. Article 2(2)(g) could be included in a separate item.

- Article 4(2): An enforcement authority thought that there remains some lack of clarity on the provisions regarding joint operations such as charters, codeshares, franchises. Recital 15 and Article 4(2) may create administrative complications for Member States when they need to have the certainty that all flights will have adequate coverage without imposing double insurance.
- Article 6: Some enforcement authorities consider it is unclear whether the minimum insurance should be based on the commercial capacity of the plane as defined by the operator, or the maximum number of seats which could be installed, as defined by the manufacturer - although as the requirement is per passenger, we are unclear that this should be a problem.
- Article 6: An enforcement authority thought that additional coverage for the air carriers authorized to carry dangerous goods would require clarification and/or action.
- Article 7: Aggregates or “combined single limits” are customary for the insurance aviation market and are authorised when they do not undermine overall compliance of the air operator with its minimum obligations but one enforcement authority noted that it generated additional calculations and administrative checks.
- An enforcement authority explained that they would appreciate clarification on small aircraft operations on local flights (take-off and landing from the same airfield) for commercial and private purposes. For small aircraft the owner of the aircraft is the “aircraft operator” (as per Article 3(d)) and the insurance certificate according to Regulation 785/2004 is in name of the owner. Non-commercial operations do not require minimum insurance cover for baggage and cargo and limited insurance cover in most Member States if passengers are carried (Article 6). When the aircraft is leased to an operator for sight-seeing for instance, the adequate minimum insurance cover must be purchased for passengers, baggage and cargo. However if it is still in the name of the owner and not the operator, then the CAA does not accept the insurance certificate. It does not consider either that the small local aircraft operator is a “community air carrier”, because according to Regulation 1008/2008 recast of Regulation 2407/92 local flights are exempted from having an operating license.

Impact of sanctions

- 5.77 Some of the insurance industry representatives that responded to the study expressed a concern that sanctions imposed by the EU, the USA or the UN on some countries may have a detrimental effect on insurance coverage. For instance there have been US sanctions on Iran since 1987 whereby the USA prevents companies that have links to the US from doing business with Iranian companies, and the EU introduced similar sanctions in October 2010. Until that point, Iranian airlines had been insured in the London market. However this has not stopped flights between the EU and Iran, operated by Iranian airlines: Iran Air for instance flies to/from Heathrow three times weekly. Iranian airlines have been able to produce insurance certificates showing that they meet the requirements of the Regulation, but the industry has questioned the underwriting of this insurance, as it does not come from the London or any western country market.

Identity of the insurer

- 5.78 Insurers and re-insurers are strictly regulated in the EU, and this will be further strengthened in future by Solvency II. Other large developed markets also have strict regulation applying to insurance, but this may not be the case everywhere else. One national authority raised a concern about insurance being contracted from providers in third countries with weak regulatory or legal systems, or where judgements could be difficult to enforce (an example was given of a company with insurance contracted in Northern Cyprus).
- 5.79 A stakeholder also mentioned that, Germany requires that all the insurance should be secured with EU registered insurance companies (if the aircraft is registered in Germany). This means that German operators can be precluded from using perfectly acceptable insurance security from outside the EU thus narrowing the options to buy insurance.
- 5.80 However, the LBA requirement (if our enquiry confirms that it is true) of asking for insurance to be purchased from EU-based insurers seems to be excessive: insurance contracted in a developed and effectively regulated market, such as the US, should be sufficient.

Deductibles

- 5.81 The use of policies with deductibles is standard industry practice, as for other types of insurance. The deductible is an amount that is covered by the policyholder before the insurer pays any claim. We have been told that, for hull insurance, it is standard practice for deductibles to be as high as US\$1 million. However, it is not normal practice in the aviation insurance market for there to be deductibles in respect of aircraft liability coverage (other than small amounts relating to passenger baggage/personal effects (normally no more than US\$1,250) and cargo (normally no more than US\$10,000). For liability, the airline may opt to retain a certain amount of the liability risk, but this would normally be insured within a captive²⁶.
- 5.82 In most circumstances the air carrier or aircraft operator should have sufficient assets to cover the deductible, and so this should not raise any problems. However, in theory some air carriers may become insolvent shortly after (and perhaps in part as a consequence of) major accidents. In the event that a carrier were to become insolvent after an accident, it would not be able to cover the deductible. In this case passengers and third-parties would not necessarily enjoy the level of protection that is sought from the Regulation. However, stakeholders have indicated that deductibles are usually only an internal offsetting between the insurer and the airline or operator, so there should be no risk of unpaid amounts.

MTOM bands for third party liability

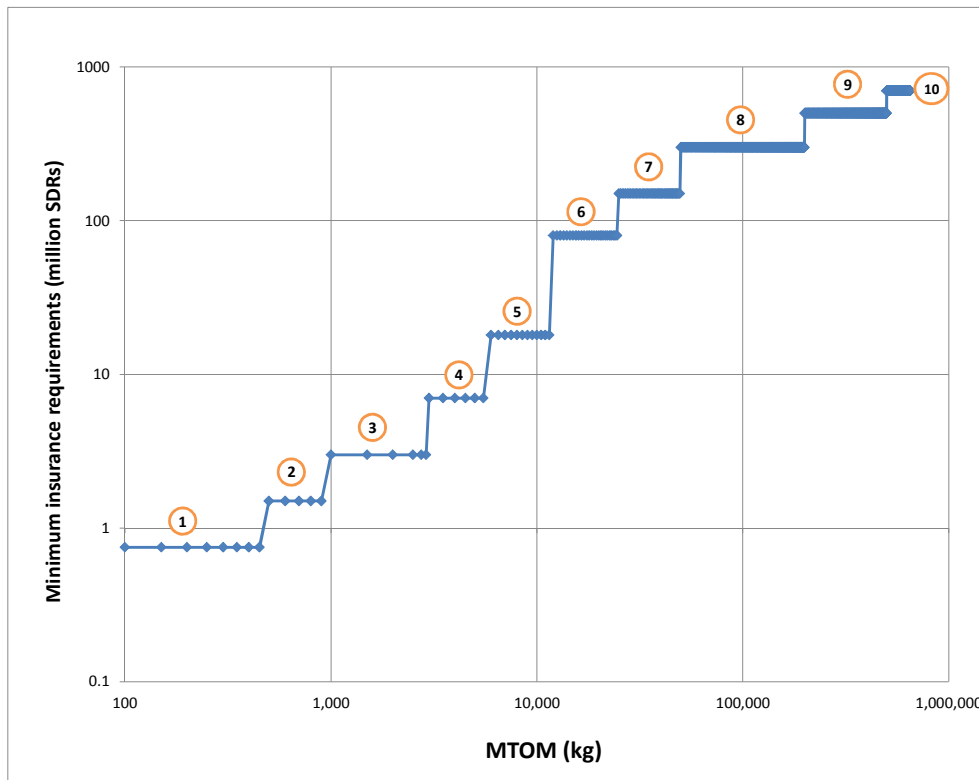
- 5.83 Third-party liability defined in Article 7 is based on MTOM bands as discussed above and imposes step changes. In particular, between categories 5 and 6, the MTOM category is multiplied by 2.1 but the insurance requirement is multiplied by 4.4. The steps between other categories are (in relative terms) significantly smaller. This is of course primarily an issue for those aircraft that are just above

²⁶ Captive insurance is insurance or reinsurance provided by a company that is formed primarily to cover the assets and risks of its parent company.

the threshold for band 6, for which the requirement appears disproportionate. Heritage aircraft operators highlighted that this was particularly an issue for non-commercial operators.

- 5.84 The current scale seems to have been designed to force most commercial aircraft types to have quite substantial third party liability insurance. If this is to be addressed it could be achieved through the introduction of an intermediate band.

FIGURE 5.2 MINIMUM THIRD-PARTY INSURANCE VS. MTOM CATEGORIES



Source: Steer Davies Gleave analysis

Update for inflation

- 5.85 The Montreal Convention liability levels were updated for inflation in 2009. A provision could be inserted to ensure that prescribed limits in Regulation 785/2004 are automatically increased in line with the Montreal Convention rather than later on through a new Regulation (285/2010).

6 Conclusions and recommendations

6.1 Regulation 785/2004 has largely achieved the objective of harmonising insurance requirements within the European Union (EU) by establishing minimum requirements for all operators, regardless of nationality. The definition of relatively high minimum thresholds for coverage has contributed to the objective of consumer protection and may also have contributed to the development of safer air travel.

The need for a regulation on insurance requirements

6.2 All stakeholders overwhelmingly supported Regulation 785/2004 and thought it addressed the issues it was meant to address. Relatively few issues were raised by the stakeholders, although as discussed in section 5 above, there were some common themes.

6.3 No stakeholders suggested that minimum requirements for insurance should be removed, and in any case, this would result in:

- A conflict with the Montreal Convention which requires the States to establish minimum requirements of liability insurance.
- A risk that some airlines operating into the EU might not have appropriate liability coverage in place and therefore a risk that potential EU and non-EU victims of accidents would not receive adequate compensation.
- EU Member State would have to establish their own minimum liability insurance requirements, which would distort the single market for air transport and increase the administrative workload for insurers and operators. Although commercial airlines might already exceed any national requirements, it could create barriers to cross-border movement of light aircraft.

6.4 Most stakeholders considered that the definition of harmonised insurance requirements in the European Union is proportionate to the issue under consideration and has a useful impact. Therefore, we conclude that there is still a need to retain these requirements at EU level.

Recommendations

6.5 Most stakeholders consider that the Regulation is working well and there is no urgent need to change it. However, some (mostly relatively minor) issues have been identified in the course of our research, and there could be some benefits from addressing these. In accordance with the Commission's normal practice, an impact assessment would be required before any such changes could be made.

Third-party liability

6.6 We do not see any significant benefits from harmonisation of rules on third party liability. The level of fragmentation is not considered by either Member States or the industry to pose a problem, and therefore we do not see a need for action from the EU on this matter. Although strictly not relevant to this evaluation, we have also been advised it is likely to be very difficult to get Member States to agree a common position.

- 6.7 However, the Commission should consider the creation of additional weight bands for third-party liability insurance requirements. At the time the Regulation was drafted, the possibility of unmanned aircraft being used for civil purposes was not considered, and the current lowest weight band (which covers all aircraft of less than 500kg) may be considered to create a disproportionate and unnecessary burden for very light unmanned aircraft. However, any addition of lower bands to accommodate very light UAs would need to be carefully weighted against the risk of damage caused by UAs in the case of accidents. The addition of lower weight bands would not necessarily mean a reduction in insurance requirements at any level; although no issues with this were raised by stakeholders, the minimum insurance for small aircraft already appears quite low given the damage these could potentially cause (for example if an aircraft crashed into a group of people).
- 6.8 Additionally, the steep change between category 5 and 6 could be softened by the addition of a middle band to make levels of third party cover required more proportionate. Again, this does not necessarily mean that there should be a reduction in the minimum level of coverage at any level - it could either be achieved by increasing the coverage required for aircraft at the upper end of band 5, or reducing the coverage required for aircraft at the lower end of band 6.
- 6.9 Any changes to the weight bands should take into account the potential damage that aircraft of different sizes could cause to third parties in the event of an accident.

Certificate of insurance

- 6.10 We recommend that a standard-format insurance certificate should be defined: if an air carrier or an aircraft operator were to provide a CAA with such a certificate a different format could not be requested. Examples of certificates are provided in Appendix A.
- 6.11 Although the standard certificate could be provided through guidance, there is then a risk that some regulatory authorities would not use it (and would not have to). Therefore we recommend that acceptance of a standard certificate should be a binding requirement. However, if a certificate was to be defined, this should not be within the main text of the Regulation, as flexibility would be needed to revise this quickly to adapt to market circumstances. This could be achieved through the Regulation delegating power to the Commission, using the mechanism in Article 290 TFEU, to define the certificate.
- 6.12 We see no reason why certificates from insurance brokers are not allowed at domestic level whereas they are for international carriers. Therefore we would recommend that the Commission clarifies that certificates from brokers can be used for both international and national carriers.

Exchange rate fluctuations

- 6.13 As explained in Chapter 5, the minimum insurance requirements are defined in SDR but insurance can only be contracted in hard currencies, in practice almost always in US dollars. Therefore, there is a risk that where operators contract the minimum specified insurance, they end up being under-insured due to exchange rate fluctuations. However, the administrative burden that this generates for regulatory authorities and the insurance industry is not excessive (limited to

occasional checks that insurance is still sufficient), and we believe there is not much that can be done on this issue. Therefore we recommend not changing the Regulation on this matter.

Mail

- 6.14 Although this is not specifically addressed in the current Regulation we have not identified any need or benefits from harmonising this requirement. The legislative framework is in place and well known by the stakeholders, so there is a risk that the disruption created by an amendment to Regulations 785/2004 and 1008/2008 would be greater than any benefits of harmonisation.

Unmanned aircraft

- 6.15 In the short-term, as explained in paragraph 6.7, we recommend that the Commission should consider the definition of one or two lower weight bands for third-party liability, to avoid creating a disproportionate and unnecessary burden for very light (usually unmanned) aircraft. We would also recommend clarifying the definition of model aircraft in Article 2, to make clear whether unmanned aircraft of less than 20kg are within the scope of the Regulation. This could be based on the distinction between recreational and commercial use.
- 6.16 In the longer term, the Commission should consider a specific legislative instrument on unmanned aircraft, and this could include consideration of whether the standard approach to third party liability insurance in the Regulation is appropriate for these aircraft.

Heritage aircraft

- 6.17 It is important that third parties are protected from potential damage from heritage aircraft, and therefore these cannot be excluded altogether from the scope of the Regulation. However, due to the nature of their operations, the minimum requirements may be excessive in specific circumstances, for example if the aircraft would only ever operate at well below their MTOM.
- 6.18 Therefore we recommend that the Commission should consider granting Member States the flexibility to reduce third party insurance requirements for these aircraft on a case-by-case basis where this is appropriate in the specific operational circumstances and other measures are taken by the State to ensure third parties are adequately protected.
- 6.19 An impact assessment would be necessary before any such proposal could be implemented, and as discussed in section 5 above, there could be some risks and issues with this proposal. Re-certification to operate at reduced MTOW as agreed between the operator and the national authority to correctly reflect the size and kinetic energy could also be considered.

Other aviation provider third-party liability

- 6.20 We have discussed with stakeholders whether there is a need for harmonised minimum insurance requirements for other aviation service providers. With respect to ANSPs, we do not believe this is necessary, as most ANSPs are State entities and therefore are in effect insured by the State. On the matter of airport insurance levels we do not believe there is an issue at EU level and recommend no further

action. The issue of insurance for ground handlers has been addressed by the Commission's recent proposal.

- 6.21 The most significant potential issue relates to insurance requirements for security service providers, who may find it difficult to obtain insurance against third party liability arising from terrorism. We would recommend that there is more research done at EU level on the impact of a lack of harmonisation on third-party liability in the case of terrorism.

Other issues

- 6.22 If the Regulation was revised, we would also suggest:
- Some of the terms which national authorities have found to be unclear could be clarified, for example relating to joint operations such as codeshares.
 - It should be clarified whether deductibles are permitted. We recommend they should be, as they are normal insurance industry practice, but this should be subject to safeguards to protect passengers and third parties in the event an accident led to the insolvency of the carrier concerned.
 - A provision could be inserted to ensure that prescribed limits in Regulation 785/2004 are automatically increased in line with the Montreal Convention rather than later on through a new Regulation.

APPENDIX

A

EXAMPLES OF INSURANCE CERTIFICATES

Reference:

CERTIFICATE OF INSURANCE

THIS IS TO CERTIFY that as insurance brokers we have placed insurance with Underwriters at Lloyd's and/or certain insurance companies who have authorised us to issue this certificate on their behalf in the name of [**Insured name**] (the Insured) covering [their fleet of aircraft **or list type(s) and registration(s) of individual aircraft**] against the following risks and up to the limits stated whilst operating anywhere in [the world **or insert any more specific geographical limits**]:

Aircraft third party, passenger (including baggage and personal effects), cargo, mail and aviation general third party legal liability for a combined single limit (bodily injury/property damage) of at least USD[],000,000 any one occurrence, any one aircraft and in the annual aggregate in respect of products liability.

The coverage provided includes war, terrorism and allied perils in accordance with the Extended Coverage Endorsement AVN52E deleting all paragraphs other than (b) of the War, Hi-jacking and Other Perils Exclusion Clause AVN48B, but aircraft third party, cargo and mail whilst not on board an aircraft and aviation general third party legal liability is subject to an overall sub-limit of USD[],000,000 any one occurrence and in the annual aggregate for all aircraft and aviation operations combined. This sub-limit is part of the above combined single limit and not in addition thereto and does not apply to cargo and mail whilst on board an aircraft, passengers and passenger baggage legal liability.

Furthermore, a separate excess third party war, terrorism and allied perils legal liability insurance has been placed to provide a limit of USD[],000,000 any one occurrence and in the annual aggregate for all aircraft and aviation operations combined excess of the sub-limit above. This combination provides an overall maximum total limit for third party war, terrorism and allied perils legal liability of USD[],000,000 any one occurrence and in the annual aggregate over both insurances at inception.

IT IS FURTHER CERTIFIED that the amounts of insurance stated above are in accordance with the minimum insurance cover requirements of Articles 6 and 7 of Regulation (EC) no 785/2004 based on (a) the rate of exchange applicable to Special Drawing Rights at inception of the insurance, (b) third party war, terrorism and allied perils being insured on an aggregate basis as above, and (c) it being understood that such aggregate limits may be reduced or exhausted during the policy period by virtue of claims made against aircraft or other operational interest covered by the insurance.

Subject to the coverage, terms, conditions, limitations, exclusions, excesses and cancellation provisions of the relative policies, numbered [] and [], which are in force from [] until [] both days inclusive [] standard time.

AUTHORISED SIGNATORY

Date

SEVERAL LIABILITY NOTICE - The subscribing insurers' obligations under policies to which they subscribe are several and not joint and are limited solely to the extent of their individual subscriptions. The subscribing insurers are not responsible for the subscription of any co-subscribing insurer who for any reason does not satisfy all or part of its obligations.

DETAILS OF AVIATION THIRD PARTY AND AVIATION PASSENGER AND CARGO LEGAL LIABILITY INSURANCES MAINTAINED IN FORCE BY LICENCE HOLDER OR APPLICANT

(Name of Licence holder or applicant)

1. POLICY DETAILS

<i>Liability</i>	<i>Policy Reference and Period of Validity</i>	<i>Aircraft type and Registration/s covered (please attach a list if necessary)</i>	<i>Limit of Insurer's Liability**</i>
AVIATION PASSENGER, THIRD PARTY AND CARGO (INCLUDING, IF ANY, EXCESS LIABILITY (PLEASE GIVE FULL DETAILS))			** Please show how limits are applicable, eg any one accident, in the aggregate, any one aircraft etc.
THIRD PARTY WAR AVN52			

2. POLICY INSURERS

We shall not require you to provide a list of all insurers participating in each policy with this application. However, please confirm the leading underwriter(s) to the risks. The CAA retains the right at any time to seek a list of all insurers participating in each policy and will if necessary invoke its powers under Section 84 of the Civil Aviation Act to obtain such lists.

3. POLICY RESTRICTIONS (in respect of each policy)

Please confirm the following:

(a) Does the permitted usage include Public Transport?:
(b) Geographical limits:
(c) Maximum number of passenger seats:

4 POLICY CANCELLATION/MATERIAL CHANGE (in respect of each policy)

(a) What period of notice is required for cancellation of or material change to the policies

(i) in respect of War and Allied Perils, if covered (AVN52)?

(ii) for any other reason?

(b) Are there circumstances in which the policies can automatically lapse

(i) in respect of War and Allied Perils, if covered (AVN52), other than Five Great Powers War, nuclear detonation or requisition of the aircraft?

(ii) for any other reason?

(c) Is this Policy subject to AVN2000A?

If so does AVN 2001A apply?

DECLARATION BY INSURER OR INSURANCE BROKER

We certify that to the best of our belief as Insurers of or Insurance Brokers to the Licence Applicant or Holder the above particulars, insofar as they relate to the insurance policies held, are correct. We further certify that each policy detailed above is in the form known as Lloyd's Aircraft Policy AVN 1C (or based thereon), or in the form agreed by the members of the Aviation Insurance Offices Association, or that the policies are no less favourable to the insured than one or other of the aforesaid forms and do not exclude liabilities which would not be excluded by one or other of the aforesaid forms.

We confirm that all underwriters participating in this policy are insurers that have been subject to this company's own vetting procedures.

Signed:	Name:
On behalf of:	Position of Signatory:
Date:	

TO WHOM IT MAY CONCERN

1 January 2005

This is to Certify that **G-XXXX** (*Aircraft type*) **[MTOM xxxxx kgs]**
 has declared a maximum of (**XXX**) passengers to be carried and is engaged in commercial/non-commercial* operations and
 is issued on behalf of **XYZ Underwriting Agency/Syndicate/Insurance Company**
(complete as applicable)~
 Policy Number: **MU04YYYYYY**
 In the name(s) of **Joe Bloggs Aviation and/or Associated and/or subsidiary Companies and/or Agents and/or Employees for their respective rights and interests.**
 For the period: **00.01 GMT 1 January 2005 to midnight GMT 1 January 2006**
 against all risks in flight or on the ground anywhere in (*complete as applicable*) e.g. EUROPE, THE MEDITERRANEAN, CANARY ISLANDS AND COUNTRIES BORDERING THE MEDITERRANEAN
 and coverage includes LEGAL LIABILITY to THIRD PARTIES and PASSENGERS up to the following Limit of Indemnity in accordance with EC Regulation 785/2004:

Part A

COMBINED SINGLE LIMIT
 (PASSENGER BAGGAGE*,
 CARGO, MAIL & THIRD PARTY LIABILITY): **£[],000,000** any one occurrence, any one aircraft and in the annual aggregate in respect of product liability
 WAR, TERRORISM AND ALLIED PERILS
 (as defined by AVN52E)

Part B

£[],000,000 any one occurrence and in the annual aggregate. Except to passengers to whom the full policy Limits shall apply.

Part C *Edit Note this paragraph will be inserted where required*

Furthermore a separate EXCESS WAR, TERRORISM AND ALLIED PERILS liability insurance has been placed

£[],000,000 any one occurrence and in the annual aggregate.

The TOTAL LEVEL OF WAR TERRORISM AND ALLIED PERILS liability insurance is

£[Part B +C],000,000 any one occurrence and in the annual aggregate.

Advice to third parties: This Certificate is evidence that the policyholder has insurance cover to comply with EC Regulation 785/2004. Full details of cover are in the Policy documents.

Signed: for and on behalf on ABC Limited
 Date:.....

*delete as appropriate
 ~ Whilst the CAA will not require a full list of insurers participating in each policy the leading underwriter(s) should be listed. The CAA reserves its right under Section 84 of the Civil Aviation Act 1982 to request such a list

Subject to the policy terms, conditions, limitations exclusions and deductibles

Edit note - the following items can be added by brokers as necessary but should be outside the "Regulatory Box" above. This is not intended to be an exhaustive list and brokers may add what they wish in this area so long as it is not in conflict with the statements made in the "Regulatory Box"

- Crown /MOD Indemnity of £7,500,000 any one accident/unlimited in all during the policy period
- Coverage herewith extends to CAA employees whilst acting as crew members and is extended to indemnify the Assured in respect of liability assumed by them in connection with the Flight Training by the assures of CAA employees.
- Danish Liability D.KR 60,000,000 Third Party Bodily Injury and D.KR 5,000,000 Property Damage any one accident/unlimited in all during the policy period. *Edit note* it maybe that this clause will no longer be required by the Danish authorities when the new Regulation comes into effect.

CONTROL SHEET

Project/Proposal Name Mid-term evaluation of Regulation 785/2004 on insurance requirements of air carriers and aircraft operators

Document Title Final Report

Client Contract/Project No. Click here to enter text.

SDG Project/Proposal No. 22408401

ISSUE HISTORY

Issue No.	Date	Details
3	11/07/2012	Issued to the Commission

REVIEW

Originator Clémence Routaboul

Other Contributors Simon Smith

Review by:

Print	Simon Smith
Sign	Approved electronically

DISTRIBUTION

Client: European Commission

Steer Davies Gleave:



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