

Air Passenger Rights

Commission's initiative on Passengers' protection in the event of airline insolvency for standalone air tickets

External study

Stakeholder workshop - 30 March 2011

Brussels 1040, Borschette Building (CCAB), rue Froissart 36, room 1D

Minutes

Executive Summary

On 30 March 2011, stakeholders related to air transport had the opportunity to present their views on the final report of a preparatory study in view of a Commission's initiative on Passengers' protection in the event of airline insolvency for standalone air tickets. Comments have stemmed from two concerns: concern for the industry and concern for consumers.

From the industry's point of view, competition must be preserved between airlines. The risk of disproportionate measures must be taken seriously given the very low number of stranded passengers concerned. The sector has been badly hit financially, an additional financial burden will be added in the framework of ETS and all these costs add up. Coverage of the insolvency risk is a commercial decision that should be taken by each airline individually. Insurance companies considered that an EU-wide compulsory insurance scheme is not feasible. From the consumer point of view, the study demonstrates that passengers with a seat-only ticket affected by an airline failure are badly hit by such an event. Package travels and seat-only tickets have the same feature of being paid in advance. There is no reason why passengers holding a ticket in the same plane should be submitted to different regimes.

A cross-cutting comment is also to use what already exists, be it by a better enforcement or modification of existing rules on financial fitness or existing arrangements within airline associations to repatriate stranded passengers.

INTRODUCTION

The realisation of a Single European Aviation Market has created new opportunities and an important increase of the air traffic within the EU and towards third countries. It has been accompanied by a process of regulatory convergence in various fields and notably passengers' protection.

The revision of the 3rd package on air services already dealt with airline insolvencies, with the objective to improve the financial fitness of airlines, which is effectively reflected in a number of provisions of Regulation 1008/2008¹ that entered into force on 1st November 2008. Passenger protection against airline insolvency is an issue directly related to citizens that has raised media and political interest: in a resolution adopted on 25 November 2009, the European Parliament asked the Commission to act on passenger protection in case of airline insolvency.

It is now time to complement the action in this field and to consider the protection of passengers in case of airline insolvency.

The Commission launched a general public consultation on air passengers' rights that included the issue of consumer protection in case of airlines' insolvencies. It ended on 28 June 2010 and its results are available on the website of DG MOVE². The Commission has taken stock of this consultation and has undertaken a second study specifically aiming at evaluating the impact of insolvencies in air transport for passengers holding a standalone (seat-only) air ticket. This preparatory study encompasses a number of possible scenarios that would bring appropriate remedies, in particular in terms of care and repatriation, but also ticket refund for passengers who had not started their journey yet.

This preparatory study has been commissioned to the Steer Davies & Gleave consultancy firm. It is now finalised. The final report will be the basis for the Commission's impact assessment in view of possible action on this subject matter. Before this report is published, the Commission has taken stakeholders' informed views on the assumptions, reasoning, envisaged options and conclusions. A workshop has been held in Brussels on 30 March 2011 where stakeholders communicated their views to the Commission on this report.

The point for the Commission in this technical meeting was getting the views of the stakeholders on this issue and checking that the consultant and the Commission were technically right on facts and figures.

¹ Regulation (EC) No 1008/2008 of the European Parliament and of the Council of 24 September 2008 on common rules for the operation of air services in the Community (Recast) (Text with EEA relevance)

² http://ec.europa.eu/transport/passengers/air/air_en.htm

STEER DAVIES & GLEAVE'S PREPARATORY STUDY: GENERAL CONCLUSIONS

From 2000 to 2010, the consultant identified 96 insolvencies of airlines providing scheduled services - a relatively small figure. The proportion of total EU passengers affected by airline insolvencies is less than 0.07% for each year. However, the impacts on each passenger can be significant: the risk to remain stranded far from home, with all its consequences (to pay another flight back home, to incur additional accommodation costs) and/or never be reimbursed for the part(s) of the journey not made. Of the passengers purchasing standalone tickets affected by insolvency over 2000 to 2010, the consultant estimates that 76% did not have any form of protection. Stranded passengers incurred the highest immediate costs resulting from airline insolvencies of over €796 on average. This figure was influenced by the failure of Air Madrid, which left numbers of passengers stranded in South America. Passengers who had not left yet and renounced to their trip lost €315 in average and passengers who decided to rebook lost €390 in average.

The conclusion of SteerDavies&Gleave's final report is that only one option is feasible AND delivers the main objectives of the Commission (assistance/care to passengers; repatriation; reimbursement): the establishment by EU legislation of general reserve funds implemented at national level. This solution would not be as such very costly for airlines, but it would distort competition since passengers on airlines at very low risk of insolvency would subsidise passengers booking with weaker airlines. Some of the largest carriers are also the financially strongest and their passengers would be major contributors to a general reserve fund, for no gain. The uniform cover would mean that passengers would no longer consider the financial stability of carriers when making purchases. The main alternative is self-regulation: the Commission could encourage the industry to take action to protect passengers (for example by improving the availability of SAFI and by repatriating stranded passengers) and make clear that action would be taken in future if this was not successful.

The 4th policy objective of the Commission is to make sure that the protection instrument(s) meets these protection objectives at a lowest cost and maximum flexibility for the sector (air companies). In the consultant's view, since reserve funds are the only feasible option which is effective in achieving the consumer-related objectives of the study, there has to be a political judgement as to whether the problem of the impacts of airline insolvencies on passengers is sufficiently large to justify this market intervention.

OPINIONS OF THE STAKEHOLDERS

On consumer detriment

Airline associations acknowledge that it can be stressful for individual consumers to be stranded at destination as a result of airline insolvency but remedies are available (ELFAA). However, the instances of insolvency occurring are sufficiently low (and the consultants' presentation to the workshop indicated no particular trend) so as not to require regulatory intervention (IACA/ELFAA). Air passengers are no different than any other consumers (ERA, IACA). Improvement of passengers' awareness of the risks of bankruptcy is important (ERA).

According to travel agents, the study demonstrates that passengers with a seat-only ticket affected by an airline failure are badly hit by such an event. For travel agents, the study lists only

bankrupt airlines registered in the EU. The impact of non-EU airlines' failure on EU passengers who bought their ticket within the EU is not taken into consideration. (ECTAA).

For consumers, the study demonstrates that passengers with a seat-only ticket affected by an airline failure have to incur major costs (BEUC, Which? Travel). Package travels and seat-only tickets have the same feature of being paid in advance; there is no reason why passengers holding a ticket in the same plane should be submitted to different regimes depending on how they bought their ticket (Which? Travel).

On Risk prevention

According to airline associations, EU Regulation 1008/2008 imposes financial supervision by EU Member States; these provisions must be implemented (IACA). Regulation 1008/2008 provides for specific rules: licensing authorities are to carry out regular assessments of their air carriers' financial situation (Recital 5). Article 9 obliges licensing authorities to suspend airline operations in case of financial problems of the airline (AEA). Regulators, when granting a licence, have a duty to ensure themselves that airlines had sufficient cash resources and access to capital backing to safely accept forward sales for long periods ahead. Consistent with this, regulatory bodies should exercise their responsibility of oversight of airlines, requiring carriers, which show signs of financial difficulty e.g. non-payment of airport charges, taxes etc, to be subject to more frequent and closer financial reporting to the regulator. When clear signs of financial weakness, such as non-payment of taxes to Government, were emitted, it would be open to Regulators to impose a limit on an airline's permitted forward-selling interval, thus limiting the number of passengers at risk. This would offer passengers more valuable protection before the event, rather than rescue following it (ELFAA).

Steer Davies & Gleave had explained before that the impact of potential measures in this field would be limited as authorities cannot intervene to prevent insolvencies. In a market economy, weak companies must be allowed to fail.

On existing protection schemes

Airline associations detailed existing protection schemes already available for passengers which according to them allow to deal satisfactorily with this issue. Self insurance gives consumers the freedom to purchase a self- and optional insurance covering passengers against any potential risk. Airlines were prepared for the Commission to mandate the offer of voluntary insurance to passengers but the passenger should be free to take it or not. This would have the added benefit of an audit trail, confirming the passenger's decision re insurance (ELFAA). Today this insurance is available (e.g.: via travel agents, airlines, insurance companies). The Package Travel Directive is applicable to air travel where it is included in a package. If the ticket is purchased on internet, direct from airlines, via travel agents, the consumer is protected before the start of the journey through credit card schemes. Accepting credit card comes at a significant cost for airlines. (AEA). Low fares airlines sell predominantly via the web. The most-preferred means of payment - credit card - offers certain protection. In addition, airlines offer to sell customers their own insurance cover, most of which policies include Scheduled Airline Failure Insurance (SAFI), as part of the insured risks (ELFAA). In the context of IATA's Billing Settlement Plan (BSP), when a carrier's licence is suspended, travel agents are instructed to suspend ticketing activities on behalf of the suspended carrier. They also have to report any sales, refunds or other transactions made on behalf of the suspended airline to the BSP to settle all outstanding billing directly with IATA's BSP or with the suspended airline. When IATA withholds funds from a suspended airline IATA will

always try to reach an agreement with the suspended airline or its administrator³. In case of interlining agreements, if a carrying airline becomes insolvent, the issuing airline will still have the money which is refundable through IATA's BSP. If passengers are stranded, they could find alternative flights with another airline part of the Multilateral Interline Traffic Agreement (MITA). If the issuing airline becomes insolvent, refund can be performed through IATA's BSP, if a refund agreement has been reached with the suspended airline (IATA).

Travel agents took note that the study indicates⁴ that payment by credit cards reach the airlines typically between 30 and 60 days and that the passengers of a bankrupt airline may be able to obtain a refund during this period. They understand that payments by credit card usually reach the payee within 3 business days, which limits tremendously the period of protection. Also, the study indicates⁵ that IATA's BSP may withhold any payment made to the airline and these may be used to refund passengers - subject to agreement with the airline or appointed administrator. According to travel agents, this finding gives the impression that IATA's BSP affords a systematic protection of passengers in case of airline failure. However, their experience in recent years has been that bankruptcy administrators have usually required the amounts withheld in IATA's BSP, which were then subject to the bankruptcy proceedings (e.g. Air Madrid). The only notably exception is in France where the French association of travel agents SNAV uses a specific feature of French law to ask a judge to block the money held by IATA's BSP in view of reimbursing passengers. Moreover, they wonder whether IATA, where it has had the possibility to use the money withheld in its BSP, used it to reimburse passengers in priority, or to settle firstly interlining agreements with other airlines (ECTAA).

According to the insurance sector, consumers should be free to choose how to protect themselves against airline insolvency (CEA). There is room for limited optional niche market insurance products like SAFI (IPP).

Consumer associations insisted that passenger information on existing schemes is totally insufficient and scattered, which makes consumer choice very difficult (BEUC, Which? Travel).

³ In 2008, 20 airlines have been suspended, in 15 cases funds were withheld with 11 refund agreements - 100% of the refunds have been processed (except for one, 95.7%). In 2009 20 Airlines have been suspended, in 9 cases funds were withheld, 5 Refund Agreements have been passed - 100% of refunds have been processed. In 2010 16 Airlines have been suspended, in 2 cases funds were withheld and 2 Refund Agreements have been passed- 100% of refunds have been processed.

⁴ Under point 3.14 of the report

⁵ In point 3.27 of the report

On compulsory airline insurance

According to airlines, consequences of compulsory insurance would be very negative. As shown in Steer Davies Gleave's report, it would distort competition with non-EU carriers, would lead to an increase in ticket prices, higher costs and less choice for consumers. A small number of passengers would benefit from it, and it would be unfair on financially viable airlines: individual airlines could be deemed uninsurable (AEA).

Insurance companies take the view that compulsory insurance schemes hinder insurer ability to spread risk whereby insurers can accommodate far bigger exposures than their own financial strength on the basis that they will not need to cover numerous claims simultaneously. On large-scale risks, reinsurance can be bought to contain losses to a financially acceptable amount (eg natural catastrophes, where a global reinsurance market exists). However, there is no widespread reinsurance market for the cover of airline insolvency; thus, current insurance capacity cannot support a compulsory insurance scheme⁶. More generally, required market preconditions (widespread reinsurance capacity, sufficient supply of insurance capacity, uniform risks, and variety of insurers - competition) do not exist for airline insolvency, as is the case on other markets where the Commission found compulsory insurance not working⁷. The EU insurance industry lacks the necessary insurance capacity to handle the demand that would result from a compulsory financial security scheme. Airline insolvencies can result in very large, complex losses larger than the financial capacity of some major EU insurers. Products like credit card protection and Scheduled Failure Airline Insurance (SAFI) function effectively because they are not compelled or restricted by EU legislation. Insurers can design cover best when they are able to freely contract with consumers and compete on price as well as scope of cover (CEA, IPP).

Travel agents disagreed with the dismissal of insurance and bank guarantee options on the basis that weaker airlines might not be able to obtain or afford those options. In the event that an airline is financially so weak that it could not cover the risk of its own failure, then it is not meeting financial fitness tests in any event. Travel agents stressed the issue of level playing field with tour operators. Tour operators which fail to provide insolvency protection are not allowed to offer and sell package travels. In this respect, they see no justification to allow airlines to sell tickets although their risk of insolvency and the damage for passengers is foreseeable. Travel agents also underlined that airlines have in recent years added to air tickets many additional fees, often at a 2 digit price, without encountering a significant loss of demand. In their view, it thus seems out of proportion to foresee that the inclusion in the air ticket price of a rather small amount covering insurance or a bank guarantee would create such disruption (ECTAA).

⁶ For instance, as multiple airlines can collapse due to an economic downturn, there could be at least 1 million passengers with an average claim of 1000 EUR, resulting in 1B EUR in total cover needed. This is larger than the market capitalisation than some of the largest EU insurers.

⁷ For cross-border healthcare, limited insurance options exist, as insurance is restricted to few insurers with a special background for handling claims in their field. The Commission concluded that the market was not strong enough to support the demands of a compulsory insurance system. With the environmental Liability Directive (ELD), the environmental liability insurance market is highly specialised and the take-up of such cover is not yet widespread. The Commission found insufficient justification for introducing compulsory insurance into the ELD at this time.

Consumer associations expressed major doubts as to the reasoning of insurance companies on the impossibility to oblige airlines to get an insurance against the insolvency risk. Why is it possible to insure packages that contain flights under the PTD and not airlines individually? (BEUC).

On compulsory Reserve fund

Airlines explained that general reserve funds would create new administrative burdens for the sector. They would lead to higher prices for all passengers while benefiting only a small number of customers. They would distort competition with non-EU carriers and would be unfair on financially viable airlines. It would also build up costs on a sector already badly hit by the financial crisis in 2008-2009, the volcano crisis in 2010 and future ETS-related measures (AEA). Regulation 1008/2008 requires airlines to offer this only as a conscious opt-in choice by the customer, many of which elect not to avail of it. It would be perverse to, on the one hand, insist that customers be able to exercise conscious choice over the purchase of such cover, while, on the other, considering imposing an across the board compulsory levy on the 600 million passengers a year, travelling from European airports, when the percentage, which might be exposed to the risk of airline failure, is decimal dust. The claim in the consultant's presentation to the workshop that a levy of the order of Euros 0.42 would have "no impact on the market" was strongly contested. The demand curve in the low cost business model - which accounts for 43% of intra-Europe point to point traffic - is extremely sensitive to reduction of demand for even the lowest increase in fare. Margins per passenger are extremely thin and, if it were possible to raise fares by 1 or 2 Euros with no effect on demand, airlines would already have done so (ELFAA). Financially "strong" airlines should not have to "pay" for financially "weak" airlines (ERA). IACA is categorically against a pan-European fund with ticket surcharge: this is unfair towards "healthy" airlines, and how to include all non-EU airlines in such scheme? Overprotection should not exist, and this is a disproportionate measure.

According to travel agents this solution would have the advantage of ensuring a level playing field between tour operators and airlines and of avoiding that consumers get confused about the protection attached to different types of products. They recommend for such a specific EU set of rules establishing a mandatory mechanism borne by air carriers to protect passengers against airline failure, of which the cost would be included in the ticket price. This protection mechanism should apply to EU carriers and to the farthest extent possible to non-EU carriers, for all tickets sold within the EU (ECTAA).

Consumers also agree with the consultant that a mandatory mechanism borne by air carriers to protect passengers against airline failure shall be set up, of which the cost would be included in the ticket price (BEUC, Which? Travel).

On Self regulation

Airline associations took different views on the matter. ELFAA's member airlines have, for some time, been voluntarily offering rescue fares to passengers, stranded as the result of the failure of another airline. As a minimum, these offer repatriation back to base for a nominal fare, for 2 weeks following the collapse of the original airline, subject to documentary evidence of a reservation with the airline concerned. In individual cases, ELFAA airlines have exceeded these minima. ELFAA pointed out that rescue fares at a nominal fee, if offered by all carriers, would enable the Commission and national regulators, via their website and help lines, to advise stranded passengers to contact whichever airline offered alternative services from the point, at

which they were stranded. While the burden on airlines would not be significant, as they would only accept such passengers if they had space, the reduction in stress for the passenger would be significant. IATA considered that it has no competence as to promoting such a solution since it concerned the commercial policy of its member airlines. AEA also mentioned that if such self-regulation were to happen, it should not be imposed. It would be up to the market to decide whether there is a need to act or not, and in the affirmative each company individually would decide the appropriate actions to take.

According to travel agents, the difference between the compulsory scheme applied to package travels and the absence of protection from airlines causes an unlevel playing field between tour operators and airlines. Tour operators which fail to provide insolvency protection are not allowed to offer and sell package travels. In this respect, travel agents see no justification to allow airlines to sell tickets although their risk of insolvency and the damage for passengers is foreseeable. In particular, options planning for no action or voluntary measures would maintain such a significant difference between extensive obligations born by tour operators and limited or voluntary measures for airlines (ECTAA).

Consumers associations firmly opposed such a self regulatory solution, which has proven inefficient in most cases in this sector. They do not see why some airlines associations are so opposed to regulation and so in favour of self regulation on the same subject while a regulatory option allows avoiding the free riding attitudes of some companies that are common in a self regulation context (BEUC, Which? Travel).

Other points

Travel agents also noted that the study has not considered the option of leaving each carrier to determine which form of protection best suits its business, subject to that protection delivering effective passenger protection. This approach has been used to implement the Package Travel Directive in some Member States. It would render void much of the alleged concerns about the options compulsory insurance and banks guarantees, to the extent that airlines that see a disadvantage in taking out insurance or a financial guarantee may opt for a reserve fund. Moreover, it would also render void the secondary concerns about the reserve funds' option that the passengers of well-established airlines may subsidise passengers of newer or less stable airlines, because well-established airlines could opt for a protection mechanism in the framework of which their status would provide them an advantage. (ECTAA)

Annex 1

List of participants

With **Steer Davies & Gleave** (Simon Smith) and under the Chairmanship of the European Commission, the attendees to the workshop have been:

Airline associations:

Association of European Airlines (AEA)

Athar Hussain Khan

International Air Transport Association (IATA)

Philippe Morin, Marco Alvarengo, Catherine Erkelens ou Leendert Creyf (Bird & Bird), Steve Huygens (British Airways)

European Low Fare Airlines Association (ELFAA)

John Hanlon

European Regions Airlines Association (ERAA)

Lorna Reader

International Air Carrier Association (IACA)

Koen Vermeir, René Maysokolua, Claude Perignon (TUI Travel PLC), Andrew V Cooper (Thomas Cook Group)

Consumer associations:

Bureau Européen des Unions de Consommateurs (BEUC)

Nuria Rodriguez

Which?GTravel

Rochelle Turner

Insurance companies:

European Insurance and Reinsurance Federation (CEA)

Kathrin Hoppe, Phil Bell

International Passenger Protection Ltd (IPP)

Michael Ward, Brian McLean, Paul McLean

Travel agents:

Group of National Travel Agents' and Tour Operators' Associations within the EU (ECTAA)

Michel de Blust, Isabelle Leroy