

INFORMATION NOTE

EU external aviation policy: why does the EU want to modify air service agreements between its member States and partner countries?

1. European Union aviation policy is developing rapidly. Within the EU, a genuine single aviation market has developed over the last decade. In this context, nationals of one EU Member State can invest in, establish and control airlines in any other EU Member State. Airlines in the EU are established and licensed under the same rules, and can operate any route within the EU. High standards are maintained and improved through common rules on key issues such as licensing, safety and security.
2. In November 2002, the European Court of Justice – equivalent to a supreme court in the EU context – found that if an Air Services Agreement (ASA) permits designation only of companies owned and controlled by nationals of the signatory EU Member State, such discrimination is in breach of EC law. As a result, every EU Member State is required to grant equal market access for routes to destinations outside the EU to any EU carrier with an establishment on its territory. ASAs between EU Member States and their bilateral partner States must be amended to reflect this position.
3. Until now, amendment of ASAs took place in the context of bilateral negotiations between an EU Member State and its partner State. While this approach remains valid, a simpler option has also been made available. The European Commission has been mandated by the Member States of the EU to conclude a "horizontal" Agreement, amending relevant provisions of all existing bilateral ASAs in the context of a single negotiation. Agreement has already been reached on these lines with a substantial number of partner States, with more to follow. This approach has the advantage of relative simplicity and speed.
4. It is important to understand that traffic rights – the provisions of existing ASAs relating to the number of airlines that may be designated and any frequency, capacity or other traffic right restrictions - remain unaffected by the proposed amendment. While the number of airlines which an EU Member State may consider for designation will increase, the number of airlines which can be

designated, provided that they are established, will remain subject to the provisions of existing bilateral Agreements. There will be no effect on the balance of air traffic rights, previously agreed between a partner State and an individual EU Member State, and existing bilateral Air Services Agreements will remain in force after amendment.

5. It is important, in the interest of both sides, that the problem is solved as soon as possible, and the risk of legal challenge to existing Agreements removed. Our aim is to eliminate the element of legal uncertainty, and to create a solid basis for the future development of our aviation relationship.
6. Attached for information purposes are the text of a model "horizontal" Agreement (MHA), and a short paper (FAQs), intended to answer possible questions which may arise on reading the text.

"Horizontal" agreement - FAQs

This text is intended to answer questions arising from examination of the text of the proposed model "horizontal" Agreement (MHA) between the EU and partner States. The Annex contains definitions of the most important terms used in the MHA.

1. At the ICAO Assembly in mid-2004, the EU presented a working paper on ownership and control and designation of air carriers.¹ What is the EU objective? If a partner State agrees to this kind of agreement, does it need to conduct additional bilateral negotiations with individual EU Member States? Is a partner State obliged to negotiate a "horizontal" agreement with the European Commission, rather than pursuing the familiar method of bilateral discussions with individual EU Member States?

REPLY:

The main purpose of the EU proposal is to bring all existing bilateral Air Service Agreements (ASAs) into line with European Community law, as defined by the European Court of Justice (ECJ).² The intention is to ensure legal certainty and the continued application of those Agreements.

In its ruling, the ECJ – equivalent to a supreme court in the EU context – found that if an ASA permits designation only of companies owned and controlled by nationals of the signatory EU Member State, such discrimination between EU economic operators is in breach of EC law.

Since the issue of non-discrimination between economic operators is one of the basic principles on which the EU Single Market is based, a solution needs to be found as a matter of urgency. Until this is done, any EU carrier may make a legal challenge to the continued application of such agreements; and such a challenge is

¹ 35th Session of the ICAO Assembly; Economic Commission, Agenda Item 27; document reference A35-WP/96; EC/17; 13/8/04

² ECJ Ruling of 5 November 2002 in cases C-466/98, C-467/98, C-468/98, C-469/98, C-471/98, C-472/98, C-475/98, and C-476/98 against the United Kingdom, Denmark, Sweden, Finland, Belgium, Luxembourg, Austria and Germany.

very likely to succeed. In such a case, the European Commission would find itself obliged to request the denunciation of the bilateral ASA in question.

The EU and its Member States are committed to finding a solution to this problem, in cooperation with partner States, so as to ensure legal certainty and the continued validity of existing bilateral ASAs.

There are two possible methods for amending existing ASAs.

The Model Horizontal Agreement, as provided to partner State authorities, represents one method, and the European Commission has already reached agreement on these lines with a number of partner States, with more to follow. This approach has the advantage of relative simplicity and speed. The MHA directly amends bilateral ASAs, and removes any need for additional negotiations with individual EU Member States.

Alternatively, a partner State can conduct individual bilateral negotiations with each EU Member State concerned, to amend each ASA separately.

It is important that the problem is solved as soon as possible, and the risk of legal challenge to existing Agreements removed.

2. The introductory section of the Model Horizontal Agreement (Recital 8) indicates that there is no intention to affect the balance of rights and obligations between EU air carriers and air carriers of the partner State. If the "Community designation" provision in the MHA replaces existing 'substantial ownership and effective control' clauses in existing ASAs, might air traffic rights for EU air carriers not be increased? Under the MHA, how would the overall balance of air traffic rights between EU Member States and partner States be maintained?

REPLY:

Air traffic rights between a partner State and an EU Member State are covered by existing bilateral Air Services Agreements, which will remain in force after amendment through the conclusion of a Model Horizontal Agreement. Unless EU Member States decide otherwise, future amendments to bilateral ASAs concerning

air traffic rights will be negotiated by each EU Member State, and not by the European Commission.

The provisions of existing ASAs relating to the number of airlines that may be designated and any frequency, capacity or other traffic right restrictions, would remain unaffected by the proposed amendment. While the number of airlines which an EU Member State may consider for designation will increase, the number of airlines which can be designated will remain subject to the provisions of existing agreements. There will be no effect on the balance of air traffic rights, previously agreed between a partner State and an individual EU Member State.

3. *In the Model Horizontal Agreement, Article 2.2.i uses the expression 'established'. Does this expression give European air carriers more flexibility than the 'principal place of business' (PPB) definition?*

REPLY:

As a consequence of the ECJ ruling, any EU carrier³ which can show that it is established in the territory of an EU Member State, must be able to exercise traffic rights from that State to a partner State, in the same manner and on the same terms as carriers which are "nationals" of the EU Member State in question.

The EU has defined establishment in the following terms:

"Establishment on the territory of a Member State implies the effective and real exercise of air transport activity through stable arrangements; the legal form of such an establishment, whether a branch or a subsidiary with a legal personality, should not be the determining factor in this respect. When an undertaking is established on the territory of several Member States, as defined by the Treaty, it should ensure, in order to avoid any circumvention of national law, that each of the establishments fulfils the obligations which may, in accordance with Community law, be imposed by the national law applicable to its activities."⁴

³ Cf. Council Regulation (EEC) No 2407/92 of 23 July 1992 on licensing of air carriers
Official Journal L 240, 24/08/1992 P. 0001 - 0007

⁴ Corrigendum to Regulation (EC) No 847/2004 of the European Parliament and of the Council of 29 April 2004 on the negotiation

Designation is possible only for EU carriers which are established in accordance with this definition. The intention is to allow an EU carrier, whose principal place of business is in EU Member State "A", to fly from the territory of EU Member State "B" within the limits of the bilateral ASA between EU Member State "B" and a partner State.

4. *The Model Horizontal Agreement (Article 2.3) states that the partner State "shall not discriminate between Community air carriers on the grounds of nationality." Might this provision give an EU air carrier additional traffic rights through multiple designation in another EU Member State, whereas the partner State would be limited to existing rights?*

REPLY:

The overall balance of traffic rights between an EU Member State and the partner State would remain unchanged. EU air carriers could exercise traffic rights from EU Member States other than their own, only in so far as such rights are at that time available and unused (i.e. in terms of frequency, capacity and designation).

Unused frequencies, where they exist, have been agreed in the context of agreements which, in principle, assume a balance of rights and obligations on each side. If one party to the agreement chooses not to exercise such rights, it does not abandon the possibility of doing so in future. Typically, such decisions are taken on commercial grounds, and a change in market conditions – such as a major increase in bilateral trade flows – may lead to greater interest on the part of carriers. Similarly, a decrease in economic activity may induce operators to reduce services.

While an EU air carrier could obtain designation in other EU Member States, it would not be able to exercise any traffic rights other than those already agreed by a partner State. In this context, the amendment of provisions on designation in bilateral ASAs cannot create additional air traffic rights for Community carriers.

and implementation of air service agreements between Member States and third countries (OJ L 157, 30.4.2004)

Official Journal L 195 , 02/06/2004 P. 0003 - 0006

5. Article 3.2 of the Model Horizontal Agreement seems to permit a parallel system for designation and for regulatory control (issuance of certificates and exercising safety oversight). Who has final responsibility for safety?

REPLY:

Safety is guaranteed in the European Union through common rules and intergovernmental cooperation. High standards of safety are ensured by a new body, the European Aviation Safety Agency (EASA), set up in 2002 to become the authority responsible for regulating and overseeing the safety of aircraft. The Commission will soon make proposals for the extension of the competences of EASA to also cover aircraft operations and flight crew licences. EASA also makes sure that maintenance organisations all over the world which repair European aircraft receive the appropriate certificates. In this way, EASA guarantees a high uniform level of civil aviation safety in Europe by regulating/overseeing certification and by gradually becoming responsible for a wide range of aviation safety matters. Certificates issued by EU Member States before EASA became operational remain valid, and EASA operates in close collaboration with national aviation authorities.

The Model Horizontal Agreement has two effects:

a) notwithstanding the obligations of the Chicago Convention, notably those stemming from its articles 32 and 33, the partner State will retain the right to inspect (carry out "ramp inspections" on) aircraft operated by the air carriers designated by an EU Member State even if safety oversight of such aircraft is exercised by another EU Member State;

b) both Parties agree to recognise certificates issued by their respective competent authorities, which in the case of the European Union may be EASA or the EU Member State aviation authority responsible for safety. For this reason, it is important for the partner State to be aware of the new distribution of responsibilities between EU Member States and EASA, as this falls within the scope of article 83bis of the Chicago Convention.

6. Does the proposed MHA affect aviation security?

REPLY

There is no direct effect. The EU has developed extensive legislation on aviation security in recent years, notably in relation to operations from European airports. Such legislation must be complied with by any operator, including partner State operators, if operating from airports in the EU.

7. Aviation fuel is exempted from taxation in bilateral air service agreements. What is the meaning of Article 4.2 of the Model Horizontal Agreement?

REPLY

This provision (Article 4.2) is included for the following reasons:

- (a) Article 6 of the EC Treaty states that environmental protection requirements must be integrated in the implementation of Community policies.**
- (b) Article 14(2) of Council Directive 2003/96/EC permits any two EU Member States to waive exemptions from fuel taxation on intra-EU flights between their territories.**

So far, no EU Member State has decided to exercise this option. It is important to ensure, however, that in the event that two EU Member States choose to apply taxation to aviation fuel on flights between their territories, these measures are applied to all carriers operating on these routes, including any partner State carriers operating on a fifth or seventh freedom basis on such routes.

In conclusion: the provision in the Model Horizontal Agreement is designed to deal with a possible future development within the Single Market, and has no specific relevance for partner State carriers. Only if a partner State carrier were to exercise fifth freedom rights between the two EU Member States concerned would the issue of fuel taxation arise, and then only if those EU Member States applied such taxation to EU carriers on the same route.

8. *In relation to Article 5, what is the European Community law regarding tariffs for carriage wholly within the European Community? Are there implications for partner State air carriers operating services within the European Community?*

REPLY

Relevant EU legislation stipulates that on intra-EU air routes “only Community air carriers shall be entitled to introduce new products or lower fares than the ones existing for identical products.”⁵ This means, for example, that partner State carriers cannot be price-leaders on air routes between two points wholly within the EU.

9. *What is the purpose of Article 6, concerning compatibility with competition rules?*

REPLY

Article 6 aims to prevent incompatibility of certain provisions of bilateral ASAs with the competition legislation of either party. In the case of the EU, provisions which require or encourage agreement between economic operators (on tariffs, capacity or other factors which may result in limitations on competition) are incompatible with European Community law.

10. *What is the relationship between the European Community and the list of European Free Trade Association (EFTA) States in Annex 3 (i.e. Iceland, Liechtenstein, Norway and Switzerland)? What impact would conclusion of a Model Horizontal Agreement between the EU and a partner State, have on relations between that partner State and EFTA States?*

REPLY

The Community and its Member States are prevented by international agreements concluded with the EFTA States⁶ from discriminating against EFTA interests in

⁵ Council Regulation (EEC) No 2409/92 of 23 July 1992 on fares and rates for air services; Article 1.3

⁶ For Norway, Iceland and Liechtenstein, the Agreement on the European Economic Area (1994); for Switzerland, the Agreement

case the latter acquire majority ownership and effective control of Community carriers. Air carriers licensed by an EFTA State do not, however, have similar rights. Thus, while an EU Member State cannot refuse to designate a carrier licensed by an EU Member State on the grounds that it is owned and controlled by EFTA State capital, it is not obliged to designate a carrier licensed by an EFTA State. Equally, a partner State would not be obliged to accept such designation.

Conclusion of a Model Horizontal Agreement has no impact on bilateral agreements between the partner State concerned and the EFTA States.

ANNEX: Definitions

“Member State” means any of the Member States of the European Community.

“Establishment of a Community air carrier on the territory of a Member State” implies the effective and real exercise of air transport activity through stable arrangements. The legal form of such an establishment, whether a branch or a subsidiary with legal personality, should not be the determining factor in this respect.

“Operating licence” means an authorisation granted by the Member State responsible to an undertaking, permitting it to carry out carriage by air of passengers, mail and/or cargo, as stated in the operating licence, for remuneration and/or hire.

“Air operator’s certificate” (AOC) means a document issued to an undertaking or a group of undertakings by the competent authorities which affirms that the operator in question has the professional ability and organisation to secure the safe operation of aircraft for the aviation activities specified in the certificate.

“Effective regulatory control” means, essentially, that: (i) the air carrier holds a valid Operating Licence issued by the competent authorities; (ii) the licensing Member State has and maintains aviation safety and security oversight programmes in compliance with ICAO standards at least; (iii) the air carrier meets the criteria for the operation of international air services established by the competent authorities. These criteria include: proof of financial fitness, ability to meet, where relevant, public interest requirement, obligations for assurance of service.