Aegean Airlines
Air France
Austrian Airlines
Air Dolomiti
Brussels Airlines
Croatia Airlines
KLM
Lufthansa German Airlines
Lufthansa Cargo
SAS Scandinavian Airlines
TAP Portugal

December 2020

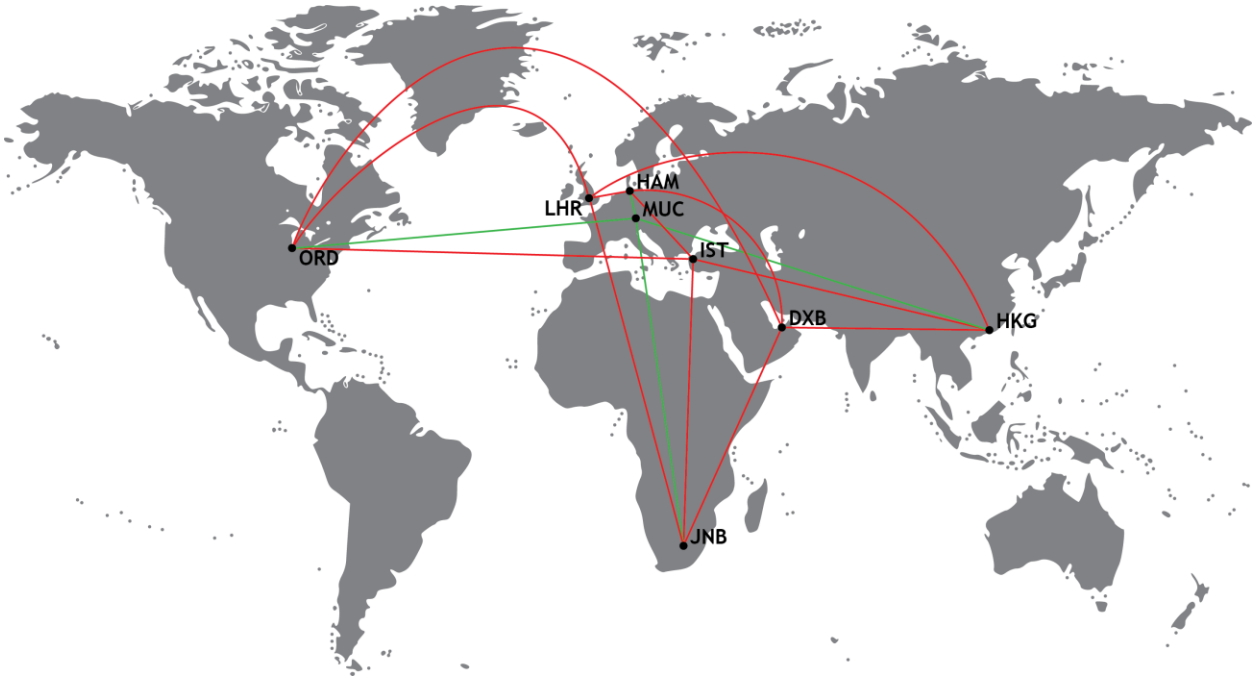
AIRLINE COORDINATION PLATFORM (ACP) POSITION PAPER ON THE GREENING OF EUROPEAN AVIATION – SAFEGUARDING A COMPETITIVE EUROPEAN AVIATION INDUSTRY

Aligning air traffic and climate protection is a common goal of society, politics and the aviation industry. The regulatory framework should pursue ambitious and binding targets for CO_2 reduction and at the same time ensure that European aviation, including value creation and employment, is not discriminated in international competition.

Given that aviation is a global business requiring global solutions also in terms of climate policy, regional regulatory pressure may sometimes be needed to make progress. To the extent that European legislation aims to lead regulatory changes reducing carbon emissions, it is necessary to keep in mind that such efforts could be counteracted by traffic and emission being shifted to hubs outside Europe ("carbon leakage"), and leading to increased CO_2 emissions. Such unintended consequences will continue even after the CO_2 compensation system for global aviation (CORSIA) of the International Civil Aviation Organisation (ICAO) enters into force in 2021,[1] as long as regional instruments, such as the EU Emissions Trading System (EU ETS), remain in place. The co-existence of both systems may even increase the distortive effect, as there is the risk of a double burden for Europe-based airlines. As a result of higher costs, EU airlines will no longer be able to compete with third country carriers and passengers will avoid using EU airlines and their hubs for intercontinental travel, taking a more-CO_2 intensive detour through non-EU hubs. Therefore, EU airlines and their hubs must not be disadvantaged in comparison to third country airlines.

[1] Participation to CORSIA will start as of 2021 on a voluntary basis.

Airline Coordination Platform | office@airlinecoordinationplatform.com | +32 474 845934
Legal domicile: Sint Canisiussingel 26, 6511 TJ Nijmegen, Netherlands



Financial competitive advantages for hubs outside of the European Economic Area (EEA) in many cases lead to longer flight routes, increasing CO_2 emissions. This is illustrated above by the example of intercontinental flight connections with start in Hamburg (HAM).

Compared to a transfer in Munich (MUC), the CO_2 emissions per passenger increase when travelling

to Hong Kong (HKG)

- by 8% when transferring in Dubai (DXB);
- by 0.5% in Istanbul (IST);
- by 9% in London (LHR);

to Johannesburg (JNB)

- by 20% when switching in Dubai (DXB);
- by 2% in Istanbul (IST),
- by 9% in London (LHR).

On the trip to Chicago (ORD), emissions increase by 96% when transferring in Dubai (DXB) and by 30% in Istanbul (IST). Only transferring in London (LHR) reduces the CO_2 emissions by 10%.

These examples show that well-intended measures to reduce CO_2 output can have the opposite effect in terms of CO_2 emissions and in addition can lead to a distortion of competition. To prevent these effects, ACP asks the Commission and EU Member States to consider the following issues:

Airline Coordination Platform | office@airlinecoordinationplatform.com | +32 474 845934
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1. The current EU ETS distorts international competition, both directly and indirectly

In order to achieve the CO_2 reduction target of the sectors covered by the EU ETS, the European Commission intends to address both the reduction of the total number of allowances (cap) and an increase of the auctioning share of allowances (reduced free allocation). Any increase of the target under the European Green Deal will reduce the number of allowances faster each year, thereby, significantly increasing the pressure on the EU ETS certificate prices. It is worth recalling that the intention of the free allowances in aviation was to address competitive disadvantages in relation to third countries.

The market-based approach to the reduction of CO_2 emissions is principally correct and efficient. However, the same conditions must apply to all global competitors. Only then will the EU ETS have its desired steering effect. At present, the EU ETS distorts competition in global aviation because its scope is limited to the European Economic Area (EEA). Airlines will have to buy CO_2 allowances for flights departing from and arriving at destinations in the EEA. This also affects intra-European feeder flights to European hubs. At these hubs, EU network airlines efficiently bundle their international long-haul traffic. The EU ETS thus creates a level playing field among hubs within the EEA.

On the other hand, flights which start in the EEA and end outside the EEA are excluded from the EU ETS. Accordingly, feeder flights to hubs outside the EEA enjoy a financial advantage. Due to their geographical proximity to the EEA, airlines and hubs in Turkey as well as the Near and Middle East in particular benefit from this unequal treatment. The EU ETS, therefore, tends to favour companies, which already have a cost advantage over their European competitors due to lower environmental, social and consumer protection standards. Once the Brexit transition period ends, hubs in the UK may also be excluded from the EU ETS.

However, the effects of the EU ETS are not limited to direct competition - the absolute cost burden is also affected. EU network airlines compete globally with network airlines from other continents, which are not subject to similar systems. The regionally limited EU ETS reduces the investment power of airlines needed to compete with intercontinental competitors.

Possible solutions:

- **Establish a Carbon Border Adjustment Mechanism (CBAM) for aviation**

  A Carbon Border Adjustment Mechanism is a method to reduce or eliminate the distortion of competition. For goods, a tax is usually levied as a compensatory mechanism. Ideally, this or a similar control principle could also be applied to airlines that operate from non-EU hubs but not subject to the ETS.

- **Alleviate financial burden on EU feeder flights within the EU**

  If the additional costs of the airlines imposed by the EU ETS are passed on to customers, they risk losing them to competitors not covered by the EU ETS. This would also have a direct impact on EU airport hubs that lose traffic to their non-European competitors. In order to avoid such a distortion of competition, intra-European feeder flights could be exempted from the EU ETS. Excluding feeder flights is within the EU's competence and could be achieved in the framework of the forthcoming revision of the EU ETS.

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Through free allocation of EU ETS allowances to individual airlines – dependent on the emissions of the individual EEA feeder shares – the distortion of competition could be effectively avoided with existing mechanisms. This approach is similar to the support measures for energy-intensive industries in case of carbon leakage (Art 10b of Directive 2003/87/EC).[2] For air transport, such a free allocation could be calculated, for example, on the basis of the emissions from feeder flights in the previous year.

Alternatively, models could be conceived whereby EEA airlines are reimbursed for the proportion of their feeder flights that contribute to the EU ETS. This reimbursement could be financed either from the revenues received from the EU ETS or a rebate on national taxes. Alternatively – although less favourable – the calculated sum could be distributed across all intra-EU point to point traffic. The total monetary volume of the EU ETS thus remains unchanged, while distortions of competition and carbon leakage are avoided at the same time.

- **Integrate environmental compliance in the EU comprehensive air transport agreements**

  In principle, air transport agreements allows for the integration of third country hubs into the EU ETS. EU comprehensive air transport agreements that have not yet been signed or pending bilateral agreements could be therefore amended accordingly. By doing so, flights by third country airlines feeding into their non-EEA hubs would be integrated into the EU ETS on a mandatory basis. For existing agreements, the Joint Committees could also work towards their subsequent inclusion in the EU ETS, although this could be an extremely difficult process.

  It is also of upmost importance that these issues are solved before the signature of any currently pending comprehensive air transport agreements (e.g. State of Qatar). Furthermore, current negotiations of comprehensive air transport agreements such as with the Sultanate of Oman and ASEAN, or initiating any new agreements should be reconsidered in light of these aspects.

2. Promote the use of Sustainable Aviation Fuels (SAFs) without distorting competition

The use of sustainable aviation fuels is generally considered as one of the most realistic and effective means to reduce aviation CO_2 emissions in the next decades. However, the problem lies in the fact that the current cost to produce SAFs is at least three times that of conventional jet fuel. Its price is also higher than that of sustainable alternative fuels used in other transport modes. As a result of these higher production costs and the currently limited supply, SAFs are, in the absence of an orchestrated support strategy, not an economically attractive substitute to conventional jet fuel.

A so-called blending mandate is currently being discussed as a means to boost production of SAFs. A blending mandate is the obligation to produce a certain amount of SAF or to purchase a certain amount of SAF to be blended with conventional fuels. However, given that the high price of SAFs remain, the blending mandates as currently being discussed would adversely impact the competitiveness of EU airlines.

A mandate that would only apply to flights within the EEA would put European airlines into a disadvantageous position, because feeder flights to international destinations would be encompassed, whilst flights to hubs outside the EU would not – a situation similar to the one described above regarding the EU ETS. If applied to all fuel uplifted in Europe, but not outside Europe, traffic connecting through an airport in the EU

[2] Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community.

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risks being diverted to hubs outside the EU (e.g. flying from the USA via London or Istanbul to India rather than via Paris or Munich).

From an ecological point of view, such a mandate, without a corresponding support mechanism, could have the unintended consequence of lowering sustainability standards as users seek to fulfil their obligations with the cheapest option available, e.g. by using HEFA (hydrotreated esters and fatty acids) or feedstock-based (e.g. palm oil) fuels instead of future-proof technologies such as lingo-cellulose feedstock fuels or synthetic fuels (e-fuels) produced from sustainable power sources and CO_2. It could also lead to an increase in the so-called tankering of fuel, a practice when air carriers (from outside the EU) carry the fuel for the return flight on board. They do so in order to avoid the higher costs for SAF at European airports with a blending mandate. More fuel on board also means that an aircraft is heavier and consumes more fuel. Consequently, this leads to unnecessary extra CO_2 emissions. These potential negative effects on the environment should be avoided.

Possible solutions:

- **Introduce mandates at global/ICAO level**

  The aviation industry is a global industry and therefore requires global solutions. European policymakers should support the development of a worldwide blending mandate if supply volumes from the right feedstock/raw materials have reached significant levels. This approach could be part of the global CORSIA scheme, ensuring that airlines do not suffer from competitive distortions as a result of regional mandates.

- **Counter-finance the price difference between SAFs and fossil fuels**

  In case of a blending mandate, the price difference between kerosene and SAF could be publicly financed, for example by using EU ETS auction revenues, part of the EU recovery funds or earmarking funds from existing taxes for this purpose. It is key to separate the financing mechanism for the mandate from the physical SAF because the financing mechanism can be designed to be neutral to competition.

- **In case of a blending mandate that applies to intra-EEA flights only, the EU should**
  - **introduce a carbon border adjustment mechanism** to tally out the distortive effects of the higher fuel price burden of EU airlines;
  - **exempt feeder flights** for passengers with a final destination outside the EEA;
  - **include feeder flights to non-EEA hub airports**, for example via air service agreements.

3. An EU kerosene tax will not reduce emissions – the opposite effect may occur

In the elaboration phase of the European Green Deal, an aviation fuel or kerosene tax has become part of the political conversation. Currently, countries around the globe do not tax aviation fuel for international flights and have included provisions in their bilateral air service agreements to this effect. EU comprehensive agreements follow the same exemptions. The rationale of this long-standing notion is simple: States know that levying a tax on international flights unilaterally will likely trigger retaliatory measures from other countries. For this reason, aviation infrastructure is not financed by taxation. Instead, it is a global practice that

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airlines and passengers are charged for the use of aviation infrastructure: Airport charges and air traffic control charges and in some cases levies for noise nuisances and house insulation costs.

An EU-level or national aviation kerosene tax would most likely not reduce CO_2 emissions and would probably even have the opposite effect:

- The funds would flow into the general national budget and would not be earmarked for climate/sustainability projects. Worse, it would withdraw funds from EU airlines that they need to invest in climate-friendly new aircraft and technology;
- It would create a competitive disadvantage for EU airlines compared to airlines with their main business in jurisdictions without such a tax. Long-haul transfer traffic could be diverted to hubs outside the EU in order to avoid the tax, often accepting longer and thus environmentally less advantageous routings.
- In order to avoid the fuel tax, airlines would increase tankering. As an example, with modern generation aircraft, this is possible from Istanbul (IST) or London (LON) to any destination in Europe and back. This results in flying with heavier aircraft leading to increased fuel burn and emissions, thus undermining the purpose of the measure;
- Contrary to popular opinion, it would likely not reduce the number of passengers (and by extension, flights), as the fierce competition in the aviation market - including from airlines with hubs outside the EU - would allow only a part of the cost to be passed through to ticket prices. This would have a negative impact on the profitability of certain routes, leading to a reduction of connectivity if such routes could no longer be served profitably.

Possible solution:

In order to achieve a steering effect, the EU should focus on carbon pricing measures such as the EU ETS or CORSIA.

4. To reduce short-haul flights, make rail a viable alternative

In the course of the discussion about environmental priorities, many have emphasised the importance of rail. There are also calls for short-haul flights to be banned by way of legislation. However, for feeder flights, this can lead not only to a non-proportionate competitive disadvantage for EU airlines and hubs, it can also be counterproductive.

From a sustainability point of view, if feeder flights into hubs are no longer possible and there is no adequate alternative, passengers will simply transfer at a different, more distant destination, possibly outside the EU. From an economic and connectivity point of view, reducing feeder flights to a specific airport without adequate alternative connection would impact the viability of long-haul flights of European carriers at this airport, as most EU hubs lack a sufficiently big catchment area to sustain a dense international network without feeder flights.

Possible solutions:

ACP supports a better integration of different transport modes in the EU and welcomes viable alternatives to the current system of efficient feeder flights that allow passengers to travel to and from overseas destinations from all parts of Europe.

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- Investment in rail should focus on making rail a viable alternative and natural choice of consumers, instead of taking the consumers' choice by way of legislation.
- Invest in adequate rail connections and infrastructure to the EU's hub airports, offering the same level of connectivity and seamless travel as with the air connections they aim to replace.
- Stop levying airlines and using the revenues to subsidise domestic state-operated rail transport.

5. Concluding remarks

As the association of the network carriers of the European Union, **ACP firmly supports the ambitions laid down in the European Green Deal and its objective to become climate neutral by 2050**. ACP is **committed to sensible environmental legislation**, a **better integration into a European transport network**, but most importantly **technological investments** in solutions that will shape the future of aviation. However, considering the particular international nature of the aviation industry, it is **essential that all measures are seen in a global context, and unilateral policy initiatives are avoided**. Policies and measures implementing the Green Deal for aviation should either be applied and enforced for all airlines serving the European market, compensated by third country airlines through a Carbon Border Adjustment Mechanism or by designing policies in such a way that distortive effects are eliminated. Connecting Europe with the world requires strong European network carriers with sustainable hubs in Europe. Such a comprehensive policy approach will be even more urgent in view of the unprecedented crisis the aviation industry is currently undergoing.

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