

# Airline Insolvency Review

Final Report



March 2019

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# Chair's Foreword



In his Budget Statement in November 2017, the Chancellor of the Exchequer announced the government's intention to commission a review of passenger protections in the event of an airline or travel company becoming insolvent. In January 2018, the Secretary of State for Transport announced the establishment of the Airline Insolvency Review, and appointed me as its independent Chair.

The Terms of Reference for the Review, published on 30 March 2018, are set out on page 6.

We published our Call for Evidence on 16 April 2018 and, following extensive engagement with stakeholders, published our Interim Report on 12 July 2018. Since then, we have worked with stakeholders, our consultants and our panel of experts to collect and analyse the evidence needed to enable us to develop our recommendations, including holding a number of workshops with stakeholders to explore the issues and options in depth.

In this Final Report, we set out the evidence we have collected, the analysis we have performed, the conclusions we have drawn, and our recommendations. We consider that, taken together, our recommendations would, if implemented, provide UK-originating air passengers with reasonable assurance that they will be appropriately protected in the event that

their carrier were to become insolvent in all but the most extreme cases. Equally, they should provide ministers with the confidence that, in all but the most exceptional circumstances, there would be no material detriment to passenger welfare requiring additional government intervention, unlike previous cases, such as Monarch Airlines in 2017, where the government of the day felt compelled to intervene.

There is currently a gap in the protections available to air passengers. Around 80% of UK-originating passengers benefit from some form of protection against financial loss should their chosen carrier become insolvent. However, only those who have bought their air tickets as part of a package covered by the ATOL scheme – around a quarter of the total – are fully protected when this leaves them stranded abroad. Passengers have told us that this is their greatest concern, and that they would be willing to pay more for their tickets to be sure they will be able to get home in a timely way, at little or no additional cost.

We have therefore focused our work on how best to secure repatriation for UK-originating passengers whose return flight was booked with an airline that becomes insolvent while they are abroad, avoiding material detriment to their welfare, and removing the need for government to intervene.

Over the past decade, the vast majority of airline failures have been small scale, affecting relatively small numbers of passengers and the Civil Aviation Authority's role has been limited. In contrast, in the rare cases where large scale failures have occurred, the CAA has been directed to put in place extensive and costly repatriation operations at public expense.

Our Terms of Reference tasked us to explore alternative ways to pay for such operations should the need arise. Necessarily, if the taxpayer is not to finance them, only the passenger can do so, one way or another. Moreover, a pool of capital will be needed to underwrite the associated costs and risks, and assure counterparties. These factors point to the need for the passenger to contribute in advance, which means the cost must be spread across, and therefore the protection afforded to, all passengers.

We are therefore proposing a comprehensive scheme to protect all UK-originating air passengers, with the associated costs met largely, if not wholly, by the private sector. We refer to this as the Flight Protection Scheme, which would be coordinated by the CAA, and backed by requiring each airline serving the UK market to provide suitable financial protection based on the estimated cost of repatriating its passengers. This would create a level playing field for all UK-originating passengers, providing reasonable assurance of repatriation protection whether or not they hold an ATOL Certificate. We also make recommendations to enhance protection relating to future bookings, and to put the ATOL scheme on a more commercial footing.

Our objective has been to make recommendations which are practicable, effectual, and affordable, and meet our understanding of the government's policy objectives, as set out in our Terms of Reference. We consider that the recommendations made in this report meet all these objectives so far as practicable. Their implementation will, however, give rise to some increase in costs, both in setting up and administering the new arrangements, and in financing the protection they will provide. We estimate that on average the new scheme would in total cost less than 50p for each passenger protected.

In accordance with the widely supported principle we adopted for the Review that the beneficiary should pay for protection, these additional costs will fall, directly or indirectly, on passengers. In part, this will reflect the explicit recognition of private costs that, under the current informal arrangements, are – in effect – subsidised by taxpayers. Overall, however, we do not expect them to have a measurable impact on supply and demand in the UK market for air travel.

In assessing our proposals, stakeholders will need to bear in mind that the efficacy of some of the measures will depend on their being implemented as a package. In particular, the CAA's ability to ensure passengers' reasonable expectations are met will be constrained if it does not have all the powers, people, tools and money it needs to be effective, or if its scope to use them is restricted. Similarly, the policy goal of minimising the need for official intervention by relying, to the greatest practicable extent, on the airlines themselves to deliver repatriation flights, will elude us if the insolvency law reforms we recommend are not made or used.

We said at the outset that we did not think there was a single, easy answer to the questions we have been asked to consider – no silver bullet, no one-size-fits-all solution. Our work has confirmed that this is the case. This should surprise no-one for if it were otherwise the issues would have been satisfactorily addressed before now. The changes we recommend represent an evolutionary, incremental approach with the aim of avoiding unnecessary disturbance. Some should be relatively uncontroversial and straightforward to implement and could be carried forward in isolation. In varying degree, the others extend the role of the state and carry greater implementation risk. We recognise ministers will therefore wish to weigh them carefully before deciding how to proceed.

In carrying out the Review, I have been most ably supported by a team of officials drawn from the Department for Transport and the Civil Aviation Authority. I wish to pay tribute to each and every one of them. Without exception, they have worked tirelessly, with great skill and commitment,

to complete the large, wide-ranging and complex programme of work that underpins our recommendations. I wish also to pay tribute to the members of our Expert Panel who have given generously of their time and expertise to advise and challenge us as we have pulled together the different strands of analysis and sought to draw conclusions in the crucial later stages of the Review. Last, but by no means least, I wish to pay tribute to the constructive engagement of all our stakeholders who have helped us find our way through the many complex and challenging issues by providing useful evidence and explanation, by presenting their particular perspectives clearly and cogently, and by challenging our thinking constructively. To all of these, I am most grateful.



**Peter Bucks**  
Chair of the Airline Insolvency Review

# Terms of Reference



The Airline Insolvency Review will assess consumer protection in the event of an airline or travel company failure.

It will consider both repatriation and refund protection and identify the market reforms necessary to ensure passengers are protected. This will include full consideration of options to allow airlines to wind down in an orderly fashion so that they are able to conduct and finance repatriation operations with minimal or no government intervention. The Review will also consider alternative models for the provision of refund protection, including through the travel insurance market.

The Review will be led by an independent chair, appointed by the Secretary of State for Transport and supported by a secretariat comprising of government officials and Civil Aviation Authority (CAA) staff, supported by professional advisers.

The Review will provide an initial report to the Secretary of State on potential options to tackle the immediate repatriation of passengers of an insolvent airline by summer 2018. The Review will produce a final report by the end of 2018 offering the Secretary of State recommendations on repatriation, refunds and on how the current financial protection arrangements for air-travel holidays can be put on a more commercial basis.

# The Review's Principles



## **The beneficiary pays for protection.**

Those who benefit ought to pay for their protection. This will require a careful balancing of the level of risk covered and the affordability of protection. The corollary of this principle is that the taxpayer's exposure should be minimised.

## **Efficient allocation of risk.**

The risks for passengers should be allocated to those best placed to manage and control them, whilst avoiding duplication where possible.

## **Minimisation of market distortions.**

Constraints on the competitiveness and size of the UK aviation market should be minimised and UK registered airlines should not be put at a competitive disadvantage vis-à-vis international competitors.

## **Simplicity for passengers.**

Passengers should understand the protection available and be able to identify which risks are covered, and to what level. In addition, passengers should be compensated in a timely and efficient manner: being brought home and compensated quickly.

## **Deliverability.**

Any one of our recommendations should be deliverable by government with minimal legal risk. In relation to consideration of financing options, this principle also considers the option's ability to provide liquidity to the coordinating body in a timely fashion to fund a repatriation operation.

# Executive summary



**1** When Monarch Airlines was placed into administration at 4am on 02 October 2017, over 110,000 passengers were overseas, and more than 300,000 bookings for future holidays were lost, affecting a further three quarters of a million people. In the wake of the administration, the government instructed the CAA to undertake a repatriation operation to bring home not only those passengers whose holidays were protected by the ATOL scheme, but all those overseas. The decision was taken because there were too few spare seats on other airlines flying the same routes as Monarch. If left to fend for themselves, many of Monarch's passengers would have had to wait days – or even weeks – to return to the UK, and face the unwelcome prospect of not being able to book somewhere to stay.

**2** Following the failure, the Chancellor of the Exchequer announced the creation of the Airline Insolvency Review. The Terms of Reference set out that the Review should consider both repatriation and refund protection to identify the market reforms necessary to ensure passengers are protected, and consider how to place existing financial protection (the ATOL scheme) on a more commercial basis.

**3** Airline insolvency is not something that most passengers consider when they book or take flights. Every year, people from the UK take some 70 million flights

abroad on business, on holiday or to visit friends and family. Most of these trips are short, on average around eight days.

**4** The vast majority of travellers are carried by a small number of airlines, with the top five having nearly 60% of the UK market, and 80% held by just 13 airlines. We have estimated that the likelihood of any of these top 13 airlines becoming insolvent in a given year is generally low (between 0.1% and 3% depending on the airline) but if it were to happen, large numbers of people would be affected.

**5** If their airline does fail, passengers in general face two main types of harm:

- 1.** Financial losses because they have paid for tickets that become worthless.
- 2.** Personal welfare losses if they are left stranded abroad (this could be delay and disruption, discomfort, anxiety and stress, and in some cases even health and employment problems).

**6** The scale of harm suffered by particular passengers will depend on their individual circumstances and may thus vary significantly from case to case.

**7** At present, protection for those who book airline tickets exists in a number of forms. They may book their flight as part of an ATOL-protected travel arrangement

(costing £2.50). They may book using a credit card and have bookings costing more than £100 protected by Section 75 of the Consumer Credit Act 1974. They may purchase travel insurance including protection against airline failure (around 50% of policies have such protection). Or they may book using another mechanism which provides a degree of non-statutory protection like the Visa and MasterCard charge-back arrangement or PayPal's Buyer Protection Scheme.

**8** Our analysis suggests that today, around 80% of passengers who book outbound flights from the UK have some form of protection against financial loss which, at the least, would enable them to recover the money they had paid for tickets that have become worthless because their airline has failed. However, only those 25% or so who have bought a travel product protected by the ATOL scheme are assured of being able to get home in a timely way at little or no extra cost.

**9** This leaves around 75% of passengers who would need to access and pay for alternative travel arrangements themselves

if they are left overseas when an airline collapses. This may involve substantial additional cost, delay and inconvenience. Some may simply be unable to do it at all because there are no practicable alternatives available, or they do not have the wherewithal to pay for them.

**10** The Review therefore concludes that for passengers to be protected in the event of airline failure, this gap should be addressed. This would create a level playing field for all passengers and provide the government and travelling public with confidence that arrangements are in place to protect passengers who otherwise face being stranded.

**11** We do not think a 'buyer beware' approach is sufficient to fill this gap. ABTA and the Air Travel Insolvency Protection Advisory Committee (ATIPAC) have both told us they had reached a similar conclusion. Despite many previous attempts to raise awareness of the risks of booking air travel without financial protection, consumer research shows that few travellers think about these risks when they book a flight or understand how they could protect themselves. Many



passengers end up unnecessarily paying for more than one form of protection; others have none at all. When asked, most said they would not expect to be stranded, but if it happened they would expect to be assisted, whether by the airline, their insurer, or the government.

**12** We recommend new arrangements be put in place to provide practicable, effectual and affordable protection for all UK originating air passengers facing stranding because the operator of their return flight has failed. At the same time the taxpayer will be shielded from picking up the costs by ensuring they are paid for by those who benefit from the protections.

**13** We refer to this as the Flight Protection Scheme, and make a number of recommendations as to how this could be put it in place.

**14** To be effective, we consider protection should cover all UK-originating passengers who hold a ticket for a return flight to the UK on an airline that fails while they are abroad. They should have the same reasonable expectation of being able to get home at little or no extra cost, and in a timely way, whether or not their ticket is part of an ATOL protected package.

**15** Under our proposals, the CAA would be given a formal responsibility to act as a Coordinating Body, and put in place arrangements to coordinate the response to the failure of any airline serving the UK market, whether based in the UK or elsewhere. The CAA's actions should be proportionate, coordinated, and efficient, with the aim of ensuring, so far as reasonably practicable in the circumstances, that all passengers who are stranded abroad by the failure can get home.

**16** To carry out this responsibility the CAA would require authority, capability, funding

and tools. It should also seek to agree collaborative arrangements with the authorities in other states which licence airlines who carry substantial numbers of UK-originating passengers.

**17** New arrangements should be put in place to finance the cost of protection, based on requiring all airlines serving the UK market to pay for financial protections to cover the estimated cost of repatriating their UK-originating passengers to the UK in the event of insolvency. To ensure universality, this should be made a condition of UK Air Operating Licences and Foreign Carrier Permits.

**18** As far as practicable, the cost of this protection should reflect each airline's risk of failure. We therefore recommend the major part of this cost should be met through requiring airlines to put up security through a financial instrument that can be relied on to pay out should they become insolvent. We recommend this should be supplemented by a small centrally-held fund to cover the remainder of each airline's exposure, establish reserves against future claims, and meet the Scheme's current expenditure. This could be funded by a small contribution from each airline.

**19** We present options for the constitution, governance and management of this fund in Chapter 8. In assessing these, and any other options identified, stakeholders should have regard to the sponsorship and accountability implications of each option, in addition to the cost, tax and classification impacts.

**20** We estimate that, on average, the overall cost of this protection would be less than 50p per UK originating passenger.

**21** The overall costs of the scheme could be reduced were other parties to



contribute where they also have an obligation to protect passengers. For example, through giving the CAA the ability to stand in the shoes of repatriated passengers with financial loss protection (e.g. provided through credit cards) and pursue claims in their stead.

**22** Delivering repatriation protection will require a number of improvements to the current legislative and regulatory arrangements for UK airlines:

- To ensure an insolvent airline can continue flight operations for a short period after entering administration so that passengers can be repatriated using the airline's own aircraft, people and systems. This will require primary legislation to introduce a Special Administration Regime for airlines.
- To enhance the CAA's ability to monitor and enforce airline licence compliance in relation to financial health.
- To require airlines to prepare and maintain plans that enable repatriation operations to be planned and executed quickly and efficiently.

● To enhance solvent airlines' provision of 'rescue fares' and other assistance to repatriate stranded passengers of an insolvent airline. This will help to keep overall costs of the flight protection scheme down, benefitting airlines and their passengers commensurately.

**23** If government choose to fully implement our recommendations, legislation will be required to give effect to several of our proposals, and a transition period may be necessary to allow airlines time to prepare. In the interim period, several of our recommendations could be implemented in isolation, with the benefit of reducing the cost of failures and improving passengers' experiences should they occur.

**24** Although existing financial protection provisions already enable a large majority of consumers to recover money lost if they are yet to take their outbound flight, we offer recommendations to improve awareness and uptake of insurance, credit card, and payment system based

protections. To improve passengers' experiences in the event they require the protection, we also make recommendations to ensure contract terms are fair and claims processes responsive and easy to navigate.

**25** As well as reviewing protections for passengers affected by airline and travel company insolvency generally, we were asked to consider how the current financial protections for air-travel holidays could be put on a more commercial footing. These are presently provided by the ATOL scheme, which is funded by a flat-rate levy of £2.50 per person charged on all package travel arrangements that include a flight and one or more other services.

**26** The levy proceeds are held in a trust fund and used to meet the cost of fulfilling packages when the organiser who sold the package becomes insolvent and is unable to do so. In recent years, the fund's annual costs have generally been less than its income, which has helped to grow the fund and ensure it has adequate resources for the foreseeable future. There are however, some events which could potentially expose the taxpayer to a liability, for example if a large ATOL holder were to fail in peak season.

**27** The ATOL scheme is governed by legislation that, among other things, reserves to the Secretary of State for Transport the power to determine the rate at which the levy is to be charged and to appoint and remove the Trustees. It also prohibits the sale of air travel products by any person who does not hold an Air Travel Organiser's Licence, unless they are exempt from the scheme. The requirement to pay the levy is part of the licence.

**28** As a result of these features, the Office for National Statistics (ONS) has classified

the Trust as a public body, meaning its financial statements (including contingent liabilities) must be consolidated in the whole-of-government accounts as the levy is classified as a tax (because it is a mandatory, unrequited charge). By putting the arrangements on a more commercial basis, the Trust may be reclassified as a private body and the levy no longer classified as a tax. This would have a beneficial effect on public expenditure.

**29** We have identified a number of relatively straightforward measures to achieve this, including separating the Trust from government so it has less ability to control it, introducing some variability into the levy, and offering ATOL holders the option of providing financial security to lower the cost of the levy.

**30** At a later stage, the government may wish to review the ATOL scheme in the light of any wider changes to flight protection or consumer uptake of financial protection, with a view to possibly making further changes to the ATOL arrangements if appropriate. In the longer term, it may make sense to combine the two schemes.

**31** Readers should note that given the nature of the Review and our task to make recommendations to government, we have not undertaken a formal options appraisal nor cost benefit analysis. Should government choose to take forward several of our recommendations, they will likely require further analysis.

**32** A summary of our recommendations can be found immediately after this Executive Summary on page 14. Chapter 1 of the report sets the scene for our work and how we have conducted the Review; Chapter 2 describes the current landscape for passengers travelling by air from the UK; Chapter 3 details the protection gaps in that landscape; Chapter 4 sets out

options for undertaking repatriation; Chapter 5 proposes improvements to existing repatriation mechanisms; Chapter 6 details changes needed to allow airlines to wind down in an orderly fashion; Chapter 7 analyses how much the proposed scheme would cost; and Chapter 8 proposes how to pay for it. Finally,

Chapter 9 details our recommendations relating to the ATOL scheme. Further information, evidence and analysis, alongside reports from the consultants who have advised us are contained in the annexes of this report (available online at <https://www.gov.uk/government/collections/airline-insolvency>).



# Recommendations



**1** The Airline Insolvency Review's recommendations are summarised below as a series of themes to help the reader understand our proposals at a high level. Some should be relatively straightforward to implement and could be carried forward in isolation. Others would be further reaching and more complicated to implement.

## Repatriation

**2** We recommend a formal repatriation protection scheme is put in place that is practicable, effectual and affordable. We refer to this as the Flight Protection Scheme.

**3** The Scheme should protect any air passenger whose journey began in the UK, and who has a ticket to return on an airline that becomes insolvent while they are already overseas. The protection would apply irrespective of how, or from whom, the ticket was purchased or paid for.

**4** To facilitate this, we recommend appointing the Civil Aviation Authority (CAA) as Coordinating Body, and giving it a duty to use its reasonable endeavours to see that passengers are repatriated to the UK, on the same day and to the same airport to which they expected to return. As in many cases the actual delivery of the repatriation will largely be performed by third-parties in the private sector, we also recommend the CAA develop agreements

to ensure they all work together effectively to develop and deliver a solution.

**5** In Chapters 5 and 6 we propose a series of recommendations to introduce and enhance the mechanisms that will be deployed to repatriate passengers, which we refer to as the repatriation toolkit. The CAA's assessment of which mechanism to adopt should be based on delivering repatriation in the most cost-effective manner based on the circumstances of the failure concerned.

### Self- and Assisted-Repatriation

**6** To improve the availability of rescue fares and enhance passengers' ability to claim them, we recommend:

**a.** The Coordinating Body hold bilateral talks with airlines to assess their appetite and ability to enhance the provision of rescue fares. When there is a chance of a failure, the Coordinating Body should, with appropriate confidentiality, engage airlines operating complementary routes to try to maximise availability of spare seats.

**b.** The Coordinating Body, airlines and airline representative bodies should work together to produce a single code of conduct for rescue fares, with the aim of drawing together existing voluntary arrangements into a cross-industry best practice document.

- c.** The Coordinating Body adopts an evolutionary approach to developing the current voluntary arrangements to introduce a single access point to rescue fare information.
- 7** If government chooses to implement the proposed Flight Protection Scheme in full, and passengers are charged, via their airlines, for protection, they would be able to reclaim the cost of replacement flights from the Scheme.

### Organised Charter

- 8** To enhance the Coordinating Body's ability to deploy Organised Charter operations where it is the most cost-effective mechanism to repatriate passengers, we recommend:
- a.** The Coordinating Body should continue to develop resilience by seeking to expand the number of airlines that may supply aircraft, including those with aircraft best suited to repatriation deployment.
  - b.** The CAA should ensure greater integrity in the data it is able to access prior to a failure so that it holds more accurate passenger number estimates. Enhancing this could be done alongside developing a system so passengers can confirm their repatriation flight.
  - c.** We recommend the Coordinating Body and industry work together to ensure flight operations management systems are up-to-date, well prepared and quick to mobilise ahead of any future need.

### Keep the Fleet Flying

- 9** Our review of the ability to keep the fleet of an insolvent airline flying suggests that it would be feasible for

UK airlines, but only if some significant challenges can be overcome. In contrast to a number of other jurisdictions around the world, the UK does not at present have all of the necessary mechanisms to enable airlines facing insolvency to wind down and repatriate their passengers in an orderly fashion even with the protection of formal insolvency proceedings. We believe that many of the challenges can be overcome with modifications to the following aspects of the current regime:

- a.** the development of a Special Administration Regime for airlines, which would enable an insolvent airline to continue to operate its fleet for a limited period to bring passengers who would otherwise be stranded home; and
  - b.** changes to the UK's aviation regulatory regime to allow airlines to operate in Administration, and to provide the CAA with greater oversight of airlines in distress and more tools to affect the outcome.
- 10** Each element of the repatriation toolkit could be used individually, or combined to improve the ability to react to failures of all sizes and complexities. In order to prepare the most effective approach, the Coordinating Body will need access to passenger data and statistics from airlines in financial distress.

- 11** The multinational nature of the aviation industry will make managing some failures far more challenging for the Coordinating Body. We recommend enhanced communication, cooperation and collaboration between the Coordinating Body and overseas authorities to improve the management of failures that span multiple jurisdictions.

## Civil Aviation Authority Powers

**12** Alongside recommendations focussed on the repatriation toolkit, we also recommend government works with the CAA to introduce a more complete regulatory toolkit, to allow it to manage a failure more effectively. We recommend the regulatory toolkit should include the following measures, entrenched in the UK Airline Operating Licence, which we consider would represent a proportionate response to the risks involved:

- a.** Annual certification to confirm financial fitness;
- b.** Development of repatriation plans and access to data as required;
- c.** A requirement for the Board of a UK airline to notify the CAA when there is a material adverse change in its financial situation; and
- d.** The ability to grant a temporary special purpose licence to enable an airline to conduct a repatriation operation, even where the airline does not have a future.

**13** These recommendations are discussed in more detail in Chapter 6.

## Paying for the Scheme

**14** To achieve effective protection, it is essential to put in place a way to pay to fly passengers home in the event of a failure. This will need to provide the Coordinating Body with swift access to funds to manage repatriation.

**15** We recommend that any mechanism to pay for the Scheme should be mandatory for UK originating passengers, practicable and apply no matter how a passenger books.

**16** We recommend a financing structure for the Scheme that would see the majority of costs met through requiring airlines to put up security that can be relied on to pay out on their failure. To cover the remainder of each airline's exposure, and provide an income stream from which to meet the Scheme's current expenditure and establish reserves against future claims, we recommend airlines also be charged a small, per passenger levy.

**17** We estimate the costs of both the security and levy together, once the Scheme is fully up-and-running, to average around 40p per passenger<sup>1</sup>. To capitalise the fund, an additional surcharge of 9p per passenger would be required for a five-year transition period.

**18** To avoid duplication of protection with existing schemes we recommend:

- a.** adopting the principle that no passenger who holds an ATOL Certificate should be taken into account when calculating an airline's contributions to the Flight Protection Scheme; and
- b.** where a passenger would have been entitled to recover a loss from a third party had the Scheme not paid for repatriation, the Scheme should have the right to seek to recover money from that third party up to the limit of the protected loss.

**19** Putting in place both the security and levy elements of the financing recommendations may require a transition period to allow the sector to adjust. We recommend that in setting this period, government balances the risk of increasing the burden on airlines too quickly against reducing government's exposure to failures during the interim period.

<sup>1</sup> This figure includes an estimate of the Scheme's administration costs, as well as the cost of repatriation protection

## Refunds

**20** There are a range of refund protections already available to passengers through credit cards, debit cards and other payment services. Passengers can also take further steps by booking an ATOL protected holiday or taking a travel insurance policy with supplier failure cover. We consider these provide an adequate level of protection for forward bookings and accordingly we do not consider there to be a strong case for setting up an additional layer of refund protection.

**21** However, we recommend that government should work with partners to help enhance existing refund protection and provide greater clarity. We propose:

- a. Increasing consumer awareness and uptake of refund protection.
- b. Minimising unnecessary duplication of protection.
- c. Helping passengers to make a claim swiftly and easily.

**22** Further details of our analysis and proposals relating to refunds can be found in Chapter 3.

## ATOL

**23** We have made a series of recommendations to increase commerciality in the current financial protection arrangements for air travel holidays (the ATOL scheme). These include changes to the nature of the Air Travel Trust (ATT), and the role of its Trustees; including:

- a. Changing the terms of the ATT Deed to reduce or remove the ability for the Secretary of State to exert control. The Trustees should be charged with stewardship of the Fund in the manner best calculated to deliver the protection required.

**b.** Changing the appointment process for Trustees of the ATT so the Secretary of State has no say over the appointment of any Trustee. We recommend that the CAA Board or an independent panel should appoint and hold Trustees to account.

**c.** Introducing greater independence to the Trust by ensuring at least some (if not all) Trustees are independent of the CAA.

**24** Trustees should also have the ability to adjust the rate of the ATOL Protection Contribution paid by businesses to increase flexibility. Any reforms to the way ATOL protection is paid for should do more to reflect the Trust's exposure and ensure financing is set at an appropriate level to meet predicted reasonable calls on the Trust's funds.

**25** Where insolvency risks cannot be met by the ATT or in the private insurance market, the government should consider charging the ATT at a commercial rate for the provision of any additional guarantee or insurance. This step will ensure commercial discipline within the Fund, and will reward taxpayers for any potential risk they insure.

**26** Where the CAA incurs costs to help it prepare for and manage both airline and ATOL holder failures, these should be assigned on a pro-rata basis between the two schemes to avoid cross-subsidy.

**27** Lastly, we recommend that should conditions arise where the government has the ability to review the protection the ATOL scheme provides in light of any wider changes to flight protection or consumer uptake of financial protection, it should do so. The objective should be to ensure the traveling public continue to benefit from adequate financial protection

at an affordable level, delivered within the private sector in a way that is simple for consumers to understand.

**28** Our recommendations in relation to enhancing the existing repatriation toolkit, improving information relating to refund protections, and increasing multinational collaboration are all low cost ways to improve the passenger experience should airlines fail. Those recommendations relating to enhancing the CAA's licencing powers would have larger direct and indirect costs for airlines and their passengers. Introducing a mechanism to keep the fleet of an insolvent airline flying could be done in isolation, but would require primary legislation, and could expose the taxpayer to potentially substantial costs unless a

mechanism were also put in place to transfer the financial burden to the private sector. The financing mechanism we propose would introduce some additional complexity and increase costs to a limited extent, and would have more significant impacts for some stakeholders. On the other hand, it would allow a protection scheme to be put in place which, in all but the most exceptional circumstances, would provide passengers with reasonable assurance that they will be repatriated in a timely way at little or no additional cost, and give ministers the confidence that no additional government intervention will be required. Our proposals relating to the ATOL scheme stand aside from those relating to airline insolvency, and could be introduced in isolation.



# 1. The Review's approach



**1.1** Following the failure of Monarch on 02 October 2017, the Chancellor of the Exchequer announced the Airline Insolvency Review, which commenced in early 2018. The Review would draw on lessons from the collapse of Monarch and consider both repatriation and refund protection to identify the market reforms necessary to ensure passengers are protected. This would include full consideration of options to allow airlines to wind down in an orderly fashion so they are able to conduct and finance repatriation operations with minimal or no government intervention.

## The Call for Evidence

**1.2** In April 2018, the Review published a Call for Evidence<sup>2</sup>, breaking down its Terms of Reference into three key questions:

- how to repatriate passengers in the immediate aftermath of an insolvency
- how to finance a system of passenger protection; and
- what reforms were necessary to the existing protection framework.

**1.3** In response to the Call for Evidence, we received 33 responses from a wide variety of individuals and organisations.

We published a summary of these responses alongside the Interim Report.

## The Interim Report

**1.4** In July 2018, the Review published its Interim Report<sup>3</sup>, setting out further detail on our emerging thinking, work programme and the approach we intended to take to answering the key questions we faced. In particular, the Interim Report described the mechanisms needed to organise and run a successful repatriation operation following any size of airline failure. Across each area of the Review's consideration, we have enhanced and solidified our thinking into concrete recommendations set out throughout this report.

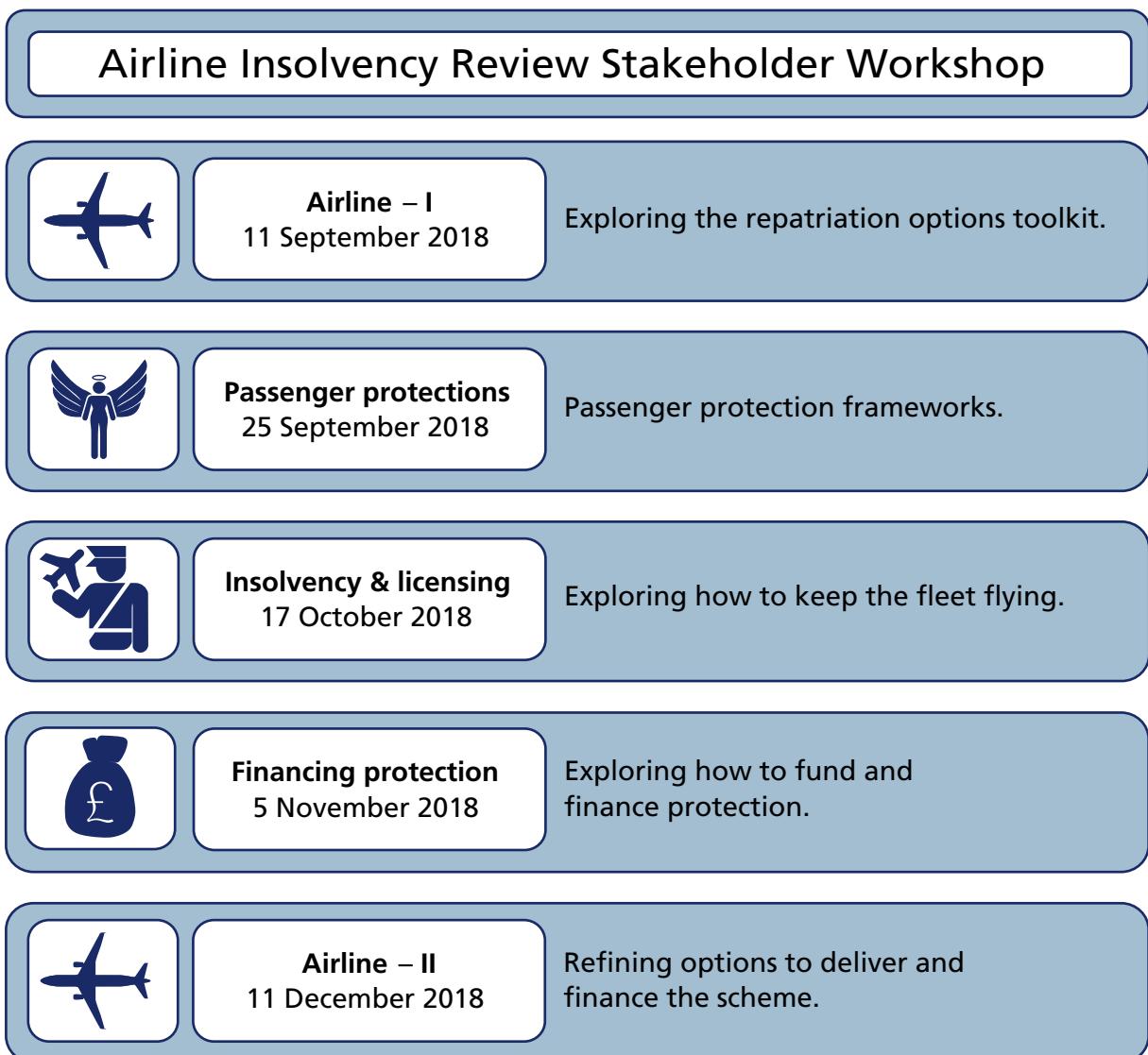
## Stakeholder Engagement

**1.5** Throughout the Review's lifecycle, the Chair and the Review team have met with interested parties to understand their views and the drivers and constraints within which they operate. Throughout late summer and autumn 2018, the Review organised a series of workshops with key stakeholder groups to discuss the key issues and questions raised by the Terms of Reference, as set out in Figure 1.1 overleaf.

2 <https://www.gov.uk/government/consultations/airline-insolvency-review-a-call-for-evidence>

3 <https://www.gov.uk/government/publications/air-insolvency-review-interim-report>

Figure 1.1: Stakeholder Workshop



**1.6** In addition, in early summer 2018, the Review organised two public evidence sessions in London and Manchester. The purpose of these sessions was to hear at first hand people's views of how the questions could be answered, engage in discussion on issues raised in the responses to the Call for Evidence and to offer anyone with an interest the opportunity to speak directly to the Chair and Review team.

**1.7** The CAA Consumer Panel made a series of recommendations in their 2018 Annual Report, to which we have had regard in developing this Final Report.

**1.8** The experience and knowledge shared through the processes described

above has helped shape our recommendations. A full list of stakeholders with whom we have engaged can be found at Annex B.

## Expert Advisory Panel

**1.9** Following publication of the Call for Evidence, the Review sought applications to join an Expert Advisory Panel to help the Chair and Review team to draw upon expert advice. The Panel comprises people with expertise relevant to the Review, including in the operation of airlines and travel companies, aviation regulations, insolvency and restructuring, and consumer protections.

**1.10** The Panel has assisted the Chair and Review team in accessing and interpreting evidence and helped us to maintain links with the external research community and other industry experts. It has also provided advice, reviewed our proposals and recommendations, and we have engaged in discussions on key policy issues. Panel members acted in their individual capacity and not as members of organisations in order to ensure their advice is impartial. Further information about the membership of the Expert Advisory Panel and its role in the Review is available from the Review's webpages (<https://www.gov.uk/government/collections/airline-insolvency>).

## Our principles

**1.11** When we published our Call for Evidence, we set out the principles detailed on page 7 which we expected to guide our thinking and help us to develop our recommendations. Throughout this report you will find reference to how consideration of them has helped us to arrive at our conclusions. In addition, we have adopted further criteria to help us select among the options for how to pay for a scheme.

## Analysis and consultancy inputs

**1.12** Alongside input from our many stakeholders, we also sought advice, analysis and research from a range of consultants – covering legal, financial, consumer research, aviation and economic expertise – and the Government Actuary's Department (GAD) to help develop the policy options and assess the potential impacts.

**1.13** These consultants included:

- **Ipsos MORI** were employed to undertake consumer research. We were interested to know the extent of consumer awareness of airline insolvencies and the existing levels of protection available. Ipsos MORI surveyed 3,669 adults. The survey was supplemented with seven focus groups, at which they explored in greater detail some of the behavioural factors motivating the survey responses. The results of the consumer research are summarised in Chapter 2, with Ipsos MORI's full report at Annex C.

339	“GENCHEN	2 1950
933	BERLIN-TEGEL	2 1950
8260	FRANKFURT	2 2000
5525	BUDAPEST	2 2005
1508	PARIS-CDG	2 2010
3248	ISTANBUL	2 2040
939	HURGHADA	2 0205
	IZMTR	1 0320

- **Government Actuary's Department (GAD)** were responsible for analysing the cost implications of financial options. GAD undertook Monte Carlo analysis to examine the likely losses associated with insolvency events and assess the cost of the different financial options: the analysis was underpinned by the meta-dataset provided by ICF. The costings produced by GAD were a key input to the ICF competition analysis. GAD's report can be found at Annex D.
- **ICF** were tasked with developing a single, comprehensive meta-dataset for the GAD financial modelling. They drew on a number of statistical sources, such as the Office of National Statistics (ONS) International Passenger Survey and CAA Airport Data. The resulting meta-dataset contained a range of information, such as estimates of the number of passengers who would need to be repatriated were an airline to become insolvent, and the probability of this occurring. In addition, ICF assessed the competition impacts of the financial options. ICF's report can be found at Annex E.
- **STEER** were employed to advise on the regulatory and legislative changes required to allow for an orderly wind down of an airline. In addition to this, Steer were tasked with developing financial options to fund a repatriation exercise. This latter task relied on analysis provided by GAD and ICF. Steer's report can be found at Annex E.
- **DLA Piper** and **Reed Smith** both provided legal advice to support our consideration of policy options.



## 2. The current airline insolvency landscape



### The risks, cost and impacts of the current system

**2.1** The UK aviation market is the fourth largest in the world<sup>4</sup> with 284 million passengers<sup>5</sup> passing through UK airports in 2017.

**2.2** Notwithstanding the Monarch failure in 2017, airline insolvencies are rare and the overwhelming majority of passengers are not affected. In 2018, the failures of Cobalt Air, Primera, FlyVLM and SkyWorks combined left over 12,000 UK-originating passengers stranded.

**2.3** Since publication of our Interim Report, we have refined our estimate of the likelihood of an airline insolvency and the number of affected passengers. Our latest analysis of the top 17 airlines<sup>6</sup> serving the UK suggests a 13% chance of an insolvency event within the next year. For all airlines serving the UK we would expect an average of 14,000 passengers to need repatriation each year<sup>7</sup>. This compares to an historic annual average of

19,500 passengers who required repatriation in the period 2008 to 2018<sup>8,9</sup>.

**2.4** Whilst these yearly average numbers are relatively small, particularly in comparison to the overall number of passengers who fly each year, it bears repeating that major insolvency events are rare but, when they do occur, the numbers affected are much greater than the annual average.

**2.5** As seen in Figure 2.1 overleaf, between 2008 and 2018, there were two UK airline insolvencies (XL Airways in 2008 and Monarch Airlines in 2018) for which the number of passengers requiring repatriation was several times greater than the annual average for the period. In addition, there were several years in which no significant airline failure affected UK passengers.

**2.6** The Interim Report highlighted there are a number of existing schemes to protect passengers against airline insolvency – see Figure 2.2 (on page 26-7).

4 Table 5, Presentation of 2017 air transport statistical results, ICAO

5 ONS: Table AVI0101 (<https://www.gov.uk/government/statistical-data-sets/aviation-statistics-data-tables-avi#avi-traffic-at-uk-airports-avi01>)

6 Consistent with the airlines analysed in our Interim Report

7 GAD (2018) Airline Insolvency Review – Risk Analysis Phase 2 – See Annex D

8 ICF (2018) Airline Insolvency Review – Aviation Data and Economics – See Annex E

9 To estimate the historic annual average number of passengers needing repatriation we replicated SDG analysis for the EC, which investigated airline insolvencies over an eleven year period from 2000 to 2010. European Commission (2011), 'Impact assessment of passenger protection in the event of airline insolvency'

[https://ec.europa.eu/transport/sites/transport/files/themes/passengers/studies/doc/2011\\_03\\_passenger-rights-airline-insolvency.pdf](https://ec.europa.eu/transport/sites/transport/files/themes/passengers/studies/doc/2011_03_passenger-rights-airline-insolvency.pdf)



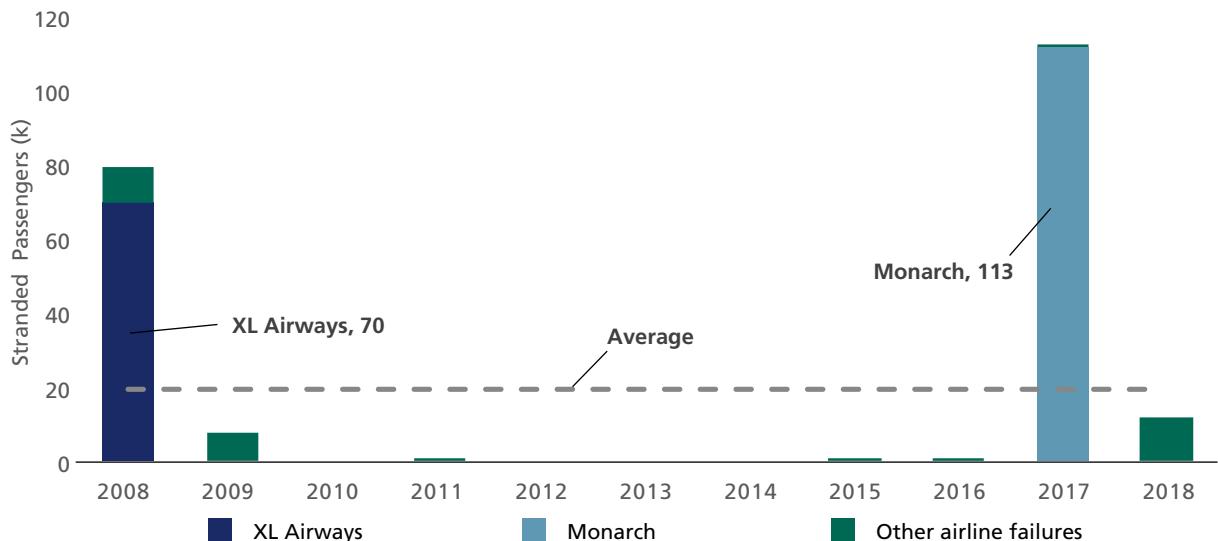
Access to protection is often determined by how passengers booked their tickets, such as by card, through an agent, or as part of a package holiday.

**2.7** As a result, passengers may unwittingly have several forms of protection. For example, if they booked a flight costing more than £100 and paid with a credit card, they would have protection under the Consumer Credit Act 1974. If they also purchased travel insurance with airline or supplier failure

protection, they would consequently have two forms of protection. As a result, it may not be clear which scheme is responsible for providing compensation in the first instance. We make recommendations on enhancing clarity in Chapter 3.

**2.8** With the exception of the ATOL scheme, none of these mechanisms offer passengers protection against all potential impacts arising from an airline insolvency. For example, debit card

**Figure 2.1: Passengers Requiring Repatriation, 2008-2018**



Source ICF (2019) Annex E

charge-back only reimburses passengers the original cost of the flight, which may be significantly less than a replacement flight. So, even where passengers are protected, it may not fully cover their losses.

**2.9** The airline industry has voluntary arrangements in the form of “rescue fares” to help passengers whose airline has failed by offering flights at a reduced price on other carriers.

**2.10** Whilst rescue fares are potentially a cost-effective means to repatriate passengers, provision and pricing is at the commercial discretion of individual airlines and subject to availability. This creates uncertainty as there is no industry

benchmark for what would be regarded as “the right price” for these seats.

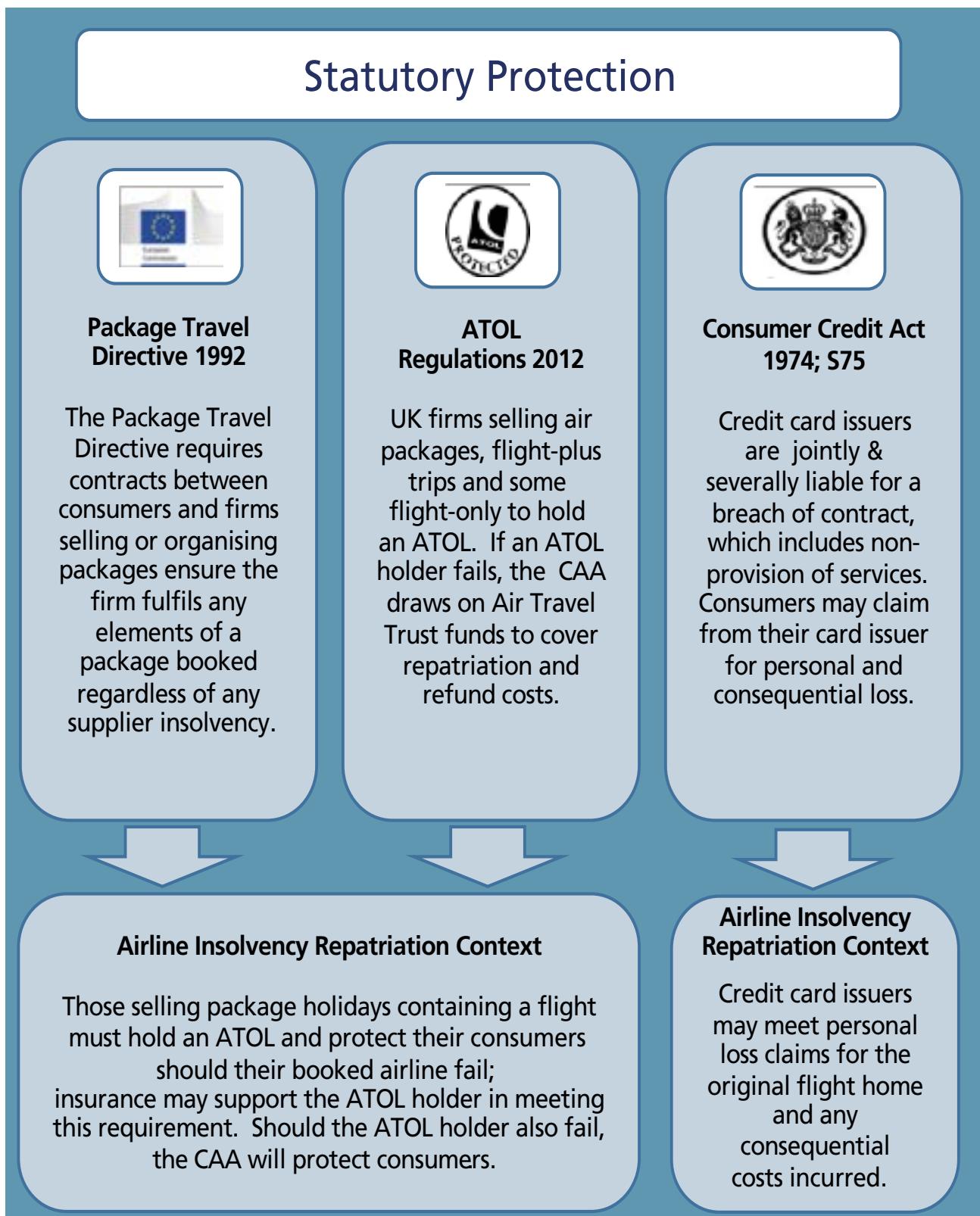
**2.11** As set out in the Interim Report, how effectively scheduled flights repatriate passengers in a timely manner will depend upon two principal factors:

1. The insolvent airline’s market share on the routes it served; and
2. The number of spare seats of competitor airlines on those routes.

**2.12** Both factors may vary throughout the year; this is particularly true of holiday destinations. Moreover, the ability of people to access and book a flight home for themselves may be limited by their personal circumstances.



Figure 2.2: Passengers Protection Landscape



## Non-Statutory Protection



### International Air Transport Association

IATA's Billing and Settlement plan (BSP) may allow travel agents to recover customer monies that have not been over to airlines.

IATA has a voluntary commitment to offer "rescue fares" where airlines are able.



### Insurance

Around 50% of travel insurance policies provide cover for scheduled airline or supplier failure.

Refunds and other compensation may be limited by policy conditions, and cover may be withdrawn.



### Charge-back

Under the Debit and Credit Card Charge-back scheme rules consumers may ask their card issuer to reverse a disputed transaction, which can include the non-provision of services.

### Airline Insolvency Repatriation Context

Subject to an airline's IATA membership, some monies may be available to some consumers. Airlines may assist consumers with rescue fares, subject to availability.

### Airline Insolvency Repatriation Context

Subject to insurance policy conditions, consumers may claim some or all of their costs.

### Airline Insolvency Repatriation Context

Debit card issuers may meet personal loss claims for the original flight, but not consequential costs incurred.

## International industry

**2.13** Aviation is, by its very nature, an international industry. As a result, regulatory oversight is multi-jurisdictional and often complex. Consumers may not always understand which national authority is responsible for regulating the airline with which they choose to book.

## Regulatory options

**2.14** This complexity has an impact not only on consumer understanding, but also on how far authorities are able to manage insolvency situations. Figure 2.3 below sets out the different type of regulatory relationship that airlines operating in the UK may have:

### Type A

**2.15** Airlines which are wholly licensed and regulated in the UK and whose passengers predominantly originate from the UK, e.g. Virgin Atlantic.

### Type B

**2.16** Airlines whose group is made up of several different airlines regulated in different countries, but where each of the airlines predominantly carries passengers originating in the country in which it is licensed, e.g. in IAG, British Airways (predominantly UK), Iberia (predominantly Spanish).

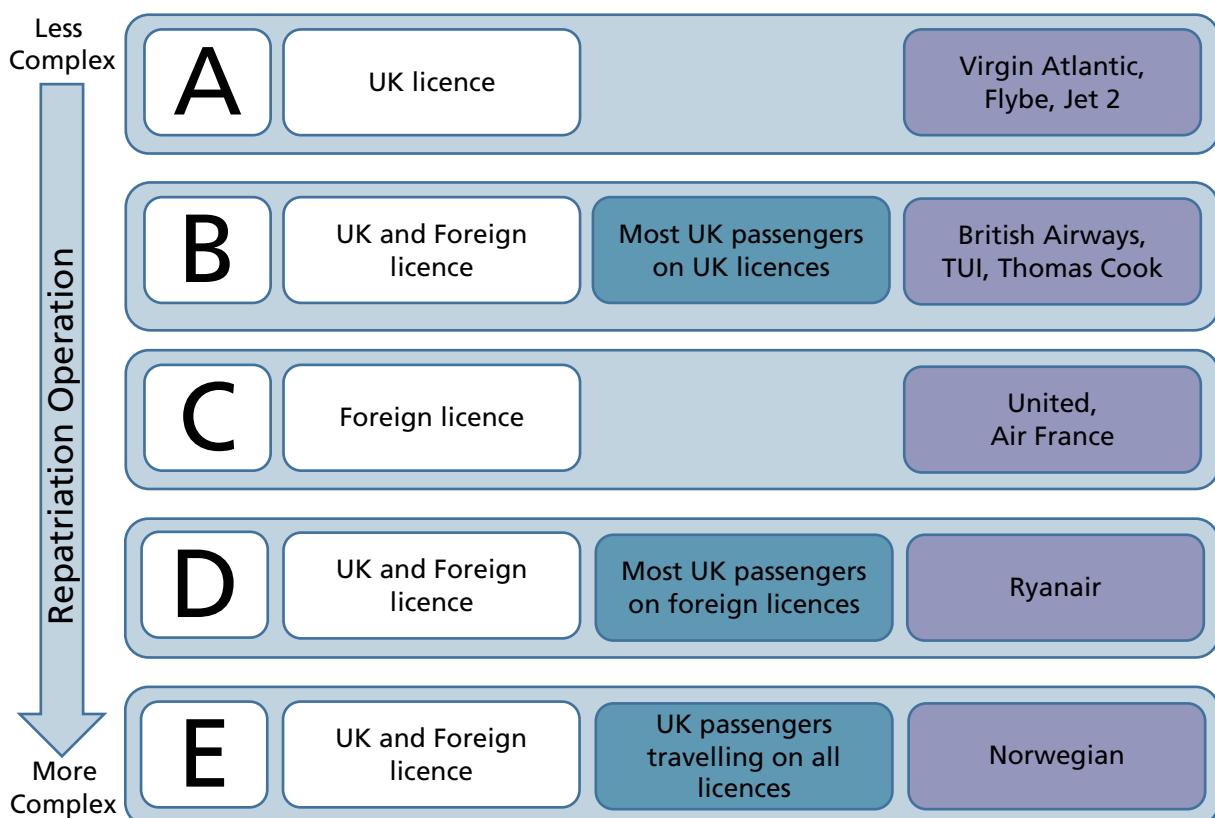
### Type C

**2.17** Airlines which are wholly regulated in another country operating some services to the UK with some passengers originating in the UK, but making up a small proportion of their total passengers, e.g. United (USA).

### Type D

**2.18** Airlines which are wholly regulated in another country whose proportion of passengers that originate in the UK is larger than those that originate in the country where it is regulated, e.g. Ryanair.

Figure 2.3: Airline Operating Types



## Type E

**2.19** Airlines in a group structure comprising several different airlines regulated in different countries where there is little or no relationship between the country where the airline is licensed and passengers originating in the UK. This means that passengers originating in the UK could be carried on any one of several airlines within a group, with little or no way of knowing which, e.g. Norwegian.

## Managing multinational failures

**2.20** With airlines in Type A and B, regulatory jurisdiction coincides with the country of origin of most of their passengers. As such the relevant state should be well placed to manage any potential risk of insolvency and plan for repatriation.

**2.21** With airlines in Type B, where the subsidiary of a UK licensed airline is regulated by another state, cooperation between states will be required to develop a clear understanding of each airline's available resources, and how each state intends to undertake and pay for repatriation operations.

**2.22** In Type C, passengers originating in the UK are likely to be only a small proportion of the total number of passengers flying with the airline. As such the market is likely to have sufficient capacity to manage repatriation flows back to the UK in many but not necessarily all cases.

**2.23** With Type D and E, the state whose residents would be most impacted may have little notice of potential insolvency as it lacks regulatory oversight. Consequently, there would be limited time and ability to react in a meaningful way to protect its residents and would be reliant largely, if

not wholly, on the actions of the failed airline's home country. In these examples, repatriation could only be undertaken with strong cooperation between states.

## Passenger views and understanding of insolvency protection

**2.24** One of the Review's core principles is that our recommendations provide simplicity for passengers. We consider it is important passengers should be able to understand the protection available and identify which risks are covered, and to what level.

**2.25** It was important to the Review that alongside significant stakeholder engagement and input, we also heard directly from those who would be protected by our recommendations. Alongside two public evidence sessions, we have also sought detailed views from the travelling public.

**2.26** In the Interim Report, we suggested the existing landscape is complex, with a number of different mechanisms available to protect passengers from an airline's insolvency. This could include ATOL protection, credit card protection, debit card charge-back protection and supplier failure cover in travel insurance. The Interim Report indicated that these protections do not apply to all passengers and may not be clear. This can lead to gaps where some are not protected, as well as overlaps, where some are covered by multiple products.

**2.27** Our Call for Evidence provided views on passenger understanding of the issue but little evidence of the depth of their knowledge. Some stakeholders contend that passengers are aware of the risks when booking, and can take out existing protections if they wish. Others say that

consumer awareness is poor, and new protection is needed to fill gaps.

## Investigating consumer views on insolvency protection

**2.28** A key task of the Review following the Interim Report, has been to improve our understanding of consumer views on insolvency protection. In particular, their awareness and take-up of existing protections, their appetite for additional protection and the price they would be prepared to pay.

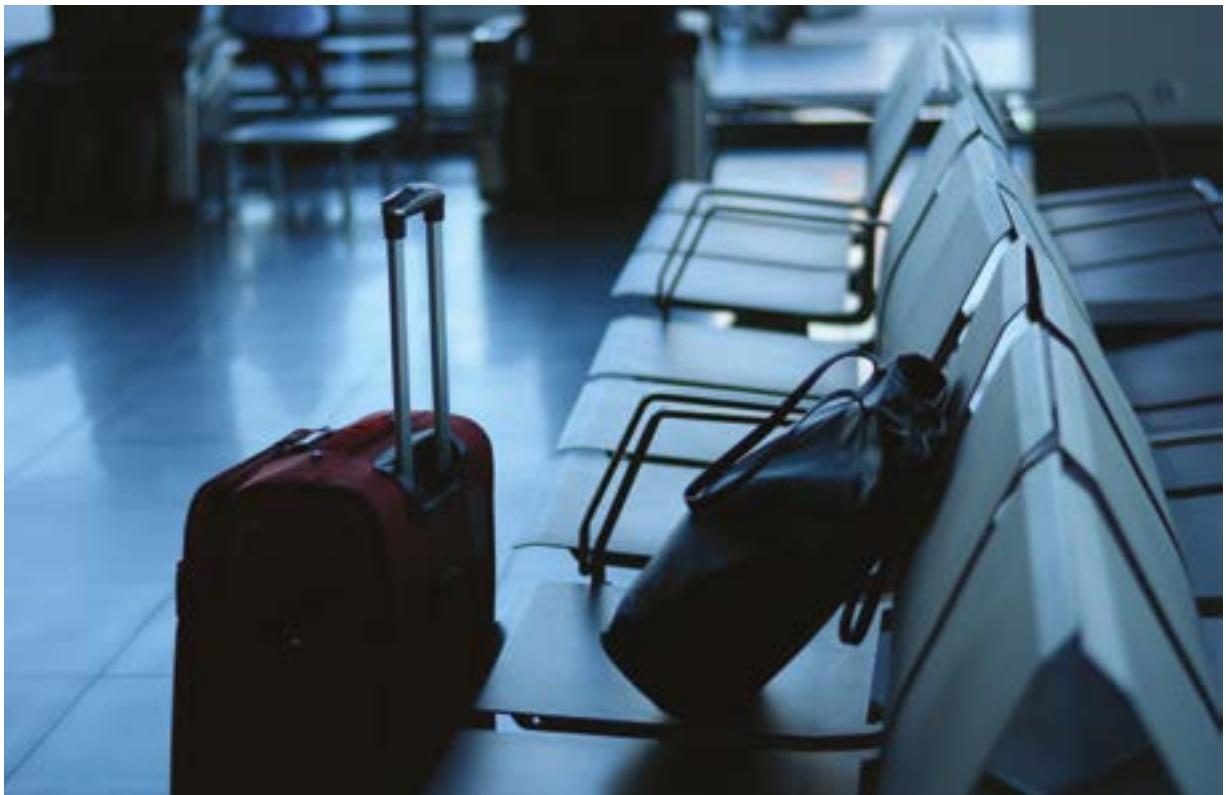
**2.29** We explored this through consumer research conducted by Ipsos MORI as part of the Department for Transport's wider research undertaken for the Aviation Strategy. This involved five face-to-face focus groups, two online focus groups and a nationally representative online survey of 3,669 people across the UK.

**2.30** The focus groups involved face-to-face sessions in Birmingham, London and

Manchester. Participants of mixed age and gender were recruited based on the frequency with which they fly (frequent and non-frequent flyers) and whether they mainly flew long-haul or short-haul. The two online focus groups included only business travellers, recruited from London, Edinburgh, Birmingham and Manchester. Throughout the chapter below we have drawn quotes from the focus groups highlighting particular insights.

**2.31** The survey comprised responses from 3,669 adults, though on some questions the base sizes were lower. The quantitative data in this report is based on all participants completing the survey who have flown in the last three years (a sample size of 2,028), unless otherwise stated. To ensure the results are nationally representative, the sample has been weighted by Ipsos MORI by location, age, gender and social class.

**2.32** The full report relating to insolvency protection from Ipsos MORI can be found at Annex C.



## Key findings from the consumer research

### Awareness and understanding of airline insolvency

**2.33** More people are flying than ever before, sometimes paying considerable sums of money months in advance of travel. We wanted to explore whether people consider the risks to which they may be exposed from an airline insolvency when booking a flight.

**2.34** The focus group discussions suggested airline insolvency is not something that participants understood in detail. Knowledge about airline insolvency ranged from not understanding the concept through to personal experience of being affected by the collapse of an airline. Those who had not considered the prospect of airline insolvency before were confused by it. They assumed they would automatically be covered by travel insurance and, learning that the collapse of an airline could leave them stranded, were surprised.

*"I'd rely on my travel insurance, it's not an act of God, it's a travel problem ... I'm going to look at my travel insurance now!"*

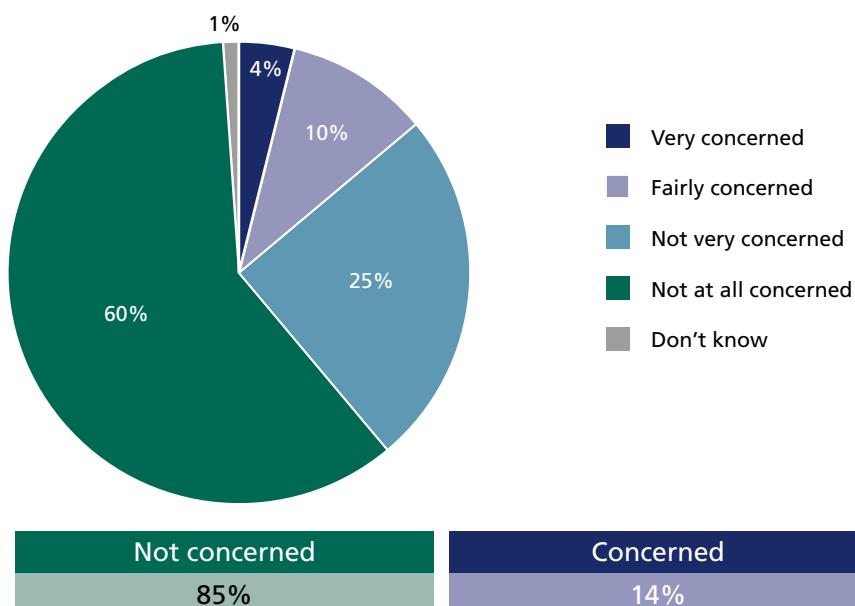
*London, frequent flyer*

**2.35** Most of the respondents (85%) said they had not been concerned about their airline becoming insolvent when they last booked a flight. This perhaps reflects the broad lack of awareness apparent in the focus groups – if there is little or no awareness of the issue, people have little to be concerned about.

**2.36** While there was little immediate concern in the focus groups, reactions to airline insolvency became more negative once participants had time to consider the implications of the situation. They differentiated between being stuck in a foreign country trying to return home, and finding out their airline had become insolvent before leaving on the outbound leg of their journey. The thought of being “stranded” in a foreign country was a particular concern, which they imagined would be distressing.

**Figure 2.4: Fear of Insolvency**

Thinking about the last time you booked a flight, how concerned, if at all, were you that your airline might go out of business before you were able to take a flight?



*"If you're stuck there you expect to be brought home. Maybe if it was the start of your journey that would be different, but here you've already entered the physical bit."*

*London, frequent flyer*

**2.37** Participants doubted an airline would become insolvent while passengers were waiting at an airport to board their flight. They assumed solutions would be in place to protect them if an airline did suddenly become insolvent leaving people stranded.

*"It's still the carrier. They have a legal responsibility. I know they [the airline] don't exist, but they should be able to book through a different airline."*

*London, frequent flyer*

## Responsibility for providing protection

**2.38** In the focus groups, those who took out travel insurance assumed that they would be covered for airline insolvency. Yet they acknowledged that they did not always take out travel insurance, and they were unsure how it would protect against airline insolvency.

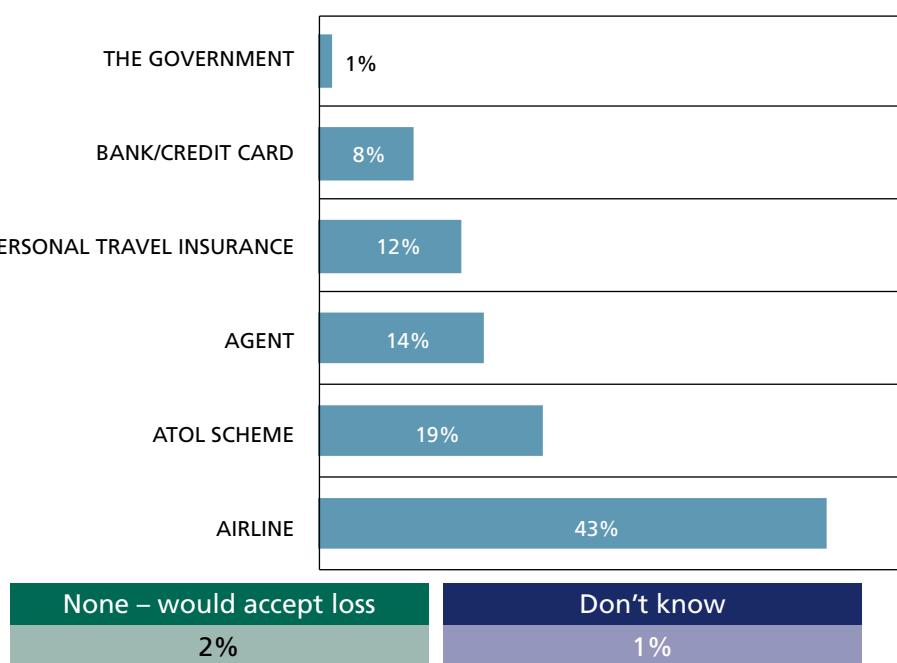
*"I fly without insurance all the time, you just forget. I've bought it a handful of times but not if you're just popping over to Europe for a couple of days."*

*London, frequent flyer*

**2.39** Participants also felt the insolvent airline should be most responsible for getting them home (even if they are no longer trading). Some suggested they would turn to the government as a last resort, if they were unable to return home.

**Figure 2.5: Responsible Organisation**

If your airline went out of business before you took your flight, from which one of the following do you believe should be most responsible for ensuring you receive a refund or replacement flight?



Source Ipsos MORI (2019) Annex C

*"You expect for something to be in place for when this happens."*

Birmingham

**2.40** In the survey, respondents were asked: who should be most responsible for ensuring a refund or replacement flight when an airline went out of business. The greatest proportion of participants (43%) indicated that the airline should be most responsible in this situation. Smaller numbers felt that the ATOL scheme, the agent, travel insurance or the bank or credit card used to make the booking should be responsible. Only 1% said they think the government is most responsible, and just 2% that they would be content to accept the loss and not expect any refund or replacement flight.

**2.41** Those who have booked a package holiday in the last three years are more likely than average to hold the ATOL scheme or the agent they booked with responsible (29% and 17% respectively).

Those who have not booked such a package are more likely than average to hold the airline (48%), their travel insurance (14%), or their bank or credit card (9%) responsible.

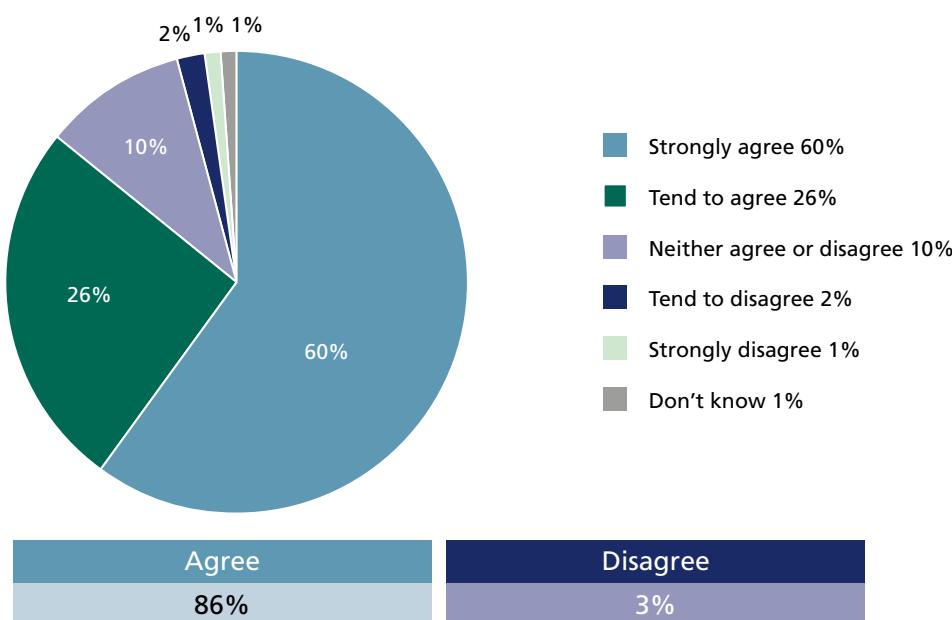
### Appetite for additional protection

**2.42** Participants in the focus groups perceived it would be necessary to purchase a replacement flight if stranded, however they felt aggrieved if they had to pay for it themselves and worried about the cost. Some said they would consider using a credit card if they had access to one, however others would not consider buying a new ticket themselves, as they did not see it as their responsibility to get themselves home.

**2.43** An appetite for additional protection against airline insolvency became clear once participants understood what insolvency entailed and what protection they currently could access.

**Figure 2.6: ATOL Extension**

The Government is currently investigating options to protect passengers in case of airlines going out of business. At present ATOL protection only applies to package holidays that include a flight. To what extent, if at all, do you agree or disagree that protection should be extended to cover individual flights, and not just package holidays that include flights?



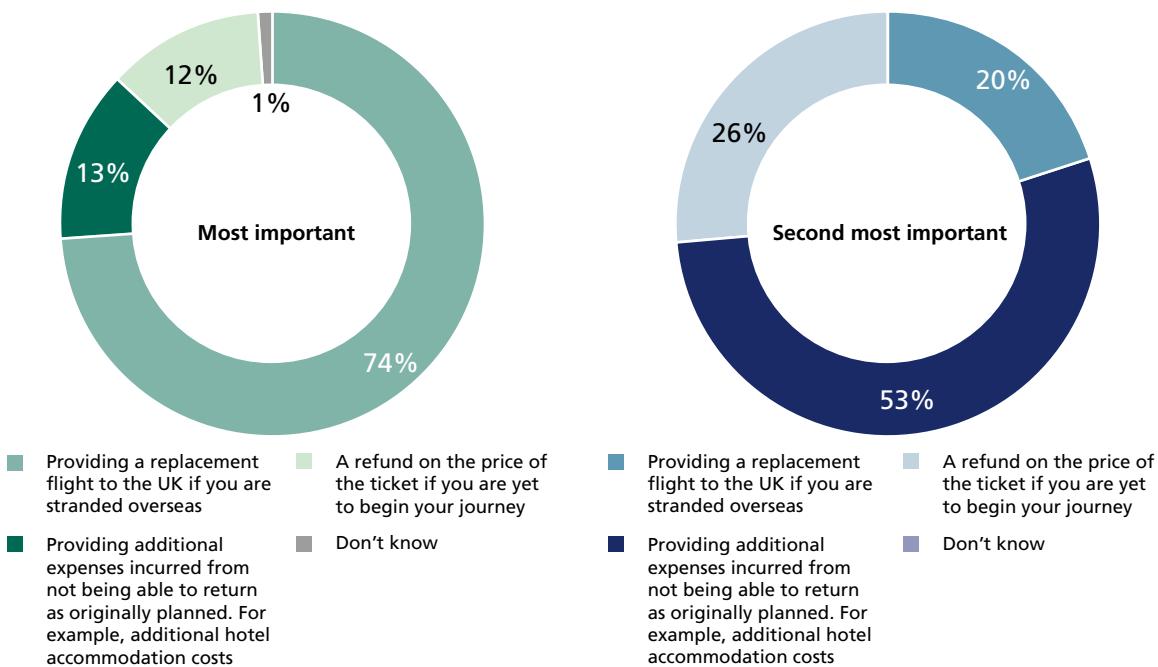
Source Ipsos MORI (2019) Annex C

**2.44** This view also came across strongly in the response to the survey, where 86% of respondents agreed that ATOL protection, or something similar, should be extended to cover all individual flights and not just those purchased as part of a package holiday.

**2.45** A large proportion (74%) felt the most important element of protection should be a replacement flight if their airline collapses while they are overseas. The provision of additional expenses incurred from not being able to return as originally planned was seen as second most important to the majority (53%).

**Figure 2.7: Most and Second Most Important Issue**

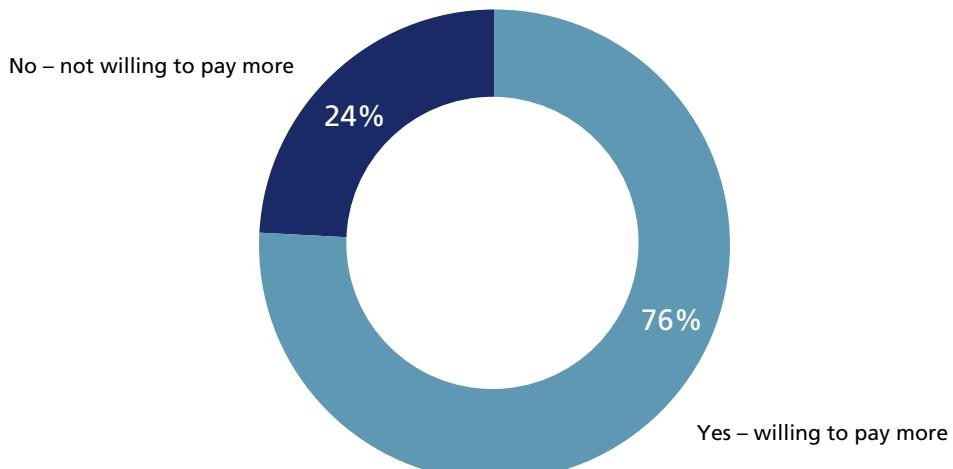
If the government were to ensure all passengers are protected when airlines go bust, in your opinion which one of the following would be most important to you personally and which would be 2nd most important to you personally?



Base: All valid responses who have flown within the last three years (2028). Source Ipsos MORI (2019) Annex C

**Figure 2.8: Willingness to Pay – I**

At present, ATOL protection only applies to package holidays and costs £2.50 per passenger. If similar insolvency protection was extended to cover all airline passengers, it could mean that the price of your airline ticket would increase slightly. Would you be willing to pay more for your airline ticket for such protection?



Source Ipsos MORI (2019) Annex C

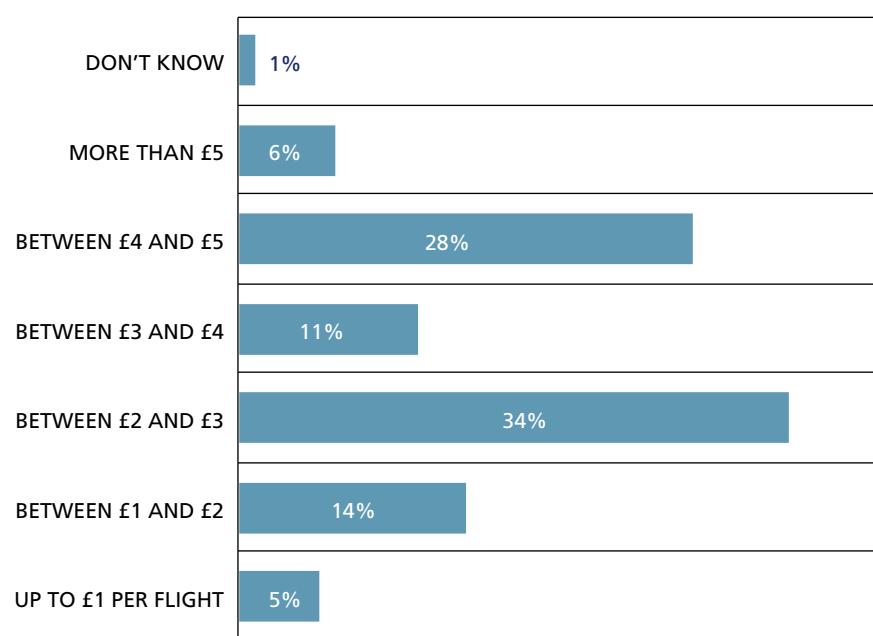
## Willingness to pay

**2.46** Most respondents (76%) would also be willing to pay more for their ticket for this protection, with 94% of these willing to pay £1 or more, and 73% willing to pay between £2 and £5.

**2.47** There was also a strong preference that if insolvency protection is extended to all flights, this should be applied as a fixed amount per flight, rather than a variable rate based upon the risk of the airline going out of business.

**Figure 2.9: Willingness to Pay – II**

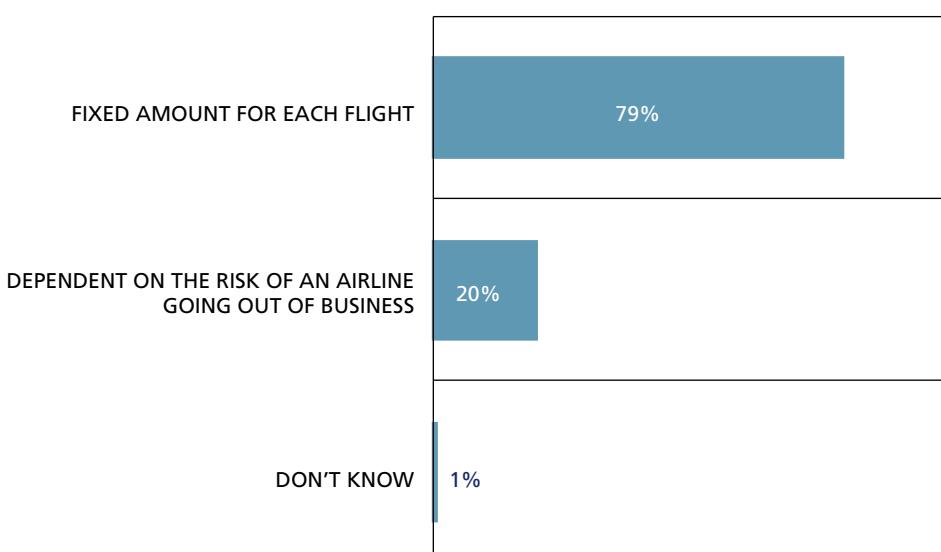
If insolvency protection was extended to cover all airlines passengers, how much would you be willing to pay for this protection for each flight you take?



Source Ipsos MORI (2019) Annex C

**Figure 2.10: Fixed or Risked Base Amount**

If insolvency protection was extended to cover all airlines passengers, In your opinion, should the cost of this be a fixed amount OR should it depend on the risk of the airline going out of business?



Source Ipsos MORI (2019) Annex C

# 3. Passenger requirements



## What protection do passengers need?

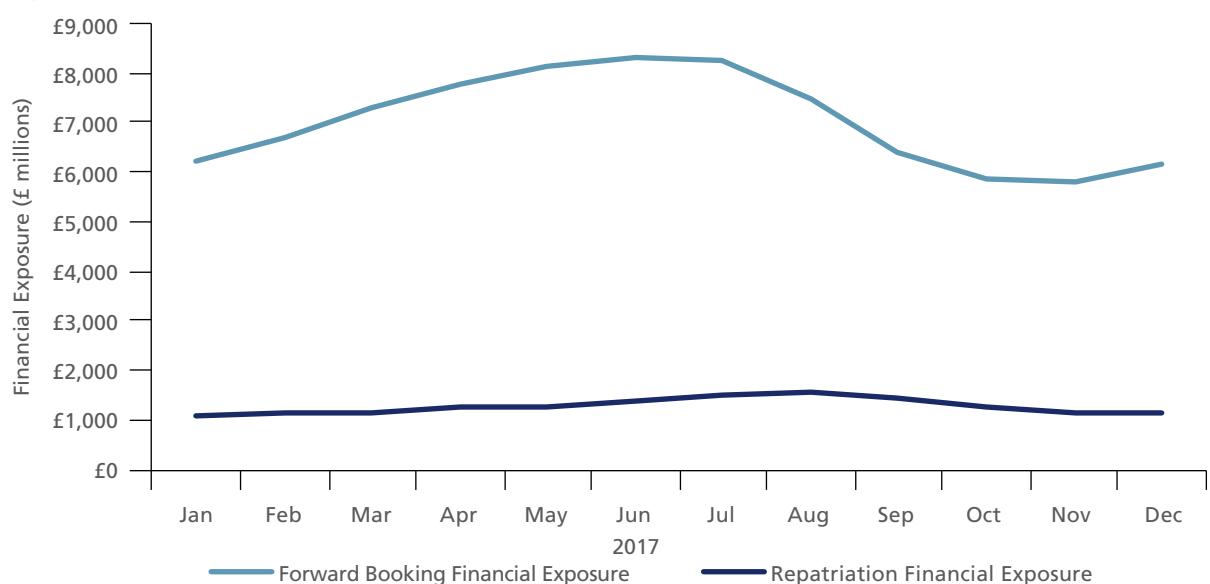
**3.1** When a passenger books a seat, they are financially exposed to the risk of the airline becoming insolvent either before they have begun their journey or, having begun it, before the journey is completed. One finding is clear: the total financial exposure of those yet to travel and needing refunds is always significantly greater than those who have already begun their journey and need repatriating, whatever the time of year. The seasonal

variation in total financial exposure arising from flights departing the UK is shown in Figure 3.1<sup>10</sup>, and the corresponding number of passengers is shown in Figure 3.2 (opposite).

**3.2** There are a variety of existing mechanisms to provide protection from the risk of insolvency events – see Figure 2.2, see page 26-7.

**3.3** We estimate approximately 80% of passengers are currently protected via the ATOL scheme, SAFL and Section 75 of the

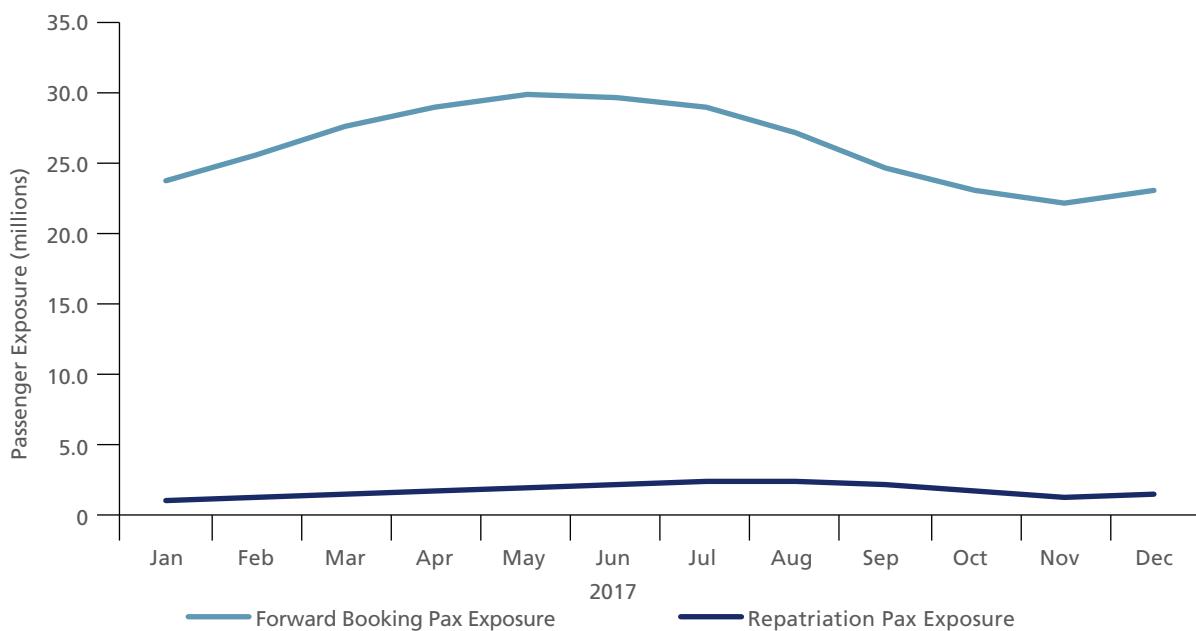
Figure 3.1: Seasonal Variation of Financial Exposure<sup>11</sup>



Source ICF (2019)

10 The total financial exposure of forward bookings was estimated by examining the level of deferred revenue on airlines' balance sheets. The total repatriation financial exposure was estimated on the basis of the most cost efficient repatriation option for each airline: the most cost efficient repatriation option is dependent upon the number of affected passengers and hence varies by airline.

11 ICF (2018) Airline Insolvency Review Aviation Data and Economics – See Annex E.

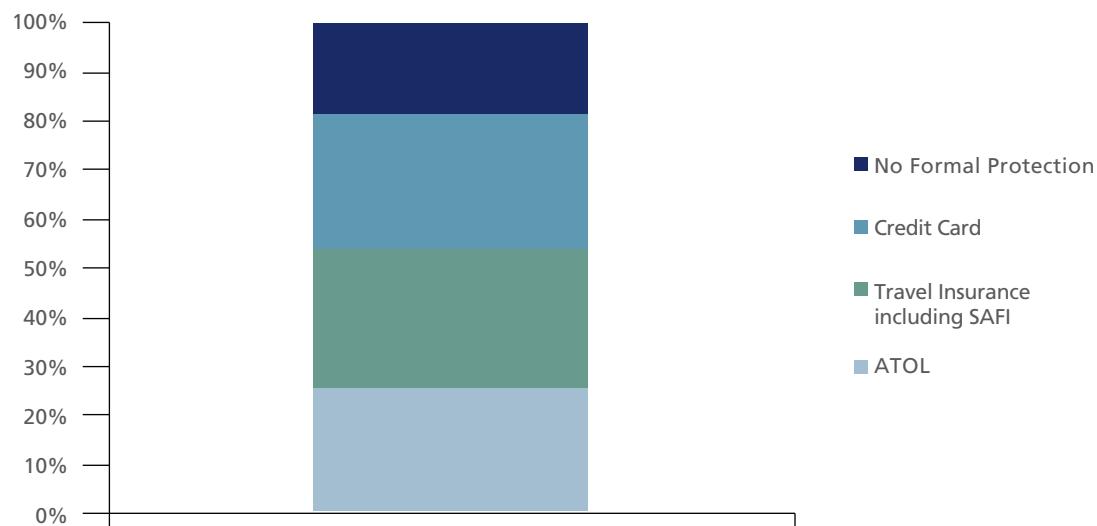
**Figure 3.2: Seasonal Variation of Passenger Numbers**

Source ICF (2019)

Consumer Credit Act 1974 – see Figure 3.3, (below). The remaining 20% may have some protection from charge-back schemes through debit card providers or other, non-statutory, protection such as PayPal's Buyer Protection Scheme.

**3.4** Apart from the ATOL scheme, existing protections only provide financial compensation after a loss is incurred and a claim has been made, which can take time

to process. As such, they are a reasonable means to obtain refunds in relation to forward bookings. They are less effective where passengers need repatriating because even if a replacement seat is available, advance payment is needed, which could prove difficult for some passengers. If a centrally organised repatriation operation is required to put in place a repatriation, immediate access to funds to pay for the operation would be key.

**Figure 3.3: Coverage of Existing Protections**

Source ICF (2019)

**3.5** We conclude that as over 80% of people have some form of formal financial protection to provide them with a refund relating to a future booking, the existing protection landscape is sufficient for protecting those bookings. We recommend government keeps this protection under regular review, however, to ensure the proportion of protected bookings does not fall and to consider whether it can be enhanced.

**3.6** In contrast, a new arrangement is needed to establish the option to repatriate because funding will be needed.

## Enhancing refund protection

**3.7** As we set out above, there are a range of refund protections already available to passengers through credit cards, debit cards and other payment services. Passengers can also take further steps by booking an ATOL protected holiday or taking a travel insurance policy with supplier failure cover. As set out above, we consider these provide an adequate level of protection for forward bookings and accordingly we do not consider there to be a strong case for setting up an additional layer of refund protection.

**3.8** However, we do recommend that government should work with partners to help enhance existing refund protection and the clarity around it. We propose:

- Increasing consumer awareness and uptake of refund protection.
- Minimising unnecessary duplication of protection.
- Helping passengers to make a claim swiftly and easily.

**3.9** Improving each of these areas is likely to require action by government, the Coordinating Body, the airline industry, insurance industry and the card payment sector.

**3.10** We recommend government creates a working group, bringing together representatives from each area to produce best practice guidance to meet all three categories above.

## Increasing the uptake of refund protection

**3.11** We know around 80% of airline passengers currently have formal refund protection, either through the ATOL scheme, their credit card company or travel insurer. While this does leave around 20% of passengers without formal refund protection, we understand many of them will have booked in a way that affords some form of non-statutory protection (for example, under the Visa or MasterCard debit card charge-back schemes or the PayPal Buyer Protection Scheme).

**3.12** While this is a largely positive picture, there will still be some passengers with no form of refund protection when booking a flight. The consumer research (see Annex C) suggests some passengers consciously decide not to pay for cover, particularly for short-haul flights. For others, the lack of protection may stem from not understanding the risks, their options, or the availability of protection. Our research suggests some passengers mistakenly believe they are already protected. For example, the Ipsos MORI survey found 53% may have taken out travel insurance without realising that it does not cover Scheduled Airline or End Supplier Failure.



**3.13** Some have suggested that this misunderstanding of the protection available extends to the ATOL scheme. In particular, whether or not passengers are always aware before or, in some cases after purchase, that their travel arrangements are protected.

**3.14** We identify a need to raise awareness about available protection and do more to actively inform passengers when they are not protected.

**3.15** We understand around half of travel insurance policies on the market do provide a degree of protection for airline failure. We have identified an appetite for airline failure cover and an expectation from many consumers that it would already be included in their travel insurance policy. We suggest insurance providers and third-party comparison websites should do more to ensure customers understand what risks are

covered by individual policies, so that consumers can make informed decisions.

**3.16** We recommend government involves all parties in its working groups to enhance understanding of the nature and extent of travel insurance. For example, third-party comparison and consumer information providers may be able to do more to generate take-up. Behavioural 'nudges' could also encourage greater take up of protection. As airlines will typically have a direct customer interface with the vast majority of passengers who would be impacted by their failure, they could help them better understand the risks. We do not propose mandating particular information be provided in the first place, but that government should work with airlines to promote the provision of relevant information to passengers at the point of booking to nudge them into making better choices about financial protection.

## Improving passengers' ability to make a claim swiftly and easily

**3.17** More information should be made available to consumers when airlines fail so they can check what protection they have for their forward booking and from which organisation to seek a refund. Government should ensure protection providers agree a unified approach to claims that is clear for consumers.

**3.18** We have heard anecdotally that some customers holding travel insurance policies including Scheduled Airlines Failure or End Supplier Failure provisions may not understand their protection, or be able to claim successfully under it, when they suffer a loss. We recommend the Financial Conduct Authority (FCA) considers reviewing these products to see whether further regulatory measures would be appropriate to ensure contract terms are fair and claims procedures are responsive and easy to navigate.

## Keeping protection under review

**3.19** We recommend government should keep refund protection under review. These protections are largely determined by how consumers book and pay for their flight, and whether they have engaged the statutory protection under the ATOL scheme or Section 75 of the Consumer Credit Act. Over the past two decades, the growth of the online marketplace provides greater choice and opportunity for consumers. The government has recently updated the ATOL scheme to reflect these changing buying habits.

**3.20** Similarly, the Review is aware of a greater diversity in the way that people can pay for their holiday, with the use of third party payment processors like PayPal providing an alternative to the use of credit and debit cards. The FCA is currently reviewing elements of the Consumer Credit Act 1974, including Section 75 protection. In its Interim Report published in August 2018, its initial view was that Section 75 should be retained in legislation to retain an appropriate degree of consumer protection<sup>12</sup>. However, it will continue to give the issue further consideration, including looking at the protection that Section 75 affords and the type of payments that it should cover.

**3.21** We recommend the Department for Transport engage with the FCA on this work, as any material changes could have an impact on the number of airline passengers entitled to receive refund protection following a failure.

## Introducing repatriation protection

**3.22** We recommend a formal repatriation protection scheme is put in place that is practicable, effectual and affordable. We refer to this as the Flight Protection Scheme.

**3.23** We recommend appointing a Coordinating Body and giving it a duty to use its reasonable endeavours to repatriate passengers to the UK, on the same day and to the same airport to which they expected to return. The nature of the journey (for example, routeing, mode and class of travel) would be left to the discretion of the Coordinating Body.

<sup>12</sup> Review of retained provisions of the Consumer Credit Act: Interim Report (Financial Conduct Authority, August 2018) [www.fca.org.uk/publication/discussion/dp18-7.pdf](http://www.fca.org.uk/publication/discussion/dp18-7.pdf)

**3.24** By “repatriation”, we mean returning passengers to where their outbound journey started. In particular, the Review’s focus has been on passengers who require repatriation to the UK (UK-originating passengers). The Flight Protection Scheme should protect any air passenger whose journey began in the UK, and who has a ticket to return on an airline that becomes insolvent while they are already overseas. The protection would apply irrespective of how, or from whom the ticket was purchased or paid for.

**3.25** There would be no time limit to this protection; however the way in which it is delivered may vary to respond to the particular situation, as described in

Chapter 4. In some cases, this might involve an active repatriation period, where the Coordinating Body takes steps to provide aircraft capacity to get stranded passengers back to the UK.

**3.26** This might only continue for a short period (typically up to 14 days) until there is sufficient capacity in the market for passengers to purchase a ticket on an alternative flight at reasonable cost. Remaining protected passengers would then be entitled to rebook and claim a refund for a replacement flight from the Scheme. We anticipate the claim period would continue beyond the point the last passenger was due to fly home, which could be up to a year.



# 4. Repatriating passengers following a failure



**4.1** In our Interim Report, we identified four factors against which a successful repatriation operation can be judged:

## Certainty

Passengers will want a high degree of certainty that repatriation arrangements have been made, or are in hand for them to get home, what those arrangements are and when they will be enacted. Much depends on scale but for any sort of sizeable repatriation operation, whenever that certainty does not exist passengers will begin to try to achieve it for themselves. Often such action leads to the flooding of communication systems with the potential to undermine the viability of any arrangements e.g. preventing agents dealing with more urgent cases.

## Clarity

Passengers need clarity about their travel arrangements and what is expected of them. If information is not useful and timely, it will heighten uncertainty, impacting on any repatriation operation as passengers seek to obtain such clarity.

## Confidence

Passengers will need confidence in any repatriation arrangements. Confidence that their individual circumstances are being catered for in a manner that is affordable to them. Any organiser (be

that the passengers themselves, the Civil Aviation Authority (CAA) or a private company) must fully and authoritatively own the operation in words and deeds, provide the services offered, and communicate confidence.

## Communication

Passengers must be able to easily access information relevant to them, whenever they need it. This requires a clear point of authority (who is responsible and accountable) with access to that authority 24/7. There needs to be a clear programme of communication such that passengers' expectations are managed and information availability (or lack of it) is understood. Finally, passengers will need to know what support is available to them and how to access it should they need to.

**4.2** The recommendations we make in this chapter are designed to facilitate successful delivery of each of these factors.

## Mechanisms to repatriate passengers

**4.3** The Review has identified four main mechanisms which could be adopted by the Coordinating Body to deliver repatriation, either in isolation or combined, depending on its nature and scale. Which solution to use will be determined by the type and size of the

failed airline, where it operates and its routes, the frequency of flights, and the time of year when the failure occurs, with the overall aim of deploying the most cost-effective solution in each case.

**4.4** The over-arching aim would be to rely to the greatest practicable extent on the airlines themselves to deliver repatriation, whether by use of spare-seat capacity under “rescue fare” arrangements or by keeping the fleet of the failed airline flying.

**4.5** The options are:

## 1 – Self-Repatriation

**4.6** Affected passengers find, book and pay for seats on other airlines, benefiting from available rescue fares, at a reduced price for a short period of peak demand, generally two weeks. At present, this is the sole form of repatriation available

following most airline failures, and passengers must seek refunds from any existing protection mechanism to which they have access (credit or debit card, travel insurance as set out in Chapter 3). If the Flight Protection Scheme is fully implemented, it would provide eligible passengers with a refund.

## 2 – Assisted Repatriation

**4.7** This is an enhancement of self-repatriation. A Coordinating Body could play a more active role following larger failures where more travellers are affected, but other airlines are still able to provide seats (including by deploying larger aircraft) to bring them home. The Coordinating Body would work with airlines to make more types of flight available (for instance, connecting flights through an intermediate airport). It would also inform passengers about available flights and provide a booking facility.



### 3 – Organised Charter

**4.8** An organised operation to charter aircraft from third-party airlines and run a programme to fly passengers home. Critical to the effectiveness of this option is having enough advance notice to be able to secure and position a sufficient number of aircraft to enable a high degree of confidence in the repatriation operation. This is how the CAA repatriated passengers following Monarch's failure.

### 4 – Keeping the Fleet Flying

**4.9** Keeping the Fleet Flying (or KFF), means introducing a mechanism to allow an insolvent airline to keep aircraft flying for long enough to repatriate its passengers or until other solutions can be deployed to bring everyone back. Currently, UK aircraft licensing and insolvency law present major obstacles to this but, given the uncertain ability to respond to a major failure using scheduled or charter capacity from other airlines, we recommend government takes steps to facilitate its use (see Chapter 6).

**4.10** We refer to these mechanisms as the 'repatriation toolkit'. In chapters 4, 5 and 6, we will examine each option, and how they can be deployed and enhanced.

### Hybrid operations

**4.11** In theory, all the repatriation options detailed above, could be combined under the Coordinating Body's control to undertake operations following the most complex failures. The ability to "pick and mix" elements of the repatriation options informs our recommendations.

**4.12** For example, it may be best to use Organised Charter at the beginning of a repatriation but as numbers of passengers dwindle towards the end of the operation, they can be accommodated on existing

spare seats on other airlines; (Self or Assisted Repatriation). This was the case during the Monarch repatriation. The Coordinating Body would need to determine in advance which mechanisms to adopt so as to manage repatriation in the most cost-effective and proportionate fashion.

### Role of a Coordinating Body

**4.13** For repatriation to be effective in all circumstances, a coordinator is needed to plan, manage and, in certain circumstances, run a repatriation operation. Throughout this report, this role has been named the Coordinating Body.

**4.14** In many cases, the actual delivery of the repatriation and other services will largely be performed by third-parties in the private sector, managed to a greater or lesser degree by the Coordinating Body depending on the nature of the failure.

**4.15** Repatriation could potentially be coordinated by a government department, the CAA, industry representatives or even by a third party such as the insurance industry or card payment bodies.

**4.16** The Coordinating Body is necessary to deliver repatriation efficiently and effectively. The nature of the role will differ depending on which toolkit mechanism is adopted, with greatest intervention necessary when an organised charter is required and least when all that passengers need is a "signpost" to book rescue fares in order to self-repatriate.

**4.17** We consider a single Coordinating Body with the authority, capability, funding and resources is best-placed to respond to failures in three key areas:

- 1.** Delivering an effective repatriation. There are likely to be multiple stakeholders involved, both in the UK and overseas. A Coordinating Body should improve planning, cooperation and communications among all parties, providing a smoother and more efficient repatriation.
- 2.** Managing funds. Organising charter aircraft or keeping the fleet flying would require finance to be available prior to the point of failure. A Coordinating Body should manage access to this finance – through routes we propose in Chapter 8.
- 3.** Providing clear communication. Hundreds of thousands of passengers could potentially be affected. They will need access to timely and relevant information to help them get home. The Coordinating Body should act as the principal point of authority to deliver clear communications.

## The Civil Aviation Authority

**4.18** Throughout the Call for Evidence and in our discussions with stakeholders over the course of the review, we have found a broad consensus that the Civil Aviation Authority (CAA) would be best placed to act as the Coordinating Body. The CAA benefits from:

- Regulatory oversight and reach: As the UK's aviation regulator, the CAA already oversees UK airlines and controls access to levers by which participation in the funding mechanism could be enforced (e.g. through licensing). It is also already recognised by overseas regulators and can draw on its existing relationships to respond to any future failures.

- Mission Alignment: the CAA already ensures consumers are protected and treated fairly.
- Capability: Through its experience of managing the ATOL scheme, the CAA has established expertise. Its ability to perform successfully in this role was tested by the Monarch failure in 2017.
- Independence: The Coordinating Body is likely to need access to confidential or sensitive information from an airline before it enters insolvency, and be able to engage with third parties appropriately. The CAA is best placed to perform this role, as it is an independent regulator with experience of handling confidential information from airlines. Existing law provides a statutory basis for this confidentiality via Section 23 of the Civil Aviation Act 1982.

**4.19** We have not identified another organisation better able to take on this role than the CAA, nor has any other body been proposed to us. Both the airlines and the card companies and insurers who provide financial loss protections have told us they are not positioned to be able to take on such a function. We, therefore, recommend the CAA is best positioned to take on this role.

**4.20** As outlined above, to act effectively as the Coordinating Body, the CAA will need authority, capability, funding and resources. We make recommendations to government in this Chapter and in Chapter 8 as to how these requirements could be met.

**4.21** We recommend the CAA develop Memoranda of Understanding and appropriate Non-Disclosure Agreements with relevant third parties to ensure they work together effectively to develop and deliver a solution.



**4.22** We recommend the CAA enhances its ability to use market data to assess in advance the most cost-effective repatriation mechanisms, and prepares to adopt hybrid operations to manage the largest and most complex failures of UK- or foreign-licenced airlines. To do this effectively, it also needs advance access to airline passenger data, covered below. Given the CAA's role as the UK's airline licensing body, it will have better access to data for UK airlines than foreign ones. This means that following the failure of larger foreign airlines, delivering effective repatriation in a timely manner may prove more challenging.

## Managing multinational failures

**4.23** As set out in Chapter 2, one of the key aspects of aviation is its multinational nature, and the way that integrated travel groups operate across Europe, with multiple Air Operator Licences and Air Operator Certificates (AOC) from different countries.

**4.24** The Review recognises this makes any form of repatriation operation to

protect UK passengers more complex. Several regulators will be involved, each of whom may have their own plans on how to intervene, whether this is within a regime in which flight operations may continue, such as in the case of Air Berlin, or an urgent organised repatriation operation, as in the case of Monarch. It is possible that different solutions would need to be deployed in different countries for one airline's failure.

**4.25** With such complexity, an airline insolvency, whether of an individual airline within a larger business group (for example an unprofitable airline being allowed to fail in the interests of the survival of the larger group), or an entire group of airlines under a single holding company, will present significant challenges for countries to manage.

**4.26** The Review recognises the UK would have to work closely with other countries in advance of a potential failure, in order to protect the interests of UK passengers. The Coordinating Body will need to have a high level of confidence in respect of both advance planning with other State regulators and the ability to

**Figure 4.1: Airline Business Model**

Type	Example	Issue for regulators
<b>Type D</b> Airlines with significant operations in countries where they are not regulated.	Ryanair is regulated in the Republic of Ireland, but has one of the largest shares of the UK Market.	The concern here is that the country whose citizens would potentially be most impacted may have no regulatory oversight to respond to an emerging financial problem and may have little advance notice of insolvency.  Effective repatriation would be reliant on the regulating country making provisions for citizens of other countries, or working in very close cooperation with overseas regulators.
<b>Type E (1)</b> Airlines with associates or subsidiaries holding licences to operate from more than one country, either with integrated or independent operations.	Norwegian holds licences from a number of different countries, including the UK.	As with Type D, but with the added complexity of establishing whether the associate airline would be able to continue to operate as a distinct unit or would fail alongside the parent.  If the latter, should the country which regulates the associate airline solely protect its citizens, or work alongside the other country in a coordinated operation?
<b>Type E (2)</b> Integrated holiday groups with UK and non-UK airlines operating independently of each other.	TUI	An additional scenario may be that an associate airline in one country is allowed to fail by its parent airline in another, leaving the country that licenses the failed element with the problem of protecting its citizens.

efficiently execute any joint operation, in particular to meet the needs of UK consumers. As recognised by the European Commission's 2013 communique<sup>13</sup>, inter-governmental regulator understanding and coordination is critical. In some circumstances, the Coordinating Body may have to act alone to repatriate UK consumers, but it is likely that this would lead to worse outcomes than effective cooperation with international counterparts.

**4.27** In Chapter 2 we set out five types of airline regulatory relationship. In three of these types (set out in Figure 4.1 above), the Review considers that collaboration could improve the consumer protection:

## International cooperation

**4.28** The Review considers international agreements are essential to improve consumer protection outcomes across Europe.

**4.29** We recommend that the Coordinating Body engages with its international counterparts to gather information to understand:

- What regulatory monitoring and enforcement procedures are in place to manage licensing and safety where an airline is poorly performing and at risk of insolvency.
- What insolvency provisions are in place to support an airline to maintain services to passengers.

<sup>13</sup> Communication From The Commission To The European Parliament, The Council, The European Economic And Social Committee And The Committee Of The Regions Passenger Protection In The Event Of Airline Insolvency <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52013DC0129>

- What contingency plans or other provisions exist to transition an airline to recovery or closure which safeguard passengers.
- What restrictions, risks and issues may hamper the ability of regulators to coordinate repatriation operations.

**4.30** The outcome of this exercise will assist the Coordinating Body in determining other states' approaches to airline insolvency, whether they have safeguards in place to protect their citizens, and their appetite for international cooperation.

**4.31** Government and the CAA should maintain regular communication with other international organisations where appropriate to share information and best practice.

**4.32** Where there is a likelihood that significant numbers of UK-originating passengers could be adversely affected, the Coordinating Body should look to develop of a formal co-operation framework. This should be set out in a Memorandum of Understanding (or other appropriate form of protocol) and provide a sufficient level of detail to enable it to be put into effect at short notice should occasion require it.



# 5. Enhancing existing repatriation mechanisms



## Self-Repatriation

**5.1** Self-Repatriation is likely to be the most cost-effective repatriation mechanism when a small or medium-sized airline becomes insolvent. It is also a solution when a larger foreign airline fails if it is carrying a smaller proportion of UK-originating passengers.

**5.2** Most recent failures (with the exception of Monarch in 2017) have been small enough to be managed using Self-Repatriation, but this is dependent on the time of year of the failure, and the routes served by the failed carrier, which affect the availability of seats. Our proposals relating to Assisted Repatriation would allow a similarly cost-effective mechanism to be applied following (some) larger failures.

## Assisted Repatriation

**5.3** In the interim report, we committed to exploring how the Self-Repatriation option could be improved upon and applied to a greater number of failures. We propose Assisted Repatriation to achieve this.

**5.4** Following larger failures, where more travellers are affected, but where it has been established that other airlines have enough spare seats to bring at least some home, we envisage a scenario where the Coordinating Body plays a

more active role. It would work with airlines to make a wider range of types of flight available (for instance connecting flights via another country and flights between nearby airports rather than the same ones). Over time, the Coordinating Body might develop its role to provide services that would inform passengers about available flights and allow them to book their return flight – essentially acting as a travel agent.

**5.5** A central aspect for both options is the availability and cost of rescue fares, which we explore below.

## Rescue fares for Self- and Assisted Repatriation

**5.6** Rescue fares are discounted tickets offered by other airlines to passengers affected by an airline failure, who normally need to show proof that they had booked with the failed airline. When smaller operators, or foreign operators with a relatively small number of UK passengers, fail, these fares offer a way for passengers to return home. This is what happened in the case of Primera Air in 2018, among others.

**5.7** There is no focal point or set procedure to find or to offer rescue fares; they are sold at the discretion of the airline concerned, which will generally only make them available if it flies the same routes as the failed carrier.

## Case Study Primera Air

Icelandic-owned Primera Air Scandinavia started life in 2008 as a charter service from northern Europe to the Mediterranean. Seven years later, it was a low-cost scheduled airline with flights including from the UK to North America and Canada on 14 mixed-type aircraft.

On 02 October 2018, it ceased operations, pointing to growing losses and financial difficulties, leaving an estimated 5,000 UK passengers without flights home.

### Airlines' Response

The Review saw communications co-ordination among British airlines – through Airlines UK especially – to help passengers re-book. The airlines' approach was assisted by the CAA, which helped by sharing information such as on-line and call-centre details.

British Airways, Virgin Atlantic, Delta Air Lines and Norwegian provided support to UK passengers on US routes, with some offering significant discounts, as did BA, EasyJet and Ryanair in Spain.

500 UK passengers (of 5,000 affected) claimed these rescue fares. However, 8% of rescue bookings examined at check-in were passengers who did not qualify and were asked to pay the right fare: an indication of the risk to airlines in offering rescue fares and their limitations.

**5.8** Airlines and their trade bodies have told the Review that, as a general matter, they will usually try to assist passengers of a failed airline in this way when they are able to do so. In particular, this is subject to the availability of spare seat capacity. They are not therefore able to make a firm commitment to do so in all cases. The voluntary nature of rescue fares gives them control over the commercial impact on their operations. They also told us that having control of prices without a set formula or regulation gives them the flexibility to decide the fare level on a case-by-case basis.

**5.9** The Review accepts this but nonetheless considers there is scope to make it simpler for affected passengers to access these fares and to widen their availability, which may ultimately reduce the costs of any further repatriation operation.

### Enhancing capacity and participation in rescue fares

**5.10** We recommend that the Coordinating Body holds bilateral talks with airlines to assess their appetite and ability to enhance the provision of rescue fares, with a view to widening rescue fare provision. The Coordinating Body will need to hold appropriate confidentiality agreements with key airlines so that where it considers there is a chance of an airline failing, it is able to engage airlines operating similar routes to try to maximise availability of spare seats.

### Code of conduct for rescue fares

**5.11** We recommend the Coordinating Body, airlines and airline representative bodies work together to produce a single code for rescue fares, with the aim of drawing together existing voluntary arrangements into a cross-industry Best

Practice document, which should include the following:

- Establish an agreed formula by which rescue fares may be set and defined to provide clarity to passengers and the Coordinating Body, as well as identify what financial arrangements may be put into place to maximise the number of seats available at these fares.
- Identify improvements to be carried out for preparations ahead of any future airline insolvency.
- Explore greater participation of the widest number of airlines that may offer rescue fares, explore how to expand the number of airlines offering rescue fares, including airlines that do not directly operate on a route, both in respect of the number of seats they may make available and the basis on which fares will be charged.
- To protect airlines, agree in advance how to ensure only passengers entitled to rescue fares are carried for that fare.
- Provide passenger access to fares, regardless of their circumstances or how they have paid, and whether or not they have relevant insurance cover;

consider the feasibility of a single access point to give passengers options and choice.

- Monitor the performance of airlines during a repatriation to develop understanding of the effectiveness of rescue fares and capacity, and use this intelligence to foster further improvements.
- Promote greater awareness amongst a network of key airlines and personnel of their potential role in providing rescue fares, in advance of specific failures under a confidentiality agreement, or in general.

### **Coordinating and centralising rescue fares**

**5.12** We consider that there are significant benefits in achieving a single access point to rescue fare information, for consumers and the Coordinating Body.

**5.13** When Monarch failed, a central flight information system by which passengers could easily access their new flight home played a critical role in providing information and certainty to passengers about their repatriation flights.



**5.14** Similar benefits can be achieved in the provision of rescue fares and we recommend the Coordinating Body adopts an evolutionary approach to developing the current voluntary arrangements to introduce a single access point to rescue fare information.

## Organised Charter

**5.15** This is the mechanism adopted by the CAA to repatriate passengers following Monarch's failure in 2017. Monarch used only narrow-bodied, smaller aircraft. The operation was able to utilise larger, wide-bodied aircraft to a significant degree in its first week. One of larger aircraft could bring home the equivalent of two passenger-loads of a smaller aircraft. However, if a future failed airline's fleet were made up of larger aircraft, it would pose significant problems in sourcing enough available aircraft to mount an operation. This is especially relevant as it is generally accepted that the Monarch operation was only possible because of exceptional circumstances in which crucial additional capacity was available, which is unlikely to be the case in future. This issue is explored below.

### Enhancing Organised Charter

**5.16** Organised Charter operations provide a high level of confidence in operational capability and effectiveness, which was clearly demonstrated in the Monarch repatriation. Our recommendations below are designed to augment the CAA's ability to deliver these types of operation.

**5.17** In the Interim Report, we stated that in current market conditions, outside the peak summer period, it should be possible to secure at least 60 aircraft needed to operate a substitute service of an airline with around 80 aircraft. This was based on

the CAA's critical mass formula which comprised these three factors:

- type and number of aircraft operated;
- the airline's load factors; and
- estimated availability of spare aircraft and seats.

**5.18** The ability to organise charters beyond 60 aircraft will always depend on the last factor, which is dependent on a large number of external factors (many of which are beyond the CAA's control). As such, depending on when they are required, scope to organise charters beyond 60 aircraft may be limited. As such, we recommend the CAA explores the extent to which it may be possible to increase this figure, including establishing whether using airlines' standby aircraft could be an option and how this would be achieved.

**5.19** Beyond this, we agree that available aircraft capacity will remain a challenge for short-term, high-demand repatriations. Creating a Hybrid Operation by combining an Organised Charter with Self- or Assisted Repatriation may help to manage airline failures involving larger fleets but there is a clear limit. This is explored in the Keep the Fleet Flying option later in this chapter.

### Enhancing Organised Charter resilience

**5.20** The Coordinating Body should continue to develop resilience by seeking to expand the number of airlines that may supply aircraft through advance agreements. In addition the coordinating body should seek a greater understanding of the potential of the spot-market to augment and support the pre-secured fleet.

**5.21** The airlines acknowledge the CAA has the skills and oversight required to implement and lead an Organised Charter repatriation operation.

**5.22** Bilateral contact between the Coordinating Body and airlines with aircraft best suited to repatriation deployment (i.e. larger, wide-bodied types) should be developed.

## Enhancing passenger data

**5.23** When Monarch Airlines failed, the number of passengers that were expected to be flown home was around 110,000. In the event, 85,000 were repatriated by the CAA. The CAA's initial estimate based on information supplied to it by Monarch had included all people booked to fly home with Monarch in the repatriation period from 02 October. Some of these had not travelled before the date of failure, while others made their own arrangements to get home.

**5.24** To ensure the scale of the repatriation operation matches the number of affected passengers as closely as possible, we recommend the CAA, as Coordinating Body, improve its access to data in advance of insolvency events. As such, data access should be included within the requirements for repatriation plans of UK airlines. Where possible this could extend to foreign airlines, but is likely to be more difficult for the CAA to access, and require engagement with overseas regulators (repatriation plans are discussed in more detail in Chapter 6).

**5.25** Also, if information held by a failed airline on its passengers can be accessed, including contact details, this can be used to contact passengers in advance.

**5.26** The CAA Monarch website was highly effective in ensuring people could easily check details of their new flight home, but in just telling people when they could fly, gave the CAA little certainty whether they would arrive for that flight. In developing systems to draw together flight information for passengers, the CAA

should consider whether it would be appropriate to introduce the ability for passengers to confirm their intention to take a flight in advance.

## Organised Charter and flight operations management

**5.27** Flight operations management and the technology which supports it are crucial in planning and executing an Organised Charter.

**5.28** The technology must also be able to communicate effectively with those systems that convey information to passengers about their flight arrangements in a timely way.

**5.29** Resources and technology should be developed so there is confidence in its ability to manage airline failures to the upper limits of the size and operational complexity of any affected fleet.

**5.30** We recommend the Coordinating Body and industry work together to ensure this is up-to-date, well prepared and quick to mobilise ahead of any future need.



# 6. Enabling an orderly wind down



**6.1** The Review was tasked with investigating how airlines could wind down in an orderly fashion to conduct a repatriation with minimal need for government intervention. A key element of this task is to explore how to keep an airline's fleet of aircraft flying at the point of insolvency.

**6.2** Many stakeholders told us this would be an optimal solution to the repatriation problem if it could be made to work. It appears to be the only viable way of responding to the collapse of a large airline, or a failure in peak season when alternative capacity in the market may be insufficient. The airline should already be set up to deliver its schedule in the most efficient and effective way possible. This could provide a better outcome for the consumer, ensuring there is sufficient capacity in the right place to get them home, and simplifying the coordination, communications and booking process.

**6.3** The broad aim would be to maintain the airline's service using its existing fleet, in order to meet the immediate travel needs of passengers left overseas. For most airlines we consider these operations would only be required for a short period (in most cases 14 days, or less), until the market can cope with residual demand.

**6.4** Even in situations where it is possible to get passengers home through an organised charter approach, it might still

be essential to maintain other parts of an airline or the wider company, to support a repatriation operation. This was evident in the Monarch repatriation, as even though the CAA was able to source aircraft from the market, it was still necessary to keep parts of the Monarch Group running in administration. While the Monarch situation demonstrated it is possible to keep parts of an airline running in administration, the prospect of keeping the airline's fleet flying would have presented a much greater degree of challenge.

**6.5** In the period following the publication of the Interim Report we have worked with our advisors and stakeholders to get a better understanding of the challenges and constraints around keeping a fleet flying. In the remainder of this section we discuss the ability to keep a UK airline running at the point of administration, and the risks and challenges involved with that approach. Then in the remaining sections of this chapter we make recommendations on how to enhance the ability to deliver a repatriation in this way.

**6.6** We identify two broad areas of development that will help to ensure a UK airline can keep flying at the point of insolvency. The first relates to the UK's insolvency rules and the ability to create a regime that is better suited to an orderly wind down of an airline. The other is the



UK's regulatory framework for air operator licensing, to provide the CAA with better oversight and control of the situation.

**6.7** Combined, these will help to address the potential risks and challenges inherent in this option, and provide more control over costs and delivery. This could allow for a less disruptive, and lower cost repatriation operation in many cases, and would be essential to deal with the collapse of a large UK airline. The full advice from Steer can be found alongside this report at Annex F.

## Current ability to keep a fleet flying

**6.8** There are a number of issues which could influence the ability to arrange an organised wind down of an airline at the point of insolvency. These will vary depending on the unique commercial situation of the airline involved, its structure and how it exits the market.

In the Interim Report we identified that several UK and European airlines have exited the market in recent years with markedly different outcomes<sup>14</sup>.

**6.9** In the UK, the practice of operating an airline in administration is rare, though not unheard of. The Interim Report discussed the most recent example of Paramount Airways, a UK registered airline, which failed in the peak summer holiday season in 1989. While there was some success in keeping the airline flying for a short period, the costs and operational issues were significant. In particular, it highlighted the potential for creditors in the UK and overseas to frustrate the operation by detaining aircraft, and demanding payment for their release.

**6.10** More typically, airline insolvencies in the UK have led to an immediate cessation of operations and grounding of the fleet when the airline enters administration.

<sup>14</sup> See page 7 of the Interim Report, available at [www.gov.uk/government/publications/air-insolvency-review-interim-report](http://www.gov.uk/government/publications/air-insolvency-review-interim-report)

In the Interim Report we described the failure of Monarch airlines, which collapsed into administration leaving 110,000 passengers stranded overseas. In that case, the CAA and UK Government stepped in to provide charter services to successfully repatriate Monarch's passengers. This was largely paid for by taxpayers and the Air Travel Trust (for ATOL protected passengers), though some contributions were also received from credit card providers and large tour operators.

**6.11** In contrast, the sale of British Midland International (BMI) in 2011, provided an example of a less typical approach to the potential wind-down of an airline. This involved collaboration among CAA, BMI's management and the parent company to make plans for an organised wind-down of the airline if a sale had not been possible. In that situation the contingency plans were not needed and therefore were untested. However, it did demonstrate that, in some circumstances, UK airlines can take steps to prepare for their own failure and minimise impacts on their customers.

## Challenges for the Coordinating Body

**6.12** The range of examples above demonstrates that it is not always possible to predict whether an airline will exit the market, how it will do so, and the timescales in which it will play out. This would present the CAA with some key challenges, both as a Coordinating Body and as the UK's licensing authority. While the CAA do have ongoing oversight of UK airlines through the airline operator licencing (AOL) regime, they have limited control over the following aspects:

- **The timing of insolvency.** The timing will depend on a variety of factors, though it is often determined by the directors concluding that the company is insolvent and may no longer trade

lawfully. There is currently a requirement for ATOL holders to notify the CAA when they seek advice from an Insolvency Practitioner (IP), however a similar requirement does not exist within the AOL. This means that CAA may not always have the notice they need to make effective contingency plans when an airline becomes insolvent.

- **The type of insolvency.** At the point of insolvency, the company will cease trading and its fleet will be grounded unless the administrator is satisfied that it is feasible and would be in the interests of creditors to continue to operate (for example, where sale as a going concern is in prospect). In some circumstances the company may be placed into liquidation and the winding-up immediately commenced, which may prevent access to key services or staff in the company
- **The degree of cooperation from the airline in preparing for their own failure.** At present the directors of an airline do not have a specific duty to repatriate passengers stranded overseas. This means that when an airline is in financial distress their focus is likely to be on the interests of creditors as a whole to whom they will owe their principal duty, rather than on the protection of their passengers.

- 6.13** The absence of any specific controls over the above factors can make it difficult for CAA to prepare for an orderly wind down and repatriation. The cooperation of the airline's directors, management and advisors is essential to ensure there is a smooth transition to any repatriation operation after an airline becomes insolvent. This co-operation is needed to ensure the CAA have sufficient notice about insolvency plans and timing, and access to information

that is essential to the repatriation (e.g. passenger data, and details about suppliers/creditors).

## Operating an airline in administration

**6.14** The CAA's ability to coordinate a repatriation using an airline in administration requires several key elements to be in place. These are summarised in Figure 6.1, and discussed in more detail in the remainder of the chapter. These elements are essential, whether an airline is operating in administration or under normal trading conditions, as any disruption will potentially lead to delay, additional cost or even impede the airline operation entirely.

**6.15** This would require co-operation from several parties, both in the UK and overseas, who may not be incentivised or compelled to do so under the UK's current insolvency regime. This includes the airline's key suppliers and major creditors including their financing partners, secured creditors and trade creditors (for

example, fuel suppliers and ground handling suppliers).

**6.16** The insolvency event is also likely to result in a change in the control of the airline, with the appointment of an IP to act as administrator or receiver. The Coordinating Body, the IP and the airline's management will need to work together to manage this transition and ensure the insolvent airline can continue to operate. This will also require the retention of key staff to ensure the safe operation of the airline.

**6.17** Typically, airline insolvencies in the UK have led to an immediate cessation of operations and grounding of the fleet. This is primarily because the repatriation of passengers would be loss making (and carry very large risks for the estate), which is contrary to the objectives of administration or liquidation in the UK. The insolvency can also lead to an immediate loss of key employees, systems and suppliers, and trigger the withdrawal of the airline's operating licence by the CAA.

Figure 6.1: Trading Essentials

Trading essentials: The operation of an airline requires several key elements to be in place, including those below. For an airline to keep flying in administration, several parties would need to support the operation.							
 <b>Management</b> The airline needs to be in the hands of an Insolvency Practitioner and/or Board willing and able to undertake a repatriation exercise.	 <b>Key employees</b> and systems need to be retained to ensure smooth and safe operation of an airline in administration.	 <b>Regulatory compliance</b> is needed to maintain an Operating Licence and Air Operator Certificate and comply with other regulatory requirements.	 <b>Insurance</b> will need to be in place to cover potential liabilities as an airline and a business.	 <b>Airports</b> Airport charges are levied on a range of services, including take off and landing. If these are unpaid the airport may seek to exercise a lien and impound aircraft.	 <b>Aircraft</b> Most airlines lease aircraft and engines from lessors. The lessors may seek to exercise a right to terminate the lease for default.	 <b>Key suppliers</b> Including air traffic management, fuel, ground handling and maintenance suppliers. They may seek to withhold services, or detain aircraft for unpaid charges.	 <b>Sufficient working capital</b> Regardless of the source of funding, it is essential that liquidity is provided swiftly to allow the airline to operate in administration.



### Management of airline operations in administration

**6.18** Where all these elements can be secured, it might be possible for the repatriation services to be carried out by the airline under the control of a court appointed administrator (or equivalent), by the directors under a debtor in possession regime, or by a receiver or other agent of the creditors.

**6.19** While there are several precedents overseas where airlines have operated during a formal insolvency process, these have generally been where a rescue or restructuring process was being attempted, rather than simply as a means to support a repatriation operation. These are often facilitated by debtor in possession bankruptcy regimes, where the directors of the company, rather than an administrator (or other judicially appointed

officer), remain in control (for example, under Chapter 11 of the US Bankruptcy Code). Chapter 11 provides protections from creditor action and other mechanisms to facilitate restructuring of the business (including access to finance). These elements help to support continuity of service using the airline's existing infrastructure.

**6.20** The failure of Air Berlin in Germany provides a recent example where a large airline was able to continue operating in administration while the company was restructured and ultimately wound down with the profitable parts of its business sold to other carriers. Air Berlin filed for insolvency on 15 August 2017 under the German insolvency regime, and continued operating services until October 2017 with substantial financial support from KfW, a state-owned institution, before it was

## Air Berlin Case Study

Air Berlin was a large German registered airline with a fleet of over 140 aircraft, which operated a range of short, medium and long-haul services. It entered administration on 15 August 2017 after Etihad, Air Berlin's main shareholder, withdrew its financial backing for the loss-making company.

Faced with a sudden failure, the German Government agreed to grant a €150m bridging loan to Air Berlin, which was provided through a credit facility from the German public credit institution KfW. The purpose of the loan was to allow Air Berlin to continue its operations for a short period while it concluded ongoing negotiations to sell its assets before it exited the market. The German Government anticipated that the loan would be repaid in full as it was secured against the expected proceeds from the asset sales, which had a reasonable prospect of value realisation.

The restructuring plan and loan were also agreed by a panel of key creditors before the company went into administration, which allowed Air Berlin's Directors to continue trading and operating the airline in administration with lower risks of creditor action. This was also supported by an administration regime which permits a debtor in possession approach to administration. The airline was still able to sell tickets to consumers during the administration period, however the money raised from these sales was protected in an escrow account until the service was delivered.

Air Berlin's aircraft continued flying until 27 October 2017, and the airline continued operating services through other carriers until the company finally exited the market in January 2018. During that period the Directors managed an orderly wind down, completing the sale of several assets and the transfer of some operations and staff to other carriers. It has been reported that a proportion of the loan has been repaid, though the full amount may not be recovered after a deal to sell parts of the airline to Lufthansa fell through.

finally wound down in January 2018. The case study box above summarises some of the key lessons from the orderly wind down of Air Berlin.

**6.21** For any company facing insolvency in the UK, the control of the company is likely to change. In some circumstances, the Board of Directors may maintain control for a period while they attempt to secure a sale or restructuring of the business, but potentially under changed obligations to business as usual. Under formal insolvency proceedings (administration or liquidation), an IP is appointed to take management control of

the company and secure the best outcome for creditors and members through a sale, restructuring or liquidation of the business.

**6.22** We have worked with Reed Smith and Steer to consider the applicability of options for keeping an airline flying under UK insolvency legislation. Their advice suggests that administration is likely to be the most feasible way to keep an airline fleet flying in the UK. This is because it brings with it a moratorium which allows for some level of EU recognition and it also avoids some of the disadvantages of the other options. However, they also suggest there are significant challenges with all the

options. Steer suggest these challenges may well be impossible to overcome without a significant amount of money, or specific interventions to modify the terms under which an airline insolvency takes place in the UK.

**6.23** One common theme of all of the options under UK insolvency legislation is the potential personal liability of the individuals entrusted with running the airline. Directors of an airline do not have a specific duty to look after their passengers at the point of insolvency. Indeed, they are compelled not to treat them more favourably than other creditors. They would be at risk of incurring a liability for wrongful trading if they chose to operate repatriation flights outside of formal insolvency proceedings, when they have taken a decision that the airline is no longer solvent and continuing such flights would prejudice the position of creditors.

**6.24** In August last year, the government announced plans to update the UK's insolvency regime<sup>15</sup>. This will introduce new tools that could improve the rescue, or restructuring opportunities for financially distressed airlines. These include a moratorium to provide space for distressed but still viable businesses to consider opportunities for rescue. As this moratorium would only be available in some circumstances, we do not consider it could be relied upon to support a repatriation using the airline's fleet.

**6.25** The continued operation of an airline could also be inconsistent with the duties of an IP appointed as administrator or liquidator, as their statutory duties require them to achieve the best outcome for creditors. A repatriation exercise is likely to be inconsistent with this duty, as in many

cases it would not generate revenues to offset the associated costs, eroding prospective returns to creditors. Moreover, airline operations intrinsically carry major risks (from impounding of the aircraft to accidents or even terrorism). IPs can become personally liable in some circumstances, and while some insurance to cover this is possible, not all risks can be easily or affordably insured against (e.g. reputational risk or some risks relating to health and safety).

**6.26** In their report, Steer propose several interventions in order for a repatriation exercise to be undertaken in insolvency, including (see Annex F):

- the “purpose” of the administration needs to go beyond the normal duties of administration; and
- more specifically, a special regime is needed to place the airline’s fleet and other operations under the control of a suitably qualified administrator to allow for repatriation.

### Airline staff

**6.27** Airline staff are crucial to the continued operation of an airline. Many staff have particular skills, and associated licences, which mean that the possibility of operating the airline without such staff would be very difficult. Key personnel, including the Accountable Manager and Safety Manager need to be in place to allow the Air Operator Certificate (AOC) to be maintained. The retention of key staff is therefore likely to be a key consideration for any IP tasked with running the airline.

**6.28** The need to retain staff means that compulsory liquidation is a less viable option, as that would lead to the automatic dismissal of all staff. Other models, including provisional insolvency,

<sup>15</sup> New tools to improve rescue opportunities for financially distressed companies (published 26 August 2018) – [www.gov.uk/government/news/new-tools-to-improve-rescue-opportunities-for-financially-distressed-companies](http://www.gov.uk/government/news/new-tools-to-improve-rescue-opportunities-for-financially-distressed-companies)



administration and a director-led operation do not automatically terminate employment contracts and therefore appear more viable from this perspective.

**6.29** Nevertheless, it is likely that staff attrition in such a situation could still be high, since staff would be motivated to look for alternative employment. Therefore, the key requirement to ensure staff are available for a repatriation exercise is that funding is available to pay salaries and benefits, and that staff are given convincing reassurances that they will be paid. This is perhaps most straightforward under an administration, where staff salaries are treated as expenses of the administration to be paid ahead of most other debts.

### Airline licensing

**6.30** An airline would still need to comply with airline licensing regulations when it is operating under administration. For a UK carrier, this would mean holding a valid Operating Licence (AOL) and Air Operator Certificate (AOC) granted by the CAA in accordance with the UK's licensing framework (ORS1)<sup>16</sup>. As airlines cannot

operate without these licences, it is important to understand the circumstances under which they may be withdrawn in an insolvency situation.

**6.31** The current legal basis for the licensing regulations is in Regulation (EC) 1008/2008, which sets the rules for the operation of air services in the European Economic Area (EEA)<sup>17</sup>. In order for an airline to be granted an Operating Licence for the first time, strict financial criteria are applied and a test of "good repute" is applied to the managers (in particular, that they have never been bankrupt). In order to retain the AOL the carrier would also need to:

- hold an Air Operator Certificate (AOC);
- have adequate financial resources to meet its obligations; and
- have passenger liability and third-party insurance (discussed later in this chapter).

**6.32** The ability for an airline to continue operating in administration is therefore critically dependent on its ability to retain

<sup>16</sup> Licensing Airlines in the UK: the framework and criteria for granting Operating Licences, Route Licences and Air Transport Licences (ORS1) – Civil Aviation Authority

<sup>17</sup> <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2008:293:0003:0020:EN:PDF>

its AOC. The CAA would need to be satisfied that the operator remains competent to secure the safe operation of the aircraft. This is likely to require that key personnel, systems and processes are maintained to ensure safe operations. This in turn is dependent on sufficient funding being available to cover the costs of maintaining these safety-critical elements in administration.

**6.33** The regulations relating to financial resources could also lead to the revoking of an AOL, although there is some flexibility. There are requirements for continuous monitoring of the airline's financial health. In situations where financial problems clearly exist or when insolvency proceedings are opened, the CAA would need to assess the situation without delay and review the status of the operating licence within three months. If the CAA were no longer satisfied that the operator can meet its obligations for a 12-month period, they would need to revoke or suspend the AOL. Alternatively, they could grant a temporary licence (up to 12 months) if they were satisfied that safety is not at risk, and there is a realistic prospect of a satisfactory financial reconstruction within that time period.

**6.34** The CAA acknowledges the implications of these provisions in ORS1, stating that:

*"The CAA ... may in certain circumstances take action to revoke an Operating Licence. Its objective in doing so is primarily to secure a better outcome for the travelling public, and revocation will in many cases not have this effect: revoking a licence will turn a potential failure into an actual failure and may lead to losses on the part of ticket holders and disruption to passengers' travel plans."*

**6.35** We note that in the Air Berlin case, the German licensing body (das Luftfahrt-Bundesamt, Federal Aviation Office) did suspend the operating licence. This was then immediately replaced with a temporary licence, which allowed Air Berlin to operate after its bankruptcy. Licensing decisions will need to be taken according to the specific case and the facts. However, it appears that it would be possible for CAA to take similar licensing actions, to temporarily preserve an airline's ability to continue operating its flights in administration.

**6.36** We discuss airline licensing later in the chapter, including whether the UK's licensing regime could be adapted to help put a failing airline onto a path towards recovery or an orderly wind down.

## Aircraft, airports and air navigation

**6.37** Aircraft are particularly vulnerable when an airline is in administration. They are often owned by and leased from third parties (lessors) who will want to get hold of their expensive assets as quickly as possible to put them back on to the market. In operating repatriation flights it will be necessary to fly these aircraft between UK and overseas airports, where there is a risk they could be detained for unpaid debt. This represents a significant delivery risk, which has the potential to delay or increase the costs involved in keeping the fleet flying. In considering this issue, it is important to look at the ability to retain leased aircraft and other suppliers in administration, and also the potential for creditor action at airports.

## Retaining leased aircraft in administration

**6.38** All of the major UK airlines lease some or all of their aircraft from lessors or finance them with loans from banks (or other lenders) who take a security interest in them. The Interim Report noted that

these will generally be underpinned by agreements containing termination clauses. The Steer report has identified particular clauses that could be triggered following the insolvency of the airline (for example, relating to default of payment). These are placed in the contract to manage the risk of non-payment by the lessee, or seizure of the lessor's asset by another creditor.

**6.39** Normally, entry into administration would provide for an automatic moratorium on legal actions, including those that can be taken by a lessor. However, Reed Smith have advised that this open-ended moratorium does not extend to the aircraft leases, as these are instead covered by the Cape Town Convention, to which the UK is a signatory. As the convention is an international treaty implemented into UK law, it has primacy over the contractual terms in individual lease agreements.

**6.40** The UK has adopted a particular option in respect of insolvency regimes within the Convention ("Option A"), which means that the lessee must give up the aircraft to the lessor or cure all debts by the end of a "waiting period" of 60 days. The lessor can repossess the aircraft after the waiting period without any further legal intervention. In Reed Smith's opinion, this provides lessors with more confidence in the outcome, such that they may be less inclined to seek to repossess an aircraft at the first signs of distress. This may therefore facilitate operation of an airline for a short, time-limited period during insolvency to undertake a repatriation operation.

**6.41** In stakeholder workshops we explored whether lessors would be willing to continue to make their aircraft available for the duration of a repatriation. There was general support for this in principle if

they could be assured that they would not be unfairly prejudiced as a consequence. At a basic level, this includes ensuring that the lessor will receive payment for any ongoing leasing costs incurred during the repatriation and that the terms of lease agreements continue to be met, in particular in relation to maintaining the condition of the aircraft. Some also indicated that they would want their assets to be returned to an airfield of their choice, and that any debt asserted against the aircraft during the administration period should be paid by the administrator. This latter point is discussed in more detail below.

### Retaining other key suppliers

**6.42** When an airline fails they are likely to leave unpaid airport charges (typically landing and parking charges and passenger terminal charges), relating to the airport's "Conditions of Use" contract. Airlines are also obliged to pay the air navigation service providers (ANSPs) at the airports it is flying from, and for the countries it flies over. If the airline is unable to pay these, the airport could deny access to the airline's aircraft or may prevent the aircraft from departing until debts are paid. ANSPs and airports can take actions to ensure that payments are made by placing a lien on the aircraft and holding the aircraft until the debt is paid.

**6.43** While entry into administration leads to a moratorium on creditor action against the airline and its assets, this only applies automatically in England and Wales. The moratorium can in principle also be enforced in other EU states and a number of other countries under the mutual recognition arrangements currently in place. It would, however, be necessary to obtain a court order in states with whom the UK does not have mutual recognition treaties (and potentially in some with whom it does) to prevent such actions

being taken there. There is therefore a risk that aircraft could be detained in overseas airports until a court order is made or the debts are paid, which could lead to increased cost and delays for a repatriation operation.

**6.44** In addition to airports, both the CAA and Eurocontrol (the coordinator of ANSPs across Europe) are able to impose tail or fleet liens in cases when their charges are not paid. The Eurocontrol fleet lien is a power that is unique to the UK CAA. It is rarely used, but it does have the potential to involve significant costs to individual lessors, which are not necessarily connected to their own aircraft. This naturally means that lessors are particularly wary about their assets being detained at UK airports when an airline enters administration. They would normally mitigate this by requesting their aircraft are returned to a neutral airport outside the UK at the point of administration, or by negotiating a return of the asset with the UK airport before a fleet lien is applied.

**6.45** Where there is no unpaid debt, airports may still refuse to allow access or departure, unless fees for continuing usage are paid in advance. Similar

considerations also apply to other service providers. All airlines need to purchase fuel from aviation fuel suppliers and many airlines, particularly away from their main airport bases, rely on third parties to undertake aircraft handling and maintenance checks. It is highly likely that the airline's supply contracts with these organisations include termination clauses triggered by insolvency (in a broad sense, not just on entering into formal legal processes). Therefore, such suppliers will be under no obligation to provide services on existing terms, and can be expected to demand advance payments for future supply of fuel, ground handling or maintenance services.

**6.46** More generally, the prospect of an insolvency is likely to lead to an overall 'tightening' in the supply chain as suppliers become concerned about the payment risk around the airline. This may lead to demands for prepayment or a refusal to supply. This places extra emphasis on the need for any liquidity and funding mechanism (discussed in Chapter 8) to be seen as a 'cast-iron' agreement to pay on a full and timely basis. This is likely to be necessary to keep the supply chain operating smoothly through the repatriation.



## Insurances

**6.47** Airlines are also required to hold insurance in order to operate. Indeed, the Airline Operating Licence is dependent on holding a requisite level of insurance under the Licensing Regulation (1008/2008) and, more specifically, in Regulation (EC) 785/2004 “on insurance requirements for air carriers and aircraft operators”. In the Interim Report we indicated that some insurance contracts may include termination clauses relating to insolvency. Steer have considered this further, and have advised that in most cases it can be expected that insurance would continue to be available to an airline which has:

- a valid Airline Operator Certificate, which relates to air safety;
- a valid Operating Licence (including a temporary Operating Licence issued after insolvency); and
- sufficient funds to continue to pay premiums.

**6.48** In Steer’s view, if these matters have been successfully managed, then a lack of insurance is unlikely to be the reason why an insolvent airline was unable to continue to operate, and in particular, to undertake a repatriation exercise. Whilst existing insurance arrangements should remain in place, it may not be adequate to protect the insolvent estate or the IP from all risks, as noted in paragraph 6.25 above.

## How to Keep the Fleet Flying in summary

**6.49** Our review of the ability to keep the fleet of an insolvent airline flying suggests that it would be feasible in the UK, but only if some significant challenges can be overcome. In contrast to many other jurisdictions around the world, the UK does not at present have all of the necessary mechanisms to enable airlines facing insolvency to wind down and repatriate their passengers in an orderly

fashion even with the protection of formal insolvency proceedings. Our work with Steer and Reed Smith indicates that the challenges can be overcome with modifications to the following aspects of the current regime:

- the development of a Special Administration Regime (SAR) for airlines, which would enable an insolvent airline to continue to operate its fleet for a limited period to bring home passengers who would otherwise be stranded;
- changes to the UK’s regulatory regime to allow airlines to operate in administration, and to provide the CAA with greater oversight of airlines in distress and more tools to affect the outcome; and
- more than any other type of repatriation operation, keeping the fleet flying will require immediate access to a source of liquidity. In Chapter 8 we set out our recommended structure to achieve this.

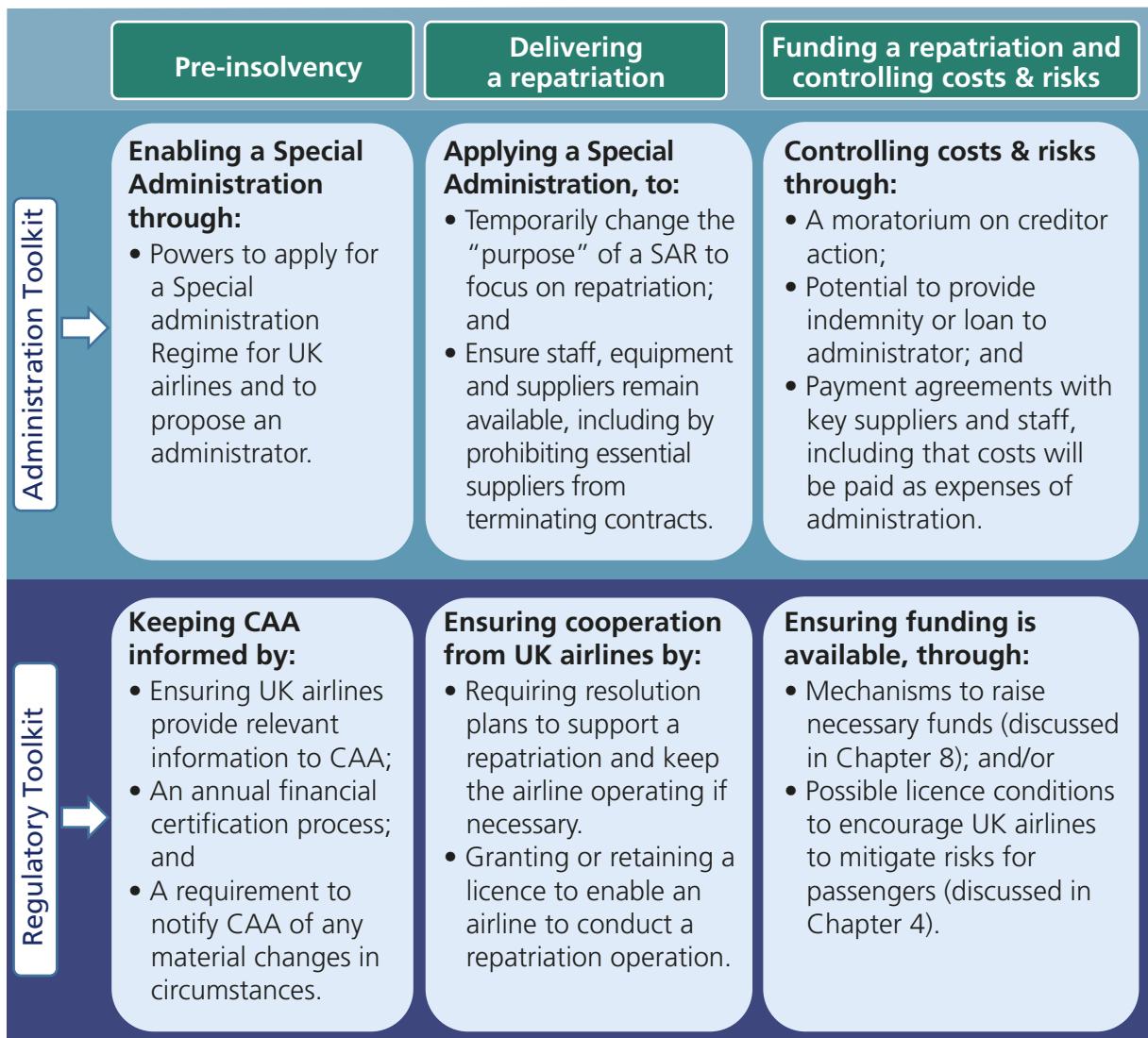
## Improving the ability to Keep the Fleet Flying in Administration

**6.50** In considering the ability to repatriate passengers using an airline’s own fleet in administration, we have identified the following key challenges:

- the inability for CAA to control the timing of airline insolvency;
- the misalignment between directors’ and an administrator’s duties and the purpose of repatriating passengers;
- the need to retain key airline staff to operate the airline following insolvency;
- the need for the airline to continue to hold an operating licence;
- the need to retain the freedom to use aircraft that are leased or mortgaged and for them not be re-possessed by

- lessors or mortgagees nor detained for lengthy periods by creditors;
- the need to retain access to airports and air navigation services and to retain key supplies (such as aviation fuel supplies and ground handling services).
- 6.51** In order to address these challenges when a UK airline is facing insolvency, we propose modifications to the UK's airline insolvency and licensing regimes. This would provide an improved ability to manage deficiencies in the following areas:
- Pre-insolvency** – improving the CAA's ability to enable an orderly wind down of an airline and ensure it is in the hands of a person or persons willing
- and able to undertake a repatriation exercise;
- Delivering a repatriation in administration** – ensuring essential staff and suppliers remain available to operate safely and effectively;
  - Funding a repatriation** and controlling risks and costs.
- 6.52** We consider that a Special Administration Regime (SAR) and enhanced regulatory toolkit will be needed to address constraints in these areas and improve the ability to keeping a fleet flying. An illustrative summary of the potential interventions can be seen in Figure 6.2. These interventions are discussed in more detail below, and in

**Figure 6.2: Keeping the Fleet Flying – potential interventions**



the section covering enhancements to the licensing regime.

**6.53** It is important to be clear that there would be no ability for authorities in the UK to keep the fleet of an airline established in a foreign country flying were it to fail, so this mechanism can only be applied to UK airlines. The failure of any airline incorporated and licensed in another state would be the concern of the authorities in that other state. Where such a failure would impact significant numbers of UK-originating passengers, the CAA could be restricted in its ability to intervene effectively to ensure their repatriation.

## Elements of a Special Administration Regime for airlines

**6.54** We recommend the introduction of a SAR for airlines, which would support the continuation of services and a repatriation if necessary. We suggest the regime could be designed to include the following elements and supplementary measures, which have similarities with SARs in other sectors.

### Amending the purpose of an airline administration

**6.55** We consider a SAR is necessary to amend the primary purpose of airline administration to include a specific duty for the administrator to undertake a repatriation exercise. This would temporarily align the role of the administrator with the purpose of repatriation, and ensure duties to creditors do not over-ride this. This would eliminate ambiguity and address any concerns that an administrator may otherwise have that they would be acting out of line with their primary duties. Once the repatriation is concluded, the administrator would then proceed in effect as if it were a normal administration.

There would need to be a clear cut-off point between the SAR and normal administration, and a mechanism to allow the settlement of expenses incurred by the administrator as part of the repatriation operation.

### Opportunity to introduce a Special Airline Administration

**6.56** It would also be necessary to include powers to trigger the SAR when considered appropriate, given that normal administration procedures would still otherwise apply to an insolvent airline. This could include a restriction on seeking an administration or winding-up order or the appointment of an administrator under a floating charge until the Secretary of State has been provided with 14 days' notice of the intention to do so. This would create a window of opportunity to ensure the CAA has notice to prepare for a failure and avoid a sudden and unexpected collapse, while also providing an opportunity to apply for an airline SAR order if that course is chosen. If the airline has been co-operating effectively with the CAA in advance, then the full 14 day notice period may not be needed.

### Appointing the Airline Administrator

**6.57** It would be essential that the Airline Administrator has the necessary skills to oversee the management of the repatriation exercise, which would be undertaken by airline management and staff. This could be ensured by providing the Secretary of State with the opportunity of proposing the Airline administrator. It would be possible to select the administrator from a panel of IPs, who have been pre-approved by the Coordinating Body on the basis that they are able to meet the requirements. The Airline Administrator should be required to cooperate with a Coordinating Body in delivering the repatriation exercise.

**6.58** Changing the purpose of airline administration will provide some comfort to IPs appointed as Airline Administrators that they cannot be held liable for additional debts that arise from the repatriation exercise. However, it may not entirely address their concerns around potential liability from operating the airline, particularly for any risks that cannot easily or affordably be insured against. It may be possible to reduce the risks significantly where the existing management team are retained and the operator's usual policies and procedures in areas, such as health and safety, can be continued under the supervision of the administrator. It would also be possible to mitigate some risks further by way of professional indemnity insurance, if an appropriate policy were available.

**6.59** In other SARs there are also powers for a Secretary of State to provide a grant, loan, or indemnity to administrators appointed under these regimes, in order to provide comfort that they will not be held personally liable for continuing a particular service. We consider a similar power should be included in an airline SAR, to be exercised at the Secretary of State's discretion having regard to the circumstances of the given case.

### Retaining key suppliers and staff

**6.60** During the 14-day window, and in any special administration period, it would be essential for the airline to retain the key elements that allow it to operate as an airline. This makes it necessary to introduce powers to prohibit essential suppliers (e.g. aircraft lessors and fuel suppliers) from terminating contracts and demanding 'ransom payments'. This would need to be in place both during the 14-day window, and during the repatriation process.

**6.61** A key concern for suppliers and employees will be whether they will receive payment for their services during the administration period. They may require payments to be made in advance, or as an expense of the administration. Under the Insolvency Act 1986 expenses properly incurred by the administrator in the conduct of the administration are by definition expenses of the administration and may be paid out of the insolvent estate in priority to the generality of unsecured and some secured creditor claims. In other SARs there is generally an express confirmation that any expenses incurred by the administrator in pursuit of the SAR can be treated as expenses of the administration. In the absence of a dedicated source of finance, this would be likely to provide comfort to staff or suppliers retained to deliver a SAR, as it would mean their wages or fees could be paid as super-priority payments in advance of almost all other creditors of the company. It may also be necessary to provide additional incentives to ensure key employees are retained, and the administrator may need to make staffing contingency plans to cover gaps created by attrition that may have occurred.

### Restricting creditor action

**6.62** The SAR could also introduce a moratorium to stop creditors from seizing airline assets, particularly aircraft, which would otherwise hamper a repatriation exercise. This is similar to the statutory moratorium that already exists under the standard administration regime when a notice of intention to appoint administrators is filed. This would need to be in place both during the 14-day window, and during the repatriation process.

**6.63** The challenge will be in ensuring a moratorium is recognised by creditors overseas. At present, insolvency



procedures in the UK are recognised by the courts of other EU Member States. A number of jurisdictions (including the UK and USA) have also adopted the United Nations model law on cross-border insolvency, which provides similar recognition of overseas insolvency procedures. Where recognition exists, the process by which an administrator may obtain a court order confirming the moratorium is simplified, however it will still be necessary to obtain a court order from the jurisdiction in which the assets are located in order for the moratorium to be recognised.

**6.64** Experience in other jurisdictions (including Germany and USA) shows that airlines operating in administration are able to function across borders largely unhindered by creditor action. In the case of US airlines, this is partly effective because of the nature of Chapter 11 protection<sup>18</sup> and extra-territorial jurisdiction of the US courts, enforced by the application of contempt of court orders against overseas creditors who disregard the moratorium, which can be

enforced against any asset or officer of the creditor that is present in the USA. However, even in Chapter 11 proceedings, ransom claims from overseas creditors often have to be addressed by settling the claim, because of the delays or difficulties associated with seeking to enforce through the local courts.

**6.65** The ability to control creditor action is a particular concern for lessors, given the potential limitations to the effectiveness of the moratorium and the opportunity for creditors to assert liens on their assets. As such, an airline SAR should also include provision for the following elements:

- The administrator must be responsible for discharging or dismissing any liens asserted against the aircraft during the administration period (for example by foreign airports not under the jurisdiction of the UK courts, and therefore not bound by the terms of the SAR). This would include liens relating to the operation of the aircraft before the administration.

<sup>18</sup> Chapter 11 of the US Bankruptcy Code relates to reorganisation of a business. For more see:

<https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-11-bankruptcy-basics>

- The moratorium under the SAR should explicitly extend to statutory detention powers (e.g. by Eurocontrol) as well as other creditor actions.
- The terms of lease agreements must continue to be met, and lessors must be given the opportunity to receive their aircraft at an airfield of their choosing before the special administration is brought to an end, so as to prevent a fleet lien being exercised at that point.

### Liquidity and funding issues

**6.66** It is clear from our work with Steer that the key requirement to ensure a successful repatriation exercise is adequate liquidity being available. This is particularly relevant when attempting to keep the fleet flying, to ensure that aircraft lease rentals and other payments can be made to equipment owners, airline staff, airports, air navigation service providers and other key suppliers.

**6.67** Regardless of the ultimate source of funding, it is essential that sufficient liquidity can be provided swiftly and be available following any airline failure (UK or foreign). To achieve this, the Review intends that passengers (via their airline) pay for their own protection in advance, the detail of which is discussed in Chapter 8.

**6.68** As set out above, some features of a SAR could adversely affect the rights of an airline's suppliers and other creditors. This may have the effect of making it harder, or more expensive, for UK airlines to obtain supplies or raise funding particularly when their financial position is deteriorating. As our intention is to see funding for repatriation costs provided in advance of failure, we do not recommend adoption of the approach from other SARs whereby returns to creditors and shareholders are reduced by the expenses of the administration arising from fulfillment of

the special repatriation purpose having first claim on any assets of the insolvent estate. This should mitigate this risk, and based on our discussions with several stakeholders, facilitate cooperation with an airline SAR.

**6.69** Putting in place a financed organised repatriation scheme could however, present an incentive for creditors who provide essential supplies to make ransom claims, in the knowledge that the administrator will have access to funds from the scheme. This risk can be mitigated where the creditor is within the reach of the UK courts, enabling effective enforcement of the moratorium.

**6.70** Creditors beyond the reach of the UK courts would not be similarly constrained, which may lead to increased costs. The Coordinating Body will need to take this risk into account when assessing the most efficient mechanism to adopt when planning repatriation operations.

## Improving the airline regulatory framework to allow an orderly wind down

**6.71** CAA's existing licensing framework provides for the financial regulation of UK airlines. However it is not designed to support the repatriation of passengers when airlines do fail. This section identifies changes to the UK's airline licensing regime that would assist the CAA in managing airline failures and delivering a repatriation exercise. This is based upon our work with Steer and the CAA, and the discussions we have had with other stakeholders throughout the review period.

**6.72** The proposals described below take on board elements of good practice seen in other regulated sectors. None of the

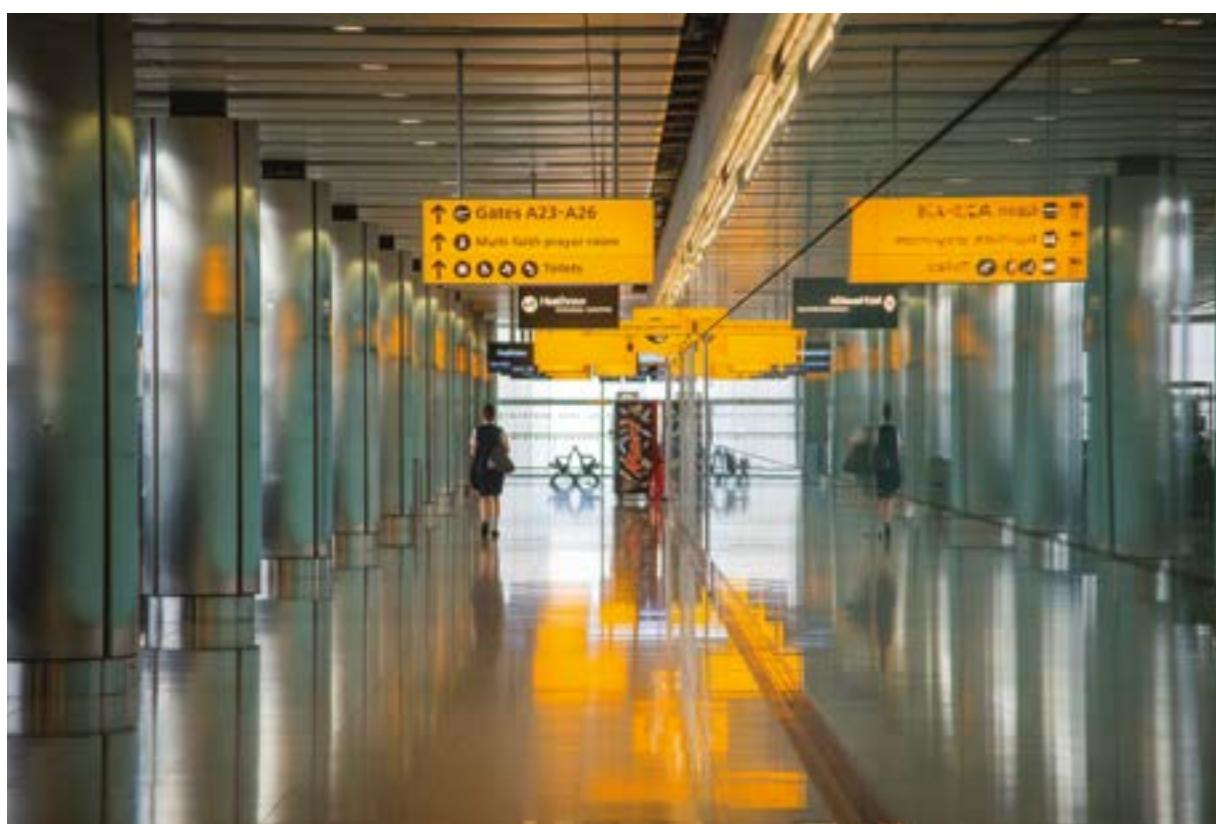
interventions are currently at the disposal of the CAA through the airline licensing regime, though similar tools are currently available to it relating to tour operators through the ATOL scheme. The overall purpose would be to enhance the CAA's regulatory toolkit to improve their oversight of airlines and encourage appropriate financial discipline. Other parts of the toolkit are designed to encourage an airline to prepare for its own failure and improve the deliverability of a repatriation, whether that is through keeping the fleet flying or the other means described in Chapter 5.

**6.73** Like the SAR, these proposals would only apply to UK-licensed airlines, so they would not be effective for monitoring or managing problems of overseas airlines. As the changes have the potential to place new regulatory burdens on UK airlines, this might have some impacts on competition in the market. We judge that the regulatory impacts for most of the interventions would be manageable and quite small. For others, the impacts and potential for market

distortion would be greater, particularly if conditions are used to require UK airlines to mitigate the cost of their own failure. These issues are described below. A more detailed assessment of the impacts would be needed before these measures are introduced.

**6.74** In our considerations, we have assumed that any changes to the licensing framework would need to remain consistent with the existing EU Licensing Regulation (EC 1008/2008). We understand there is flexibility in these regulations surrounding how financial assessments can be implemented by competent authorities. This would allow some discretion to introduce new requirements into the UK's regulatory framework, which could include:

- setting minimum financial requirements for UK carriers to satisfy;
- requiring UK carriers to develop and provide 'Repatriation Plans' which set out information required to repatriate passengers; and



- requirements that provide the CAA with more visibility of a UK air carrier's financial position, or which might be necessary to implement any repatriation plan.

## Proposed improvements to the licensing toolkit

**6.75** Through its licensing activities the CAA currently monitors the financial health of airlines on an ongoing basis and will increase its monitoring for individual airlines if they appear to be entering financial distress. If necessary, the CAA can act to revoke the Operating Licence but this can be a protracted and very much a 'last resort' option. So, while the regime does allow for proactive monitoring and a gradual ramp up of information provision, it does not provide the powers for CAA to flexibly and proportionately intervene when there are signs of material financial distress in a UK licensed airline.

**6.76** We recommend government works with the CAA to introduce a more complete regulatory toolkit, to allow CAA to manage a failure more effectively. This would bring the airline industry more closely in line with other sectors (e.g. financial services) that have introduced regulatory requirements to mitigate consumer harm from financial failure. We recommend the regulatory toolkit should include the following measures, entrenched in the Operating Licence, which we consider would represent a proportionate response to the risks involved:

- Annual certification to confirm financial fitness;
- Development of repatriation plans and access to data as required;
- A requirement for a Board of a UK airline to notify CAA when there is a material adverse change in its financial situation;

- The ability to grant a temporary special purpose licence to enable an airline to conduct a repatriation operation, even where the airline does not have a future.

**6.77** In addition, the CAA have also indicated that it would be helpful to have the ability to:

- make licence conditions that direct a UK carrier to mitigate future passenger risk; and
- sanction the Directors of UK carriers for non-compliance.

**6.78** While there may be merit in both of these measures from a regulatory perspective, they may go beyond what is necessary to provide an appropriate level of protection for passengers. They have the potential to introduce significant burdens for the individuals and entities concerned, which we have not been able to assess. We do not, therefore, feel able to make a specific recommendation, though we would suggest further work is carried out to consider how they fit with Better Regulation principles.

## Certificate of financial fitness

**6.79** This would require the Board of each UK airline to provide the CAA with an annual certificate of financial fitness for the next 12 months, in accordance with the requirements of holding an Airline Operator Licence (AOL). At present the CAA do not include an annual touchpoint with the airline as a hardwired feature of the operator licence. We consider an annual certification process would concentrate minds in boardrooms about financial adequacy and discipline on an annual basis and not only in relation to the initial application process for the AOL. This would need to be based upon the latest financial data. In other sectors where such certification is in place, the

## Financial certification and intervention plans for energy network operators

Ofgem requires that the licensees must at all times have sufficient resources (financial and personnel), assets, rights, licences, consents and facilities to properly and efficiently carry on the regulated business.

The Regulator requires the licensees to provide a Certificate of Financial Resources (by 31 July each year) signed and approved by the Board of Directors. This confirms that after the payment of dividends, the Board have reasonable expectations that they will have sufficient financial resources to carry on the regulated business for a period of 12 months from the date of the Certificate.

The Certificate of Financial Resources must be accompanied by the following:

- A statement of the main factors that the Board have taken into account for assessing the sufficiency of the financial resources;
- The main financial resources and financial facilities available to the licensee;
- The most recent cash flow statement; and
- The auditor's report confirming the financial resources or detailing any inconsistencies between the Certificate of Financial Resources and the statement submitted with it.
- In addition, Ofgem requires licencees to maintain an Intervention Plan that contains the information necessary for an Energy Administrator to take management control of an insolvent licensee.

requirement is to produce within 90 days of the end of the financial year, which in our view should enable a considered response to be given in a timely fashion if introduced for airlines. The requirement could be based on an approach similar to that taken by Ofgem in their regulation of energy network operators (see case study above), adapted to ensure it is an appropriate and proportionate response to the risks in the airline market.

### Development of a repatriation plan

**6.80** This would be a power to require a UK carrier to produce a repatriation plan, in a form acceptable to the CAA. This would be similar to the resolution plan requirements seen in other sectors, including those required by the Prudential Regulation Authority for financial

institutions, and Ofgem for energy networks as described in the case study above. In particular, it would ensure that a Airline Administrator and the Coordinating Body have all the information needed to safely and effectively deliver the repatriation, and keep the airline operating if necessary. This would involve the industry more closely in the provision of repatriation.

**6.81** The CAA suggest that this power could be invoked at any time, but would be most likely used when a carrier was in financial difficulty, or when the industry is going through a systemic shock or downturn (e.g. spike in fuel prices). We note that in some sectors (including energy networks), market participants are required to draw up and maintain a

resolution plan at all times. If the CAA's flexible approach is adopted, the repatriation plan must be required at an early enough stage to ensure the carrier has time and motivation to co-operate effectively. It would be important that the sector works with the CAA in the design and implementation of such plans.

### **Temporary operating licence provisions**

**6.82** An airline will still need to retain an Operator Licence if it is operating in Administration. The CAA will need to consider whether the commencement of formal insolvency proceedings should lead to the immediate revocation or suspension of the Operator Licence. If this action is taken, then CAA could grant a Temporary Operator Licence if they are satisfied that safety is not at risk, and there is a realistic prospect of a satisfactory financial reconstruction. We have seen in the case of Air Berlin that such an approach can be used to temporarily preserve an airline's ability to operate in administration.

**6.83** The decision to grant a Temporary Operator Licence would need to be taken based upon the facts of each case. In the case of an airline SAR, it would only need to be in place for as long as the airline needs to operate to support a repatriation. This might only be for a couple of weeks, before the SAR reverts to a normal Administration procedure. As Administration is a "rescue" procedure, designed to allow for the reorganisation of a company, or the realisation of its assets, it would seem to maintain the chance of a satisfactory financial reconstruction.

**6.84** In the future, if the UK is no longer required to meet the requirements of the EU airline licensing Regulation<sup>19</sup>, then it might be helpful to reinforce an airline SAR through the granting of a special purpose licence. This could provide the

CAA with the ability to grant a temporary operating licence which had the express purpose of enabling the business to conduct a repatriation operation, even if the airline had no future as a going concern beyond the repatriation. This licence could expressly prohibit the sale of tickets beyond a certain date and/or require that moneys paid for future flights be held in a segregated account, shielded from the claims of creditors, and refunded to the passenger if the future flight is not delivered.

### **The ability to determine the timing of an insolvency with greater precision**

**6.85** We have identified that it would be helpful for the CAA to be able to influence the exact timing of formal insolvency proceedings, both to mitigate the number of passengers needing repatriation and to ensure it can prepare effectively. Without this ability, there is a greater risk of an unmanaged collapse, or of spending resources preparing for a failure that never happens. The proposed changes to the insolvency rules described above will help to provide a greater degree of oversight and control over the exact timing of insolvency proceedings, but there are also steps that could be taken to embed this into the licensing regulations.

**6.86** We have identified that the regulations currently require the CAA to make an assessment and potentially take action against a licence, whenever financial problems exist or when insolvency or similar proceedings are opened. We recommend the CAA should require the Board of a UK airline to notify them whenever there is a material adverse change in their financial situation.

**6.87** The CAA and DfT should also explore whether changes should be made to the licensing appeal process to ensure it does

<sup>19</sup> Regulation (EC) No 1008/2008 on common rules for the operation of air services in the Community

not have an undue influence on the timing of insolvency. At present, the legislation containing the appeals procedures for operating licences give UK carriers' Directors the ability to defer licence revocation until appeal procedures are exhausted. This could impede the CAA's ability to revoke an Operating Licence immediately on the commencement of formal insolvency proceedings, including an airline SAR, and substitute a special Temporary Operating licence to which specific conditions are attached. This could be addressed by a targeted reform to restrict or remove the right of appeal in the limited circumstances necessary to enable a repatriation exercise to be launched with more precise timing.

#### **Ability to demand booking data**

**6.88** Earlier in this chapter we identified that the CAA are not always able to access the information they would need to plan and prepare for an orderly wind down and repatriation. The CAA have indicated that it would be helpful to have a power to require a UK carrier to provide passenger booking data to the CAA when required. This proposal appears reasonable and,

if implemented, would assist with an organised wind down. It would provide the CAA with greater visibility of the scale and shape of a possible failure, and also provide a basis on which they could plan a repatriation and communicate this to passengers. The CAA envisage that the information would be relatively easy for airlines to provide, so any additional administrative costs should be minimal. It will be important to ensure compliance with data protection regulations, which we understand is feasible.

#### **Ability to make licence conditions that direct a UK carrier to mitigate future passenger risk**

**6.89** This could be a power to direct a UK airline to introduce measures that would mitigate the risk to passengers who had not yet travelled. This would provide CAA with the ability to apply special licensing conditions, similar to those available under the ATOL scheme, or those applied to Air Berlin when it operated in administration.

**6.90** This could include incremental steps, which can be introduced where CAA consider the risk warrants it. This could



include the following elements, which are likely to have quite different impacts:

- **Setting required liquidity levels –** The CAA may consider taking action in the event that liquidity levels fall below a certain point. This could also be triggered by other material changes in circumstances, for example, where the financial certification process has identified matters of concern. This could encourage early intervention to improve liquidity in the airline before special conditions are applied.
- **Financial monitoring and information –** the airline may be required to provide more frequent financial information, or information relating to the repatriation plan.
- **Ring-fence –** the CAA could consider preventing monies leaving the licensed entity to other parts of the Group without their permission.
- **Security –** the CAA could require the airline to set aside, or otherwise protect, financial resources (e.g. through trusts, bonds or insurance) to be used for the purposes of passenger repatriation, or to continue running for a short period in Administration. This could also include placing the money from bookings into a trust account to enable a refund to the passenger.

**6.91** The CAA suggest the powers could be permissive rather than mandatory, which would allow them to judge whether particular conditions would be beneficial based on the facts of each case. To mitigate the risk of challenge, it may be preferable for this to be an explicit condition of the licence in effect at all times, or at the occurrence of a specified trigger event, or on the direction of the CAA.

**6.92** Such changes could help the CAA to put a failing airline onto a path towards recovery or an orderly wind down, and

provide an alternative to the more severe option of full revocation of the Operating Licence under the existing regime. The conditions could be used to help avoid, or mitigate, the problems which may be encountered during insolvency, and ensure the airline itself contributes to the costs of repatriation.

**6.93** The use of the securities provided by airlines to fund a repatriation is discussed further in Chapter 8, and in the annexes of this report. It includes a recommendation that all airlines serving the UK market should have security in place to cover the estimated cost of repatriating their UK-originating passengers in the event of insolvency. If that recommendation is taken forward, then we do not think there is a case for requiring additional security from UK licensed airlines which in any case could distort competition in the UK air travel market.

#### **Power to sanction the Directors of UK carriers for non-compliance**

**6.94** The CAA have identified difficulties in enforcing licensing conditions when a business is nearing the end of its life. At present the CAA's powers to sanction can only be made against the business holding the licence (for example the suspension of the operating licence), and these would have least effect when an airline is already at heightened risk of collapse. They suggest if the sanctions were directed at the Directors personally they would be more effective. To mitigate the risk of non-compliance, one option would be to introduce a new power to provide the ability to impose a sanction against the Directors of a UK carrier that failed to comply with any instruction given to them by the CAA in contingency planning against a potential failure (for example, failure to provide data or to produce a repatriation plan).

**6.95** It has long been the case that directors and officers of a company can be held personally liable in some instances where their actions or omissions cause the company to infringe the law. However, civil sanctions against directors and officers have generally not been a feature of regulatory regimes. We recognise that more recent developments have seen some regulatory regimes (e.g. the Financial Conduct Authority's Senior Managers and Certification Regime) adopt this approach

to improve the accountability of directors and senior managers where governance failures can lead to large-scale detriment to consumers and society, such as those which are generally thought to have been contributory causes of the global financial crisis in 2008-09. Nevertheless, it may be disproportionate to apply personal sanctions in respect of the relatively less severe welfare detriment arising where passengers are adversely affected by airline insolvency.



# 7. The cost of repatriation



**7.1** We have taken a risk-based approach to determine the likely scale of impact posed by airline insolvency. This allowed us to estimate the cost of the different financial options we have considered to pay for repatriation protection.

**7.2** Our approach was to:

- 1.** estimate the per passenger cost of each repatriation mechanism (detailed in Chapter 4);
- 2.** determine a proportionate way to repatriate customers following a failure;
- 3.** estimate the total cost of repatriation (financial exposure) for each airline serving the UK market;
- 4.** estimate the probability of an airline becoming insolvent; and then
- 5.** estimate the ‘claims profile’ for repatriation based on airlines’ insolvency probabilities and financial exposures.

## Estimating the per passenger cost of each repatriation option

**7.3** For this analysis, only repatriation flight costs were included: we did not account for any costs of administering the operation, as these will be case specific. Nor have we factored in consequential losses for passengers.

**7.4** Of the four options to repatriate passengers (set out in Chapter 4), we are treating Self- and Assisted Repatriation as the same thing for this exercise as flight costs are identical.

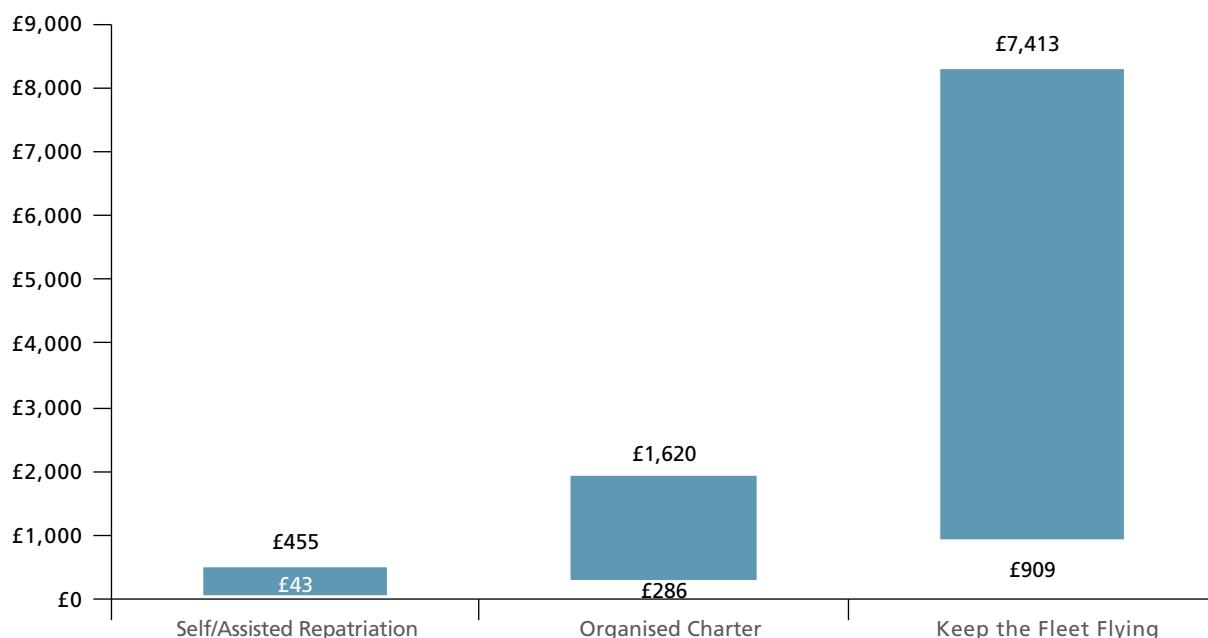
**7.5** For the different repatriation options (for full details see Annex E) ICF examined 1,996 routes, grouped into four categories:

- Long-haul;
- Short-haul leisure;
- Short-haul business; and
- Short-haul mixed.

**7.6** As seen in Figure 7.1 there is significant variation in the cost per passenger both across and within each of the repatriation options. Factors such as the month in which insolvency takes place and the particular routes served by each airline have a bearing. See Annex E, Section 5 for full details.

**7.7** It should be noted that the costs per passenger for Keep the Fleet Flying are the least certain. As well as the cost of operating an airline during a repatriation, it may be necessary to clear outstanding bills (trade credit) owed by the airline to suppliers to ensure essentials such as fuel and airport access are available. We have assumed trade credits equivalent to two weeks of operating costs; this is shown in Figure 7.1.

**Figure 7.1: Range of estimated costs per passenger of different repatriation options**



Source ICF (2018) Annex E

## Determining a proportionate means of repatriation

**7.8** As set out in Chapters 4 and 5, there are limitations to the use of Self/Assisted repatriation. These include the market share of the insolvent airline, the number of spare seats available on alternative airlines and the time of year. For some insolvencies, it may be necessary for the Coordinating Body to use the higher cost repatriation mechanisms.

**7.9** The repatriation mechanisms are not mutually exclusive: during a repatriation, a hybrid option may be best. For example, Keep the Fleet Flying may be needed in the first few days, when the number of affected passengers is at its greatest, but in the latter stages, assisted repatriation may be viable as numbers dwindle.

**7.10** We also identified the most cost-effective way to repatriate passengers on the day they were expected to fly for each

airline serving the UK. Figure 7.2 (overleaf) sets out the decision-making process used.

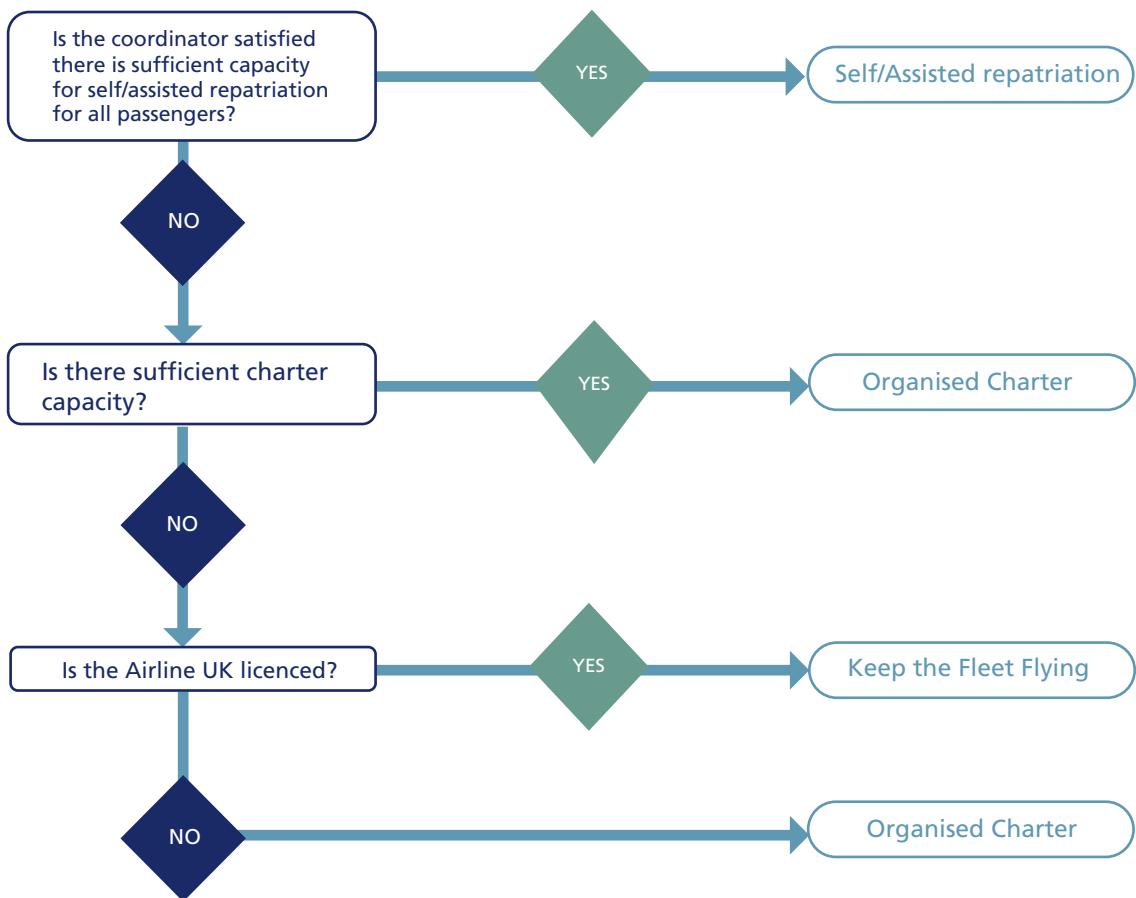
**7.11** In practice, the Coordinating Body should only adopt an Organised Charter approach if it considered it would be more financially prudent than a Keep the Fleet Flying operation, or where the latter option were not available (e.g. because the failed carrier was not incorporated in or licensed by the UK).

## Estimating each airline's financial exposure

**7.12** Given the decision about how passengers should be repatriated and the costs per passenger of each repatriation option, we estimated the potential financial exposure for each airline serving the UK.

**7.13** In general, this exposure is relatively low, less than £50m each, but for the top four airlines serving the UK it rises to over £100m, with a maximum exposure of over £450m for the most expensive. However,

**Figure 7.2: Decision tree for repatriating passengers for our analysis**



this exposure does not indicate how likely it is that an airline will become insolvent.

## Estimating the probability of an airline becoming insolvent

**7.14** To estimate the probability of an airline becoming insolvent, we refined the approach we adopted in the Interim Report.

**7.15** We estimated the probability of an airline becoming insolvent over the next 12 months by using transition probability tables published by credit rating agencies.

**7.16** Not all airlines which experience financial difficulties will become insolvent. For example, some may be taken over by stronger rivals or recover. Transition probability tables implicitly account for

these possibilities as they are an historic record of how the financial performance of companies changed over a period of time. They record the percentage of companies with improved credit ratings, those that stayed the same or declined and, in extreme cases, entered insolvency.

**7.17** ICF estimated the insolvency probability for 35 named airlines, which carry 93% of UK passengers. Credit ratings were publicly available for 18 of the 35 airlines. For the remaining 17 airlines, ICF estimated the credit rating by applying Moody's Passenger Airline Credit Rating Methodology.

**7.18** For the remaining 7% of passengers, ICF grouped these smaller airlines into twelve other categories. Credit ratings were assigned on the basis of the characteristics of the largest airline within the category.

**7.19** ICF also estimated how the insolvency probability changes throughout the year in accordance with the business cycle. See Annex E for full details on how credit ratings were assigned.

## Estimating repatriation costs

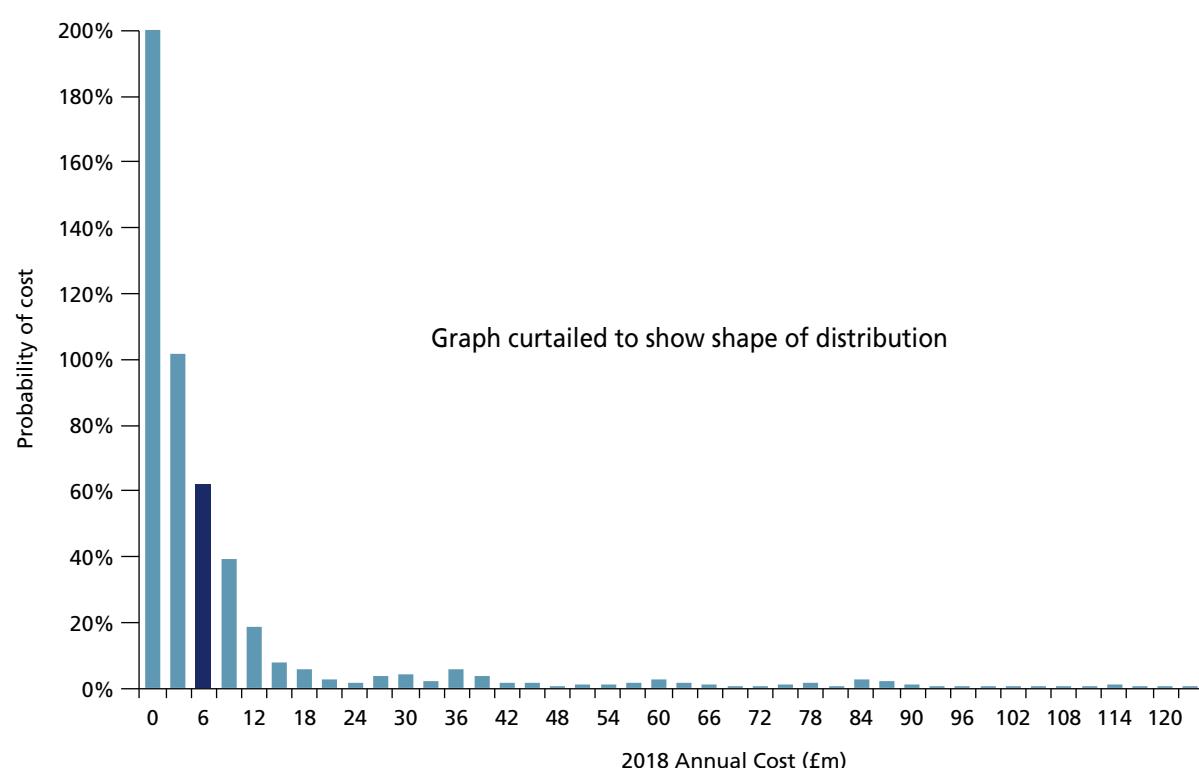
**7.20** Given airlines' financial exposure and insolvency probabilities, we can map potential repatriation costs (a claims profile) – see Annex E for further information on how this was done in the case of airline insolvencies. Claims profiles inform insurers of the annual expected costs and the probability of different levels of claims. This latter point is particularly important for insurers subject to Solvency II regulations<sup>20</sup> who are required to hold adequate capital to cover their one in 200 year event.

**7.21** As seen in Figure 7.3, the expected annual cost of repatriation operations (shown in dark blue) is very low at just under £7m, with a 70% chance of repatriation costs of less than £3m in any year.

**7.22** Conversely, there is a 2% chance of repatriation costs in excess of £70m in any year and less than a 0.5%<sup>21</sup> chance of repatriation costs in excess of £125m in any year.

**7.23** The repatriation costs associated with the failure of any of the airlines with the largest shares of the UK market could exceed this level materially. However, GAD have assessed the probability of this happening at less than 0.5%. The likelihood of more than one such airline failing in the same year is even more remote; nevertheless the associated costs were this to happen would obviously be greater still.

Figure 7.3: Airline insolvency claims profile



Source GAD (2019) Annex D

20 <https://eiopa.europa.eu/regulation-supervision/insurance/solvency-ii>

21 Equivalent to the 1 in 200 year event.



**7.24** This claims profile reflects the relative underlying financial strength and hence credit ratings of airlines serving the UK market<sup>22</sup>. Airlines with the largest financial exposure tend to be the strongest financially, while there are a larger number of smaller airlines which are financially weaker. On average, therefore, airline

insolvencies may in general be expected to have a reasonably low impact.

**7.25** Understanding this claims profile allows us to consider the most effective way to structure financial mechanisms to pay for them, which we explore further in the next chapter.

<sup>22</sup> Financial strength (credit rating) was assessed based on the most recent financial reports available up until November 2018.

# 8. Paying for passenger protection



**8.1** To achieve effective protection, it is essential to put in place a way to pay to fly passengers home in the event of a failure. The Coordinating Body needs swift access to funds to manage repatriation.

**8.2** As detailed above, our approach to repatriation is that protection should cover all who leave the UK by air and intend to return. The protection should be practicable, effectual and affordable, while ensuring that taxpayer exposure is minimal. As such, any mechanism to pay for it should be mandatory, practicable and apply no matter how a passenger books.

**8.3** The methodology applied to arrive at our recommended funding mechanism along with the detailed overview and analysis of the options we have considered can be found at Annex A to this report and within the report from Steer at Annex F.

## Options for a funding mechanism

**8.4** The appropriate mechanism must provide sufficient liquidity to the Coordinating Body to deliver the repatriation protection in an efficient fashion at a reasonable cost, in line with our Terms of Reference and Principles.

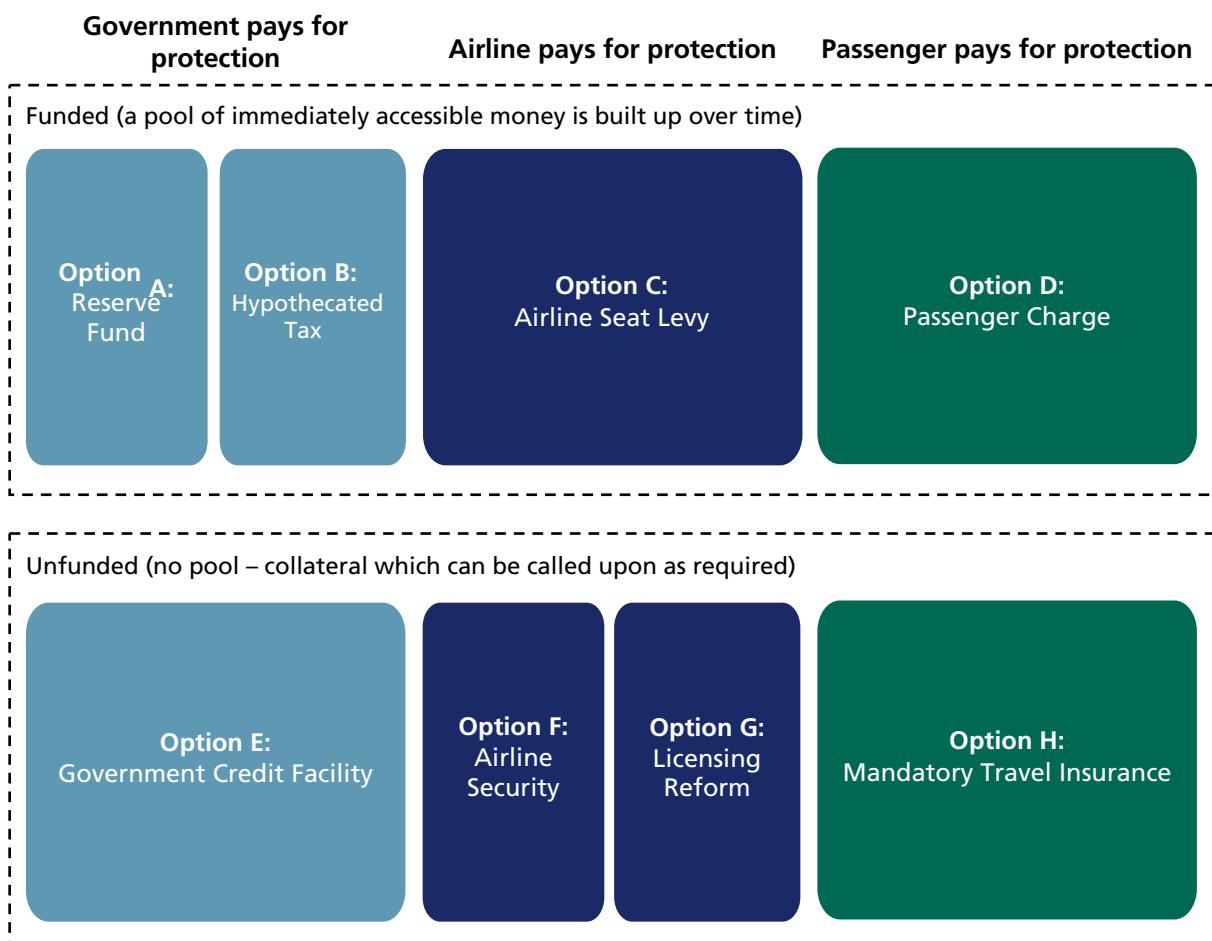
**8.5** We asked Steer to identify a universe of potential options (See Annex F) to pay for passenger protection and to select among these those they considered would best meet our criteria. The full list is shown in Figure 8.1 overleaf:

**8.6** Having filtered the options based on our Terms of Reference, principles and their costs and benefits, Steer recommended the following two:

- **Airline seat levy:** A levy would be charged on airlines on a per seat basis for seats sold to passengers originating in the UK. The levy would contribute to some type of fund vehicle, built up to a specified level, according to risk. This could finance administrative costs, bank facilities, insurance premiums, excess payments, and/or pay for repatriation operations. The levy could be flat, risk-based, or varied depending if the airline posts security against its risk of insolvency. Airlines may choose to pass this on to passengers.

- **Airline security:** Airlines are required to provide an acceptable form of security that can be called on in the event of their insolvency and can provide the necessary liquidity to manage their failure costs without a lengthy claims period. The forms of security would be chosen by the airline from a list approved by the Coordinating Body.

**Figure 8.1: Universe of options**



**8.7** Based on the analysis we have undertaken (see Annex A), we consider that neither of these short-listed options would provide a comprehensive solution to covering insolvency risk by itself. This is because each option has particular trade-offs between how efficiently it provides money, the challenges it presents to delivery, and how well it meets our principles and terms of reference.

**8.8** We therefore consider that the most effectual, deliverable and cost-effective mechanism to pay for repatriation protection should combine both elements above in a structured form. This should be structured to require that security products be provided by each airline as the first line of defence covering the greater part of its repatriation exposure. Secondly, beyond this security, any additional losses would be met from a centrally managed fund built from mandatory airline contributions

(the levy) calculated by reference to UK originating seats sold. This would be used to pay for incurred losses, administrative costs (including those of the Coordinating Body), and re-insurance premiums, and over time to build up a general reserve to provide a measure of resilience. The fund and reinsurance layers of protection would pay out sequentially to the extent the failed airline's security did not cover the costs of repatriating its passengers.

**8.9** This structure would be imposed either through requirements as part of the UK Operating Licence for UK licensed airlines or as a condition of the grant of a Route Licence for overseas airlines.

**8.10** Figure 8.2 overleaf details the structure of our proposed funding mechanism, at the point it is up and running and the fund is fully capitalised.



## Funding mechanism for the Flight Protection Scheme

### Security

Based on a pre-agreed and publicly available formula, the Coordinating Body would determine each airline's repatriation exposure, and publish a list of acceptable security products which airlines could purchase to cover the majority of this exposure. For the purposes of our analysis we set the security-protected element at 60% of the average repatriation cost for each airline. All airlines (both UK and overseas carriers) would be required to provide this security. The proportion protected by security would ultimately be determined by the Coordinating Body and could be anywhere in the range of 50-100% to meet the principle of the majority of exposure being protected this way, though we consider between 60% and 70% avoids overburdening industry.

This risk-based approach incentivises weaker carriers to improve their financial position and allows those with stronger balance sheets to obtain security at a lower cost, without tying up significant capital.

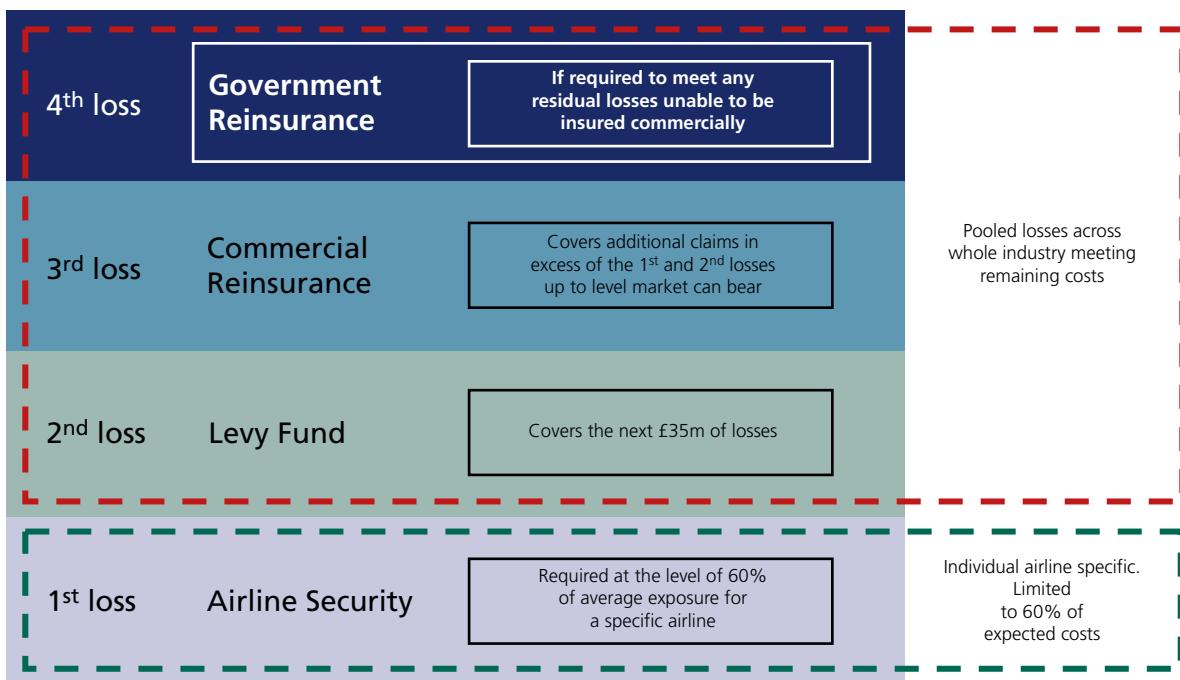
### Fund

Losses in excess of those protected by the security would be met from a centrally-held fund financed by a flat rate levy charged on airlines on a per seat basis for seats sold to passengers originating in the UK.

The levy would need to be sized to provide sufficient income to pay for the cost of meeting claims not met by the initial security or reinsurance; reinsurance premiums; running costs including relevant costs incurred by the Coordinating Body; and any general reserve. In addition, the fund would require secure access to capital to back its potential liabilities until its accumulated reserves reach a sufficient level.

### Reinsurance

The fund would be protected against excess loss by a reinsurance programme placed so far as practicable with the commercial market, with any further excess covered by government-provided reinsurance, provided on commercial terms in the manner of Pool Re.

**Figure 8.2: Structure of funding mechanism**

## Estimated costs

**8.11** GAD has undertaken analysis to estimate the annual costs of the recommendation on a per passenger basis based on 2018 data, set out in Figure 8.3 below.

**8.12** This assumes that the repatriation costs are fully covered by the scheme, and no other existing cover is in place (via the ATOL scheme) or subrogated (for example from credit cards or insurance). As set out in Chapter 9, we recommend ATOL protection remains in place and is

exempted from the Flight Protection Scheme, reducing both the scheme's total costs but also the numbers of passengers paying for protection. We also recommend government put in place mechanisms to recoup costs from providers of other forms of protection where possible, which would lower costs.

**8.13** Moreover, the figures below do not account for initial costs to capitalise the fund during any set up/transition period, as discussed further below. Nor do the estimates below factor in the running costs of the scheme<sup>23</sup>.

**Figure 8.3: Estimated cost per passenger<sup>24</sup>**

Cost to airline	Average amount (£)	Minimum amount (£)	Maximum amount (£)
Security cost (airline specific)	0.32	<0.01	6.51
Levy	Fund cost	0.03	
	Reinsurance cost	0.03	
Total cost	0.38	0.06	6.57

Totals may not sum due to rounding Source GAD (2019) Annex D

23 The ATOL scheme's costs are in the range £1.5m – £2m per annum. If our scheme had the same costs, this would equate to an additional levy of £0.02 per UK originating passenger.

24 See Annexes D and F for the analysis underpinning these estimated costs.

## Competition impacts

**8.14** ICF have assessed the competition impacts of implementing passenger protection. Given the average cost per passenger of each of the financing options is low relative to the cost of an airline ticket, we agreed they should only assess the impacts of the financing option considered with the highest cost per passenger (which saw protection delivered entirely through security, with no other financing; see Annex A for details). This indicates the worst-case competition outcome. ICF undertook the analysis on the following basis:

- Adjusted for costs already covered by ATOL protection, to ensure no duplication of protection.
- Costs will be spread over all flights to and from the UK, including those not covered by repatriation.

**8.15** ICF have estimated that were the cost of protection to be borne entirely by passengers (as opposed to spread between passengers and airline shareholders), total aviation demand would decline by around 86,000 per year (or a drop of 0.03% on 2017 figures).

**8.16** In addition, ICF examined the implications for airlines should they absorb the costs of protection (thereby lowering profits), rather than passing these on to passengers. Given the relatively low cost of protection, they do not consider this would materially affect the viability of airlines. Nevertheless, they do note that as the price of securities is airline specific, there may be distributional impacts, such that cost and demand impacts would be concentrated on financially weaker airlines.

## Worked examples

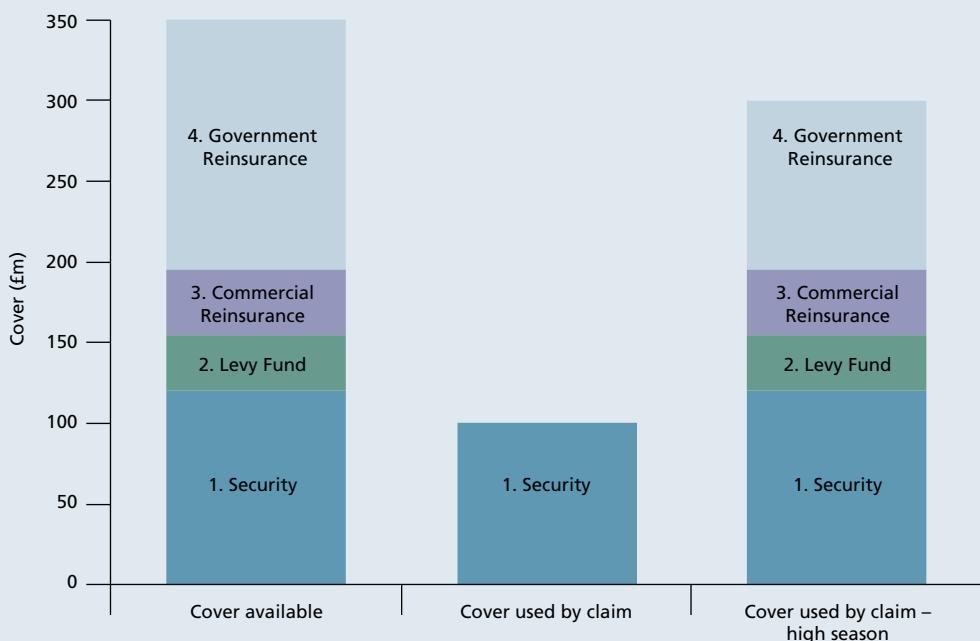
In this hypothetical example we consider a fictional airline, Fly World Airlines, to demonstrate how the repatriation cover would operate in practice. We consider two insolvency scenarios:

- 1 Low season failure with repatriation costs of £100m; and
- 2 High season failure with repatriation costs of £300m.

For the purpose of this example, it is assumed:

- Airlines will take out security for 60% of their expected average annual repatriation exposure, as determined by the Coordinating Body. Fly World Airlines provides security for £120m (60% of its expected average annual repatriation exposure of £200m).
- The Fund, will cover any claims in excess of security up to the maximum capitalisation of £35m.
- Commercial reinsurance will cover any claims above the levy fund, up to a cap of £40m.
- Government provided reinsurance for losses in excess of commercial reinsurance cover.

**Figure 8.4: The application of repatriation cover to the fictional Fly World Airlines at low and high season.**



Source GAD (2019)

### Low season failure

Fly World Airlines enters insolvency in the low season and the cost of repatriation is £100m. This is below the value of the security (£120m), such that all of the repatriation costs are met by the security (first loss).

### High season failure

Fly World Airlines enters insolvency in the high season and the cost of repatriation is £300m. This requires all four layers in order to pay the cost of repatriation:

- First loss – security pays out the full £120m of the security
- Second loss – fund pays out the £35m up to its maximum capitalisation
- Third loss – commercial reinsurance pays out the full £40m
- Fourth loss – There remains £105m of outstanding costs from the original £300m incurred, which is covered by government reinsurance

## Implementation considerations

**8.17** There are several other factors affecting the cost and choice of mechanism to finance the scheme, which will require further development before deciding whether to implement our recommended structure, including:

### Terms of security

**8.18** Any security pledged would likely need to be valid for at least 12 months and the counterparty providing the security would be assessed against a credit scoring test. The security would need to be effectively assigned to the Flight Protection Scheme. While any trust account would be available on demand, it is likely that bonding and insurance would not pay out

immediately. To cover this eventuality, in cases where its own reserves are insufficient for the purpose, the Fund would need a source of bridge finance to provide immediate liquidity. It is important that any security mechanism does not have exclusions and/or terms and conditions outside of the Fund management's control which might affect the financial protection it affords in the event of failure. Any airline

specific security should be subject to appropriate renewal terms, with significant advance notice to the airline should the provider not be willing to renew the policy on acceptable terms. It may be possible that other security mechanisms, such as a letter of credit from a financial institution or a sovereign guarantee, could alternatively be procured by the airline, if considered acceptable by the Coordinating Body.

**Figure 8.5: Vehicle for the fund**

<b>Vehicle</b>	<b>Analysis</b>
<b>Trust</b> This would be akin to the Air Travel Trust Fund (ATTF) for the ATOL scheme. The Fund is administered on behalf of the ATT by employees of the Civil Aviation Authority, but is governed by its own trustees and produces standalone financial statements.	Given the differing scopes of the schemes, it is not recommended that the funds from this structure be pooled with the existing ATOL funds. As for the ATTF, any trust could be deemed to be a Central Government Body to the extent that there was "significant government control", assessed as the ability of government to make appointments; the degree of influence over the objectives and operations of the entity; the degree of control; the degree of government funding; and the degree of government risk exposure. In this case, the fund's exposure would be accounted as a contingent liability of government. In addition, the contribution charged to airlines may be considered to be a tax, as the ATOL Protection Contribution is (as detailed in Chapter 7). Further work would be needed with HMT and ONS officials to determine whether variation of these attributes would affect their classification. In the long term, to the extent that there was reform to either the ATOL or Flight Protection schemes, for example with regards to refund protection, it may be possible to integrate both funds into one pool.
<b>Regulated insurance company</b> This could be a private, third party or mutual insurance company.	It is likely that an insurance company would need to have sufficient capital to cover its 1/200 year risk under the EU's Solvency II requirements (or an equivalent). It would be independently regulated and subject to prescribed reporting and disclosure requirements. However, as an independent corporation, it would be unlikely to be classified as a Central Government Body on the basis of the factors listed above, provided that there was minimal government involvement, oversight and control. In this case, the levy would be characterised as the payment of a premium. Airlines would be obligated to take out a contract of insurance with the company and to pay premiums at a uniform rate determined actuarially. This would potentially increase the complexity of the scheme, while having the potential benefit of setting it more firmly within the private sector. Further analysis is needed to understand the legal, tax treatment and practical implications of the structure. Market testing would be necessary to understand appetite in the private sector for initial set-up costs and the ongoing management of this risk.

\* Solvency II is an EU legislative programme implemented in all 28 Member States, including the UK, by 1 January 2016. It introduces a harmonised EU-wide insurance regulatory regime. It aims to ensure a uniform and enhanced level of policyholder protection across the EU. In this case, the company would need to have sufficient capital to cover its 1 in 200 year exposure to airline insolvencies.

## Market appetite

**8.19** The proportion of loss taken by airline security will be limited by the market's appetite for risk. Very risky airlines may not be able to obtain security at any cost. In this scenario, they would be required to set aside equivalent cash to protect against their failure. Equally, any mechanism would only be effective if the obligation to provide this security is hard-wired into an airline's legal and/or regulatory obligations. Further work would be needed to assess the availability and commercial pricing of the various forms of security acceptable to the Coordinating Body.

**8.20** In addition, the availability and cost of reinsurance would need to be assessed by issuing a prospectus to market.

**8.21** It should be noted that the Review's analysis is based on providing sufficient finance for our proposed repatriation scheme. The structure we propose could not necessarily be extended to cover lost forward bookings as well as repatriation.

## Vehicle for the fund

**8.22** There are a number of legal forms that this could take. Further work is needed to consider the options available, however, an indicative summary is provided in Figure 8.5.

**8.23** Before reaching a decision on the constitution of the vehicle, it will be necessary to have regard to a number of matters including the respective taxation, regulatory, and governance implications of the different options. We have not attempted this analysis.

## Subrogation of rights

**8.24** As set out in Chapter 2, passengers currently benefit from financial protection, though its scope and the extent of cover varies depending on its form. For example, protection will differ depending on

whether consumers have purchased travel insurance, bought their tickets using a credit or debit card, or have paid for ATOL protection. In the event of airline insolvency, a passenger's right to claim will depend on how much the ticket cost, how it was purchased, and whether the passenger can establish a loss arising out of the breach of contract.

**8.25** We set out in Chapter 9 that we recommend passengers protected by the ATOL scheme should not be covered by the Flight Protection Scheme.

**8.26** Where a passenger would have been entitled to recover a loss from a third party had the Scheme not paid for repatriation, the Scheme should have the right to seek to recover money from that third party up to the limit of the protected loss.

**8.27** We have been advised that this would require legislation, which if successfully implemented could reduce the overall exposure of the Flight Protection Scheme, and consequentially lower the amounts required in both security and levy payments.

**8.28** However, even with changes to legislation, there would still be practical issues for the CAA in claiming back monies on behalf of thousands, if not hundreds of thousands of individuals. As such, negotiating in advance an agreed settlement figure with card providers (akin to the agreements the Air Travel Trust has with Merchant Acquirers in respect of refund payments) may be a more practicable way to access some of the saving realised by the provider because the passenger has been repatriated at the Scheme's expense.

## Transition period

**8.29** An appropriate transition period would be needed to set up the scheme to allow the industry to be in a financial



position to comply. We have assumed five years for the purposes of the report.

**8.30** A transition period may be necessary as airlines may need time to restructure balance sheets and to build up to the 60% security level over the transition period. To mitigate the risk of the Scheme forcing widespread market exit, we recommend a phased approach should be taken to implementation; for example requiring security of up to 20% in year one, 40% in year three and the full 60% in year five. During any transition period, government would be exposed to costs in excess of the posted security, declining over time.

**8.31** With respect to the fund, an initial investment or other transitional arrangement would be required to ensure it has sufficient capital to cover the second loss fully.

**8.32** The levy, estimated at 6p per departing UK passenger, is designed to cover the expected (average annual) claim on the fund, which is estimated at £2.2m and therefore maintain the fund at £35m (the fund's maximum possible claim exposure net of reinsurance recoveries). In the absence of an initial investment or other transitional arrangement, the fund would have insufficient capital to meet any large claim which arose in the early years, resulting in a deficit.

**8.33** For the fund, we have assessed a transition period of five years, consisting of two elements:

- a. a surcharge with which to build up the fund to the required capital level. To fully capitalise the fund by the end of the five-year period, GAD estimate a levy surcharge at 9p per passenger in addition to the standard levy charge of 6p, which would only be payable for the five-year duration of the transition period. Such a surcharge would however have the disbenefit of seeing today's passengers charged more for the benefit of tomorrow's.
- b. a credit facility/government guarantee to cover any shortfall in the fund, which would be repaid by the levy. As the fund builds up year-on-year, the need for the credit facility/government guarantee would decline, in other words the fund would cover an increasing proportion of the second loss exposure.

**8.34** We recommend that should government choose to implement the Flight Protection Scheme, it set a transition period that balances the risk of increasing the burden on airlines too quickly against reducing the government's exposure to failures during the interim period.

### Enforcement

**8.35** The scheme would only be effective to the extent that it was appropriately enforced through legislation. For example, to the extent that appropriate security was not posted, the Coordinating Body would require statutory powers to appropriately sanction the entity, for example through putting the carrier on a temporary licence or revoking it as necessary, forcing market exit. Powers would need to be proportionate, practicable and

enforceable. However, there may be difficulties in taking enforcement action against a foreign carrier. There is also a risk that this would provoke retaliatory action by overseas authorities against UK airlines, which may be disproportionate and impact the competitiveness of UK airlines.

**8.36** We have considered whether these risks could be mitigated by relying solely on a charge payable by and collected from UK-originating passengers at the point of sale or at outbound check-in, instead of requiring the airlines to post security or make a contribution to the fund. The passenger charge could be at a single flat rate or at varying rates to reflect the relative insolvency risk of each relevant airline. However, such an approach would in our view have a number of drawbacks that are likely to prove problematic:

- It would be complex and costly to put in place and administer, and is likely to be resisted by the airlines who would bear the burden of collection and enforcement.
- A flat-rate charge would give passengers an inappropriate price signal and would confer an unfair advantage on weaker airlines at the expense of stronger ones.
- A flat-rate could make it more likely the charge would be classified as a tax.
- A variable rate charge could be confusing to passengers even with explicit messaging at point of sale.
- A variable rate charge would send a strong price signal not only to passengers but also to others who trade with airlines, potentially prejudicing those in weaker condition and distorting competition.
- Calculation of an administered variable rate charge would present a major

challenge, requiring a transparent methodology that could command general support and survive the challenges which weaker airlines would be bound to raise.

### Data availability

**8.37** Further work is necessary to ensure that the necessary data is available to:

- allow the Coordinating Body and third party advisors to accurately estimate insolvency repatriation exposure for all airlines operating in the UK (whether domestic or foreign).
- ensure airlines pay the correct levy on a periodic basis and ensure that the Coordinating Body can appropriately audit this.



# 9. Commercialising existing financial protection



## The ATOL scheme

**9.1** The ATOL (Air Travel Organiser's Licence) scheme was created in 1973 to provide financial protection to customers booking package holidays including flights. Since then, the scheme and the context within which it operates has evolved considerably. But, at its heart, it still provides the same protection: holding funds to provide repatriation and refunds, and reducing exposure to the risk of insolvency through financial oversight.

**9.2** Anyone booking an ATOL protected arrangement should be provided with an ATOL Certificate setting out their protection at the point of payment. This protection is paid for by a per-passenger levy on ATOL holders known as the ATOL Protection Contribution (APC), currently £2.50, and paid into the Air Travel Trust Fund (ATT).

**9.3** The ATOL scheme differs from the Flight Protection Scheme we recommend government creates for airline insolvency because it offers protection against the failure of a travel organiser to deliver all elements of the travel package. It not only provides repatriation protection, but also for the refund of bookings made for future travel. Given its statutory foundation, and the nature of protection offered, it can be considered the gold

standard in travel arrangement financial protection. The Review sees no immediate reason to change the nature of this protection, but offers recommendations to put the ATOL scheme and the ATT on a more commercial footing, and to ensure ATOL and the proposed Flight Protection Scheme could operate in harmony.

## The ATOL Protection Contribution and Air Travel Trust Fund

**9.4** Under ATOL Regulations, businesses such as tour operators and travel agents that offer holidays that include a flight must hold an ATOL from the CAA, unless exempt under the regulations.

**9.5** Every ATOL holder<sup>25</sup> is required to pay the APC into the ATT for each booking taken for an ATOL protected flight or holiday.

**9.6** The ATT is established by the Air Travel Trust Deed<sup>26</sup> made by the Secretary of State for Transport and the Trustees of the Air Travel Trust. In this context, the Deed sets out the powers of the Trust and for what it can use its funds. It is broadly limited to assisting customers of failed ATOL holders.

**9.7** ATOL protection is financed by the ATT, with initial costs covered by the Fund

<sup>25</sup> businesses which may sell air travel either by holding an ATOL or being a member of an ATOL Accredited Body.

<sup>26</sup> <http://publicapps.caa.co.uk/modalapplication.aspx?appid=11&mode=detail&id=4999>

itself (which had a balance of £170m at 31 March 2018)<sup>27</sup>. An insurance policy provided by a panel of insurers, is in place to provide an additional layer of cover up to £400m (to 31 March 2020), depending on the ATOL holder.

**9.8** The ATT also has a credit facility to provide additional funds and, in some ATOL failures, may also receive recoveries, such as money from bond providers. In addition, the Trustees have agreements in place with merchant acquirers by which the Trust's exposure to refund repayments is shared. The Trustees employ an investment strategy to grow the fund while limiting risk to liquidity. This adds value to the Fund by way of interest payments which build it further. There are however, some events which could potentially expose the taxpayer to a liability, for example, if a large ATOL holder were to fail in peak season.

**9.9** In 2012, the ONS reclassified the APC as a tax and the ATT as a central government body (it was previously classified as a public corporation). It based this on the judgement that the APC was a mandatory, unrequited payment, and that the government was able to exercise significant control over the Fund.

## The Package Travel Directive

**9.10** The European Union's Package Travel Directive (PTD)<sup>28</sup>, imposes obligations on the UK to ensure travellers are provided with effective protection if the organiser of their trip becomes insolvent, and was brought into UK law with the implementation of the Package Travel Regulations 2018. While the ATOL scheme predates the PTD, the UK meets its obligations to provide insolvency protection for packages involving a flight primarily through ATOL.

## Airline exemption

**9.11** Some stakeholders have suggested to the Review that the simplest mechanism to ensure passenger protection across all types of flight booking would be to remove the existing exemption from ATOL protection for airline sales. At present, the Package Travel Directive exempts airlines licenced by EU member states from its requirements, meaning that it is not currently open to the UK government to unilaterally require airlines to hold an ATOL. We have therefore not considered this approach further, but would note that to do so would see flight-only passengers on UK airlines paying for protection of forward bookings which, for the reasons set out in Chapter 3, we do not consider to be necessary and which would not be available to UK passengers of airlines licensed by other states.

## Enhancing commerciality in the ATOL scheme

**9.12** The Review's terms of reference require us to consider how the current financial protection arrangements for air-travel holidays can be put on a more commercial basis. We have broken down our consideration of the ATOL scheme into two broad areas: what more can be done to reduce the government's role in the provision of financial protection and how ATOL could interact with our proposed new Flight Protection Scheme if it is implemented.

**9.13** There are several elements to consider when thinking about how the ATOL scheme should operate in a future where all seat bookings have some form of financial protection. First is how to ensure passengers receive adequate protection and are not paying for more protection than is necessary. Second, is to

<sup>27</sup> <http://publicapps.caa.co.uk/modalapplication.aspx?catid=1&pagetype=65&appid=11&mode=detail&id=8576>

<sup>28</sup> <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32015L2302>

consider whether lessons drawn from our work on airline insolvency protection could be carried across to the ATOL scheme. Third is to examine how the respective schemes could operate in harmony and provide an insolvency protection environment fit for the 21st century.

**9.14** We recommend that the government takes steps to make the Trust independent of government involvement and, alongside our recommendations for paying for airline insolvency protection, restructures how the ATOL scheme is financed to increase private sector involvement.

## Refreshing the Air Travel Trust

**9.15** In assessing whether a body is in the public or private sector, the key test is if government exercises significant control. There are five characteristics to consider including government's ability to make appointments; the degree of influence over the objectives and operations of the entity; the degree of control; the degree of government funding; and the degree of government risk exposure. Government control may be determined by the strength of one of these characteristics alone, or by a combination of all or some only.

**9.16** If an entity is in the public sector, then its status is determined by its legislative constitution and how it is funded.

**9.17** The combination of the view that the APC is a tax and the ATT sits in the public sector means the fund is considered a central government body. This seems inappropriate for a fund that provides protection to individuals who book holidays and, in effect, substitutes for private travel insurance.

**9.18** To move the ATT closer to the private sector, where we consider it would more appropriately be seated, we recommend government:

- Changes the terms of the Trust Deed so that control exerted by the Secretary of State is removed. The Trustees should be charged with stewardship of the fund in the manner best calculated to deliver the protection required.
- Changes the appointment process for the Trustees so the Secretary of State has no say over the appointment of any Trustee. We recommend that the CAA Board or an independent panel should appoint and hold Trustees to account.



- Introduces greater independence to the Trust by ensuring at least some (if not all) Trustees are independent of the CAA.

## Reforming the ATOL scheme's finances

**9.19** In developing a financing structure for the airline insolvency scheme, we consider it would be beneficial to offer airlines flexibility in how they meet the requirement to ensure financial protection is fully funded.

**9.20** This has led us to a structure (set out in Chapter 8) that combines provision of securities by airlines to cover the majority of repatriation costs, together with a small levy in order to pay for insurance and operating costs.

**9.21** At present, this flexibility is missing from the financing of the ATT. We recommend the Trust be reconstituted to ensure Trustees have the ability to adjust the rate of the APC based on specific factors, should they wish to, and are confident passenger protection will be maintained.

## Options to vary the APC

**9.22** We have identified the following ways the APC could be varied:

- a. based on provision of additional securities by the ATOL holder;
- b. based on the amount of customer money at risk;
- c. based on the ATOL holder's risk of failure; and
- d. based on the cost of travel arrangements sold by the ATOL holder.

**9.23** The following section sets out an overview of each option, though the exact

methods to be used will require a more detailed examination. Each option is explained in more detail below, with pros and cons for each one summarised in Figure 9.1 (overleaf).

### A. Additional security

This would allow a company to offset some of its insolvency exposure by providing security from a list of products approved by the Fund (e.g. based on those set out in the UK's Package Travel Regulations 2018<sup>29</sup>). The structure would be similar to that we recommend for the Flight Protection Scheme, with an APC set by the Trustees at a level designed to ensure the fund was sufficiently capitalised to meet a defined risk threshold, discounted where companies met some of that risk through pledging collateral security.

### B. Customer money at risk

This option would see the amount each ATOL holder was required to pay into the ATT varied based on an objective measure of the fund's exposure should the firm fail. For example, this might be based on annual turnover, value of customer monies taken or unflown revenue. This would allow the firm to reduce its compliance costs by adjusting its commercial practices (for instance, by lowering the amount of deposit required; or by seeking full payment for the holiday closer to the time of departure; or by holding all customer money in a segregated trust account until paid over to the end-suppliers).

### C. Risk of failure

This would see the CAA using the financial data it holds on each ATOL holder to vary the APC charge based on their failure risk (derived from credit

29 <https://www.legislation.gov.uk/ukdsi/2018/9780111168479/contents>

**Figure 9.1: Pros and cons of each option**

<b>Option</b>	<b>Pros</b>	<b>Cons</b>
<b>Flat APC (status quo)</b>	<ul style="list-style-type: none"> <li>• Simple</li> <li>• Low admin burden</li> <li>• Accepted by business</li> <li>• Some security requirements and variation in the APC already exists in the scheme</li> </ul>	<ul style="list-style-type: none"> <li>• Lack of flexibility</li> <li>• Lack of fairness – does not reflect risk or exposure (so the strong subsidise the weak)</li> <li>• Classified as a tax</li> </ul>
<b>Additional security</b>	<ul style="list-style-type: none"> <li>• The fund would become secondary in terms of protection where security was pledged, giving a greater role to the private sector in providing protection</li> <li>• Relatively simple to implement</li> <li>• Introduces risk pricing to financial protection</li> <li>• Securities already part of ATOL landscape (for new entrants or companies which represent a greater risk)</li> </ul>	<ul style="list-style-type: none"> <li>• More complex than status quo</li> <li>• May be more costly for some ATOL holders to provide security, which could lead to the ATTF's exposure becoming concentrated on risky companies</li> <li>• Would not provide strong price signals to consumers</li> </ul>
<b>Customer money at risk</b>	<ul style="list-style-type: none"> <li>• Less admin burden than varying based on risk or holiday cost</li> <li>• Fair for consumers, it is a proxy for cost of holiday</li> <li>• More direct relationship to costs to the fund</li> <li>• Incentive to reduce exposure</li> <li>• In many cases could be delivered using existing data</li> </ul>	<ul style="list-style-type: none"> <li>• More complex than status quo</li> </ul>
<b>Risk of failure</b>	<ul style="list-style-type: none"> <li>• Arguably fairest</li> <li>• Encourages companies to reduce risk</li> </ul>	<ul style="list-style-type: none"> <li>• More complex than status quo</li> <li>• Potentially signals financial difficulties as APC levels rise</li> <li>• Significant increase in burden for business and regulator</li> </ul>
<b>Cost of holiday</b>	<ul style="list-style-type: none"> <li>• Arguably fairer for consumers, as the cost of protection is higher for expensive holidays</li> <li>• Closer relationship to costs to the fund (especially for refunds)</li> </ul>	<ul style="list-style-type: none"> <li>• Higher cost of holiday does not necessarily result in higher costs to the fund (especially for repatriation)</li> <li>• More complex than status quo</li> <li>• Significant increase in burden for business and regulator</li> <li>• Would need a costly and complete overhaul, so that the levy can be applied at point of purchase</li> <li>• Disproportionate impact on SMEs</li> </ul>



ratings or proxy credit ratings). This could be based on bands within which firms would fit depending on their failure risk, or be a specifically assigned charge for each ATOL holder.

#### D. Cost of holiday

This option would see the APC vary based on the cost of the holiday booked by the customer, either set within bands (like the geographical and class of travel bandings structure of Air Passenger Duty) or as a proportion of the overall booking cost.

**9.24** Options A. to C. above have the potential to be combined in some form to offer greater dynamism in the charging structure, at the cost of increasing complexity.

**9.25** Given our view that the Trust should maintain operational independence from government, we do not think it would be appropriate to prescribe which of the above options, or combinations thereof, should be adopted. However, we are strongly of the view that, at a minimum, offering ATOL holders the ability to offset some of the cost of the APC if they are

able to provide security covering a degree of their insolvency exposure, is appropriate, and in line with the way the Trust currently manages risk and funding.

**9.26** Any reforms to the way ATOL protection is paid for should do more to reflect the Trust's exposure and ensure financing is set at an appropriate level to meet predicted calls on the Trust's funds.

#### Reinsurance

**9.27** At present, an insurance policy protects losses beyond those which the Fund can cover itself, subject to certain specific limits and exceptions. This leaves some situations where the ATT would need to borrow money to ensure it has sufficient funds, which may require the government to provide finance or guarantee its provision by third parties.

**9.28** This exposes taxpayers to a theoretical risk that, in future, the Trust may be unable to repay government for significant losses, and creates intergenerational inequity which could see tomorrow's customers having to pay a higher levy to repay the costs of protecting today's.

**9.29** We recommend that if insolvency risks cannot be met in the private insurance market, the government should consider charging the ATT at a commercial rate for the provision of any additional guarantee or insurance, analogous to the Pool Re arrangements. This step will ensure commercial discipline within the fund, and will reward taxpayers for any potential risk they insure.

## Drawing ATOL protection and airline insolvency protection together

**9.30** Should government choose to introduce a new element to consumer travel protection in the form of airline insolvency cover, there is a risk of increasing confusion for consumers, and people paying for more protection than necessary. In relation to other types of protection, we make recommendations for government to work to enhance consumer understanding (see Chapter 3). However, with ATOL protection, we can ensure simplicity for consumers is maintained by removing the risk of double protection within the foundations of the scheme. We propose two broad phases.

### Phase 1

**9.31** Should the Flight Protection Scheme be implemented, there is a risk protection may overlap with ATOL protection for some consumers. To avoid this duplication, we recommend the Flight Protection Scheme only cover customers not protected via the ATOL scheme.

**9.32** We recommend that in principle no passenger who holds an ATOL Certificate should be taken into account when calculating an airline's contributions to the Flight Protection Scheme. However, this may present practical difficulties where an airline ticket is sold by a third party who

provides the customer with an ATOL Certificate without the airline's knowledge. We understand that where a relationship exists between agent and airline, this can be mitigated, but a new approach may be required to manage this in other cases to avoid duplication.

**9.33** This approach will mean that the ATOL scheme remains the gold standard for holiday financial protection – with full refund and repatriation protection provided based on the payment of the APC and provision of an ATOL Certificate.

**9.34** At present, the Package Travel Regulations (2018) direct the business which sold the package to acquire replacement flights for their consumers should the airline they book with fail – ensuring businesses have some incentive to work with more financially sound airlines.

**9.35** Alongside ensuring customers are not charged twice for the same protection, our proposed approach will maintain this discipline on ATOL holders to perform due diligence when they make bookings involving third party airlines.

**9.36** ATOL holders may continue to reduce their exposure including through airline failure insurance, and, in some circumstances, the CAA may decide to take overall charge of arrangements to ensure the integrity of an operation and reduce the immediate impact on potentially vulnerable ATOL holders.

**9.37** At present, there may be some cross-subsidy involved should government direct the CAA to utilise the experience, relationships and systems it has developed in relation to the ATOL scheme to help manage airline failures or other civil contingency operations.

**9.38** Introducing the proposed Flight Protection Scheme, would allow the CAA to ensure the correct party pays their costs in future, while maintaining the considerable benefit of their repatriation operation experience to assist in the management of low-probability, high-impact scenarios.

**9.39** There will, of course, be benefits to the CAA's management of ATOL holder failures if the recommendations set out in Chapters 4 to 6 relating to enhancing its abilities to manage all sizes of failure are adopted. Where activity to improve preparedness and delivery of repatriation operations will have benefits for both airline and ATOL holder insolvency situations, the CAA should assign its costs on a pro-rata basis between the two schemes.

## Phase 2

**9.40** Today, the protection provided by the ATOL scheme is defined by European Union regulations by means of the Package Travel Directive. This ensures

that no matter where they book travel packages within the European Economic Area, consumers should benefit from a harmonised level of protection. However, this does also limit government's ability to reflect changing booking patterns, protection mechanisms and other rapidly changing context to insolvency protection.

**9.41** We recommend that should conditions arise where the government has the ability to review the protection the ATOL scheme provides in light of the existence of the Flight Protection Scheme, the proportion of bookings that are protected via other means (credit cards, insurance etc.) and the broader financial protection landscape, it should do so.

**9.42** Were it to do so, we suggest government's objective should be to ensure the traveling public continue to benefit from adequate financial protection at an affordable level, delivered within the private sector in a way that is simple for consumers to understand.



# Appendix 1: Glossary



<b>ABTA</b>	The Association of British Travel Agents – the UK's largest travel association, representing travel agents and tour operators.
<b>Air Operator Certificate (AOC)</b>	Certificate of operational safety granted by the CAA and required to operate a commercial aircraft. There are several certificates depending on the type of aircraft, routes to be flown, and conditions they will be flown in.
<b>Air Operator Licence (AOL)</b>	Licence to operate commercial air transport services granted by the CAA, which covers nature, ownership and financial health of an airline business.
<b>Air Passenger Duty (APD)</b>	An excise duty charged on the carriage of passengers flying from the UK and the Isle of Man.
<b>Air Travel Organiser's Licence (ATOL) Scheme</b>	Scheme offering financial protection to people who have purchased package holidays and flights from ATOL-holding travel businesses.
<b>Air Travel Trust/Air Travel Trust Fund (ATT)</b>	The primary source of funding when an ATOL holder fails. Monies from the ATT are used to meet refund and repatriation costs. The fund is administered on behalf of the ATT by the CAA.
<b>Air Travel Trust Deed</b>	The legal instrument establishing the rights and obligations of the Air Travel Trust.
<b>Assisted Repatriation</b>	A repatriation operation in which a co-ordinator plays a more active role than in Self-Repatriation but is still reliant on accessing spare capacity from other airlines.
<b>ATOL Protection Contribution (APC)</b>	£2.50 per passenger charge payable by ATOL holders to the Air Travel Trust Fund
<b>Air Travel Insolvency Advisory Committee (ATIPAC)</b>	Committee established by the Secretary of State for Transport to provide advice on the financial protection arrangements for air travellers and customers of air travel organisers.
<b>Aviation 2050</b>	The Government's long term Aviation Strategy to achieve a safe, secure and sustainable aviation sector that meets the needs of consumers and of a global, outward-looking Britain.
<b>Billing and Settlement Plan (BSP)</b>	A system designed to facilitate and simplify the selling, reporting and remitting procedures of IATA accredited passenger sales agents, as well as improve financial control and cash flow for BSP Airlines.
<b>CAA Consumer Panel</b>	A non-statutory body established to act as a 'critical friend' to the CAA. It provides expert advice to make sure that the consumer interest remains central to CAA policy development.

<b>Cape Town Convention</b>	International framework for the formation, registration, protection and enforcement of certain international interests in airframes, aircraft engines and helicopters.
<b>Central Government Body</b>	Government Departments and their arm's length bodies, and any other non-market bodies controlled and mainly financed by them.
<b>Chancellor of the Exchequer</b>	The government's chief financial minister, responsible for raising revenue through taxation or borrowing and for controlling public spending.
<b>Chapter 11 in US Bankruptcy Law</b>	Chapter 11 of the United States Bankruptcy Code, which generally provides for reorganisation, usually involving a corporation or partnership.
<b>Charge-back</b>	A transaction reversal made in the event of failure to receive goods, which secures a refund of the purchase price for the consumer.
<b>Civil Aviation Authority (CAA)</b>	The UK's independent aviation regulator.
<b>Coordinating Body</b>	The body proposed by the Review to coordinate repatriation in the event of an airline failure.
<b>End Supplier Failure Insurance (ESFI)</b>	Insurance that protects the customer in the event of financial failure of an "end supplier" such as a hotel or scheduled airline. See also Scheduled Airline Failure Insurance.
<b>European Commission (EC)</b>	The European Commission is one institution of the EU, responsible for proposing legislation, implementing decisions, upholding treaties and managing day-to-day business.
<b>European Union (EU)</b>	The European Union is an economic and political union between member states.
<b>Expert Advisory Panel</b>	Independent advisory panel to the Review, comprising of individuals with expertise relevant to the Review, including in the operation of airlines and travel companies, aviation regulations, insolvency and restructuring, and consumer protections.
<b>Financial Conduct Authority (FCA)</b>	Regulator of the UK's financial services industry. Its role includes protecting consumers, keeping the industry stable, and promoting healthy competition between financial service providers.
<b>Fleet Size</b>	Number of aircraft operated by an airline.
<b>Flight Protection Scheme</b>	The Review's proposed scheme for the organised and financed repatriation of UK-originating passengers in the event of airline failure.
<b>Government Actuary's Department (GAD)</b>	Provider of financial and risk analysis to the Review.
<b>Her Majesty's Treasury (HMT)</b>	The UK's economic and finance ministry.
<b>ICF International</b>	Provider of aviation data and economic evidence for financial modelling and understanding of competition impacts to the Review.
<b>International Air Transport Association (IATA)</b>	Private organization promoting cooperation among scheduled airlines.
<b>Ipsos MORI</b>	Provider of research for the Review into consumer understanding of airline failure risk and protection.

<b>Keep the Fleet Flying (KFF)</b>	A repatriation operation undertaken through continuing to use the aircraft, crew and support staff of the airline concerned.
<b>Non-statutory protection</b>	Protection that falls outside the scope of legally binding provisions set out in legislation, and therefore may be subject to change.
<b>Office of Gas and Electricity Markets (Ofgem)</b>	The government regulator for gas and electricity markets in Great Britain.
<b>Office of National Statistics (ONS)</b>	The UK's largest independent producer of official statistics and the recognised national statistical institute of the UK.
<b>Organised Charter</b>	A repatriation operation to centrally organise charter aircraft from third-party airlines and run a flying programme to bring passengers home.
<b>Package Travel Directive 2015</b>	The EU law protecting consumers who purchase package holidays organised by tour operators and other forms of combined travel. Incorporated into UK legislation through the Package Travel Regulations 2018.
<b>Package Travel Regulations (PTR) 2018</b>	See Package Travel Directive 2015.
<b>PayPal Buyer Scheme</b>	A scheme offering protection to consumers who pay with PayPal, if there is a problem with the transaction.
<b>Prudential Regulation Authority (PRA)</b>	Regulator responsible for supervision of around 1,500 UK banks, building societies, credit unions, insurers and major investment firms in the UK.
<b>Pool Re</b>	Pool Re offers reinsurance in relation to terrorism risk in the UK. If losses ever became so large as to exhaust its reserves, Pool Re would draw funds from the UK government to meet its obligations. Pool Re, in turn, pays a premium to government for this cover and would be required to repay any funds drawn down in this way from its future income.
<b>Regulation (EC) 1008/2008</b>	Common rules set out by the EC for the operation of air services in the Community.
<b>Regulation (EC) 261/2004</b>	Common rules set out by the EC on compensation and assistance to airline passengers in the event of denied boarding, flight cancellations, or long delays of flights.
<b>Rescue Fares</b>	A discounted fare offered by other airlines to aid repatriation of passengers who are booked to return home with an airline that has gone out of business.
<b>Route Density</b>	The available capacity between a given pair of destinations.
<b>Section 23 Civil Aviation Act 1982</b>	Prohibits the disclosure of information that relates to a particular person and has been furnished to the CAA in pursuance of any provision of the Act, other than in particular circumstances as set out in the Act.
<b>Scheduled Airline Failure Insurance (SAFI)</b>	Insurance that protects the policyholder against losses arising from airline insolvencies. See also End Supplier Failure Insurance.
<b>Section 75 of the Consumer Credit Act 1974</b>	Section 75 legislates that a credit card issuer is jointly and severally liable to its cardholders when they suffer losses because the merchant fails to supply goods that have been purchased using the issuer's card, or the goods are defective.

<b>Self-repatriation</b>	Repatriation mechanism wherein passengers buy seats on other airlines to get themselves home, sometimes benefiting from 'Rescue Fares'.
<b>Solvency II Directive</b>	Solvency II is an EU Directive implemented in all 28 Member States, including the UK, by 01 January 2016. It introduced a harmonised EU-wide regulatory regime for insurance providers.
<b>Special Administration Regime (for airlines)</b>	A proposed new type of Administration which would achieve greater legal certainty, and control of the timing of administration, and delivery of the repatriation by enabling an orderly wind down.
<b>Spot market</b>	Market where commodities are traded for immediate delivery.
<b>Statutory protection</b>	Financial protection that an organisation is legislatively obligated to provide.
<b>Steer</b>	Provider of administration and finance advice on how to deliver an orderly wind down; and how to finance and fund repatriation to the Review. Formerly known as Steer Davies Gleave (SDG).
<b>UK-originating passenger</b>	An air passenger whose journey began in the UK, and who has a ticket to return.
<b>Wet Leasing</b>	A wet lease is a leasing arrangement whereby one airline (the lessor) provides an aircraft, crew, maintenance, and insurance (ACMI) to another airline (the lessee). The lessee pays the lessor by the hours the aircraft is operated. The lessee provides fuel and covers airport fees, and any other duties, taxes, etc. Flights are operated under the flight number of the lessee.



