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COMMISSION OF THE EUROPEAN COMMUNITIES

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**REPORT FROM THE COMMISSION**

**on financing aviation security**

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#### **INTRODUCTION**

1. The terrorist attacks of 11 September 2001 in the United States had a profound impact on the global aviation sector as well as on the European aviation sector. Strong measures were essential to address the threats posed by international terrorism and to restore public confidence in the aviation sector. The European Union therefore took immediate steps to adopt new rules on aviation security.
2. These new rules on aviation security obliged Member States to introduce new measures that inevitably meant making significant investments in infrastructure, technical equipment and human resources at most European airports. The need for increased security controls also affected airport operations. According to ACI-Europe, security costs now represent up to 35% of overall airport operating costs instead of 5% to 8% prior to the events of September 2001.
3. Consequently, the financing of these new measures is again on the policy agenda of the European Union, as confirmed by Article 22 of the new framework Regulation (EC) No 300/2008.
4. Following the adoption on 11 March 2008 of the revised framework Regulation (EC) No 300/2008 on aviation security, the Commission is obliged to report on the principles of financing the costs of civil aviation security measures. This Commission report sets out to comply with this requirement and to prepare policy conclusions on this important matter.
5. The report addresses four issues: whether security charges are exclusively used to meet security costs, the transparency of security charges, the impact of aviation security and its financing on competition between airports and between airlines, and consumer protection as regards the distribution of the costs of security measures between taxpayers and users.
6. To prepare the report, the Commission sent a questionnaire to Member States, representatives from industry and consumer organisations. The questionnaire asked Member States whether existing national legislation ensured transparency and that security levies are used to exclusively to meet security costs. 5 Member States replied that existing airport charges consultations provide airlines with sufficient information on security costs as well. Similarly for cost-relatedness of security levies, 11 Member States replied that the same consultations ensure that security levies are used to exclusively to meet security costs. However, these consultations do not require the approval of the operators to modify security levies and do therefore not ensure transparency and cost-relatedness. Actually, only the Netherlands have specific legislation in force requiring security levies to be both transparent and cost-related. The Italian legislation, which is the other national legislation targeting security levies, only ensures transparency. The replies also confirmed that aviation security is mainly financed through security levies on airlines, air passengers and

cargo shippers. This is usually referred to the "user-pays" principle. 11 Member States rely almost entirely on such levies. 6 Member States sometimes make significant contributions to the security costs. 4 Member States did not reply or did not reply in sufficient detail for the Commission to draw any conclusions on their replies.

7. Organisations representing airlines, airports and consumers were asked to provide information on the cost and impact of aviation security. 9 organisations, mainly airport and airline organisations, replied and they all argued that States should cover for security costs because the threats are targeted against States and not against the industry. Unfortunately, only one consumer organisation replied to the questionnaire. Several replies argued that aviation is at a disadvantage in comparison with financing security in other transport modes and that this negatively impacts the competitiveness of the European aviation sector. All stakeholder replies endorsed increased cooperation within the International Civil Aviation Organization (ICAO) as the best solution to harmonise international aviation security measures and address differences in the level of state-funding between the EU and its main trade partners.

## **BACKGROUND**

8. The main cost for aviation security is airport security services to screen passengers and cargo, which usually has two main components: staff costs and costs for infrastructure and equipment.
9. As aviation security is a core state responsibility, national authorities are ultimately responsible for these services. National authorities can either provide these services themselves or delegate them to the airport, which may subcontract some of the tasks to security contractors.
10. To finance airport security services, the airport or the national authorities can levy a tax, a fee or a charge on airlines, passengers and cargo shippers. However, these levies usually do not cover the costs of measures imposed directly on airlines or the additional operational costs these measures may cause for airlines. Some costs of aviation security are also borne by the Member States.
11. Following the implementation of new European rules in 2002, the overall cost of aviation security increased. Significant new investments were necessary, such as the refurbishment of some airport terminals, the acquisition of additional screening equipment and the recruitment of additional staff to meet the increased requirements on security controls of passengers and cargo.
12. Before 2001 security costs were often a component of the passenger charge that airports levy to cover the cost of terminals. When airports consulted with airlines on airport charges, security charges were therefore also discussed. Security costs were previously a negligible part of total airline cost and airlines did therefore not insist on more information on these costs. However, with increased security costs in 2002 it became more common to separate security levies from airport charges. A separation also allowed the air transport industry to focus the attention of its customers on security costs.

13. Separating security levies from airport charges did not significantly increase transparency of security costs. Replies to the questionnaire confirmed that security costs are passed on to cargo shippers and air passengers, with no possibility for them to assess whether the correct amount is levied. One reply pointed out that airline customers may be charged for additional services that are not mandatory. Actually, a customer may even disagree with the airline that the security levy recovers the relevant cost.
14. The rise in costs fuelled a discussion on financing aviation security. The air transport industry has argued since then that the share of public financing of aviation should increase as these measures generally aim to protect against attacks on society as a whole and not the aviation industry and its customers.
15. The European Parliament used similar arguments during the discussions with the Council on the first framework Regulation (EC) No 2320/2002 on civil aviation security. The European Parliament wanted to prevent the whole cost of increased aviation security being imposed on air passengers, cargo shippers and airlines.
16. The European Parliament, the Council and the European Commission therefore agreed to address the issue of financing in a declaration attached to the decision on Regulation (EC) No 2320/2002<sup>1</sup>. In the declaration, the three institutions recognised that new aviation security measures raise important issues on financing and asked for further analyses to identify differences existing in the Community in financing aviation security and solutions to any potential distortions to the aviation market.
17. External consultants were commissioned to analyse the issues raised in the inter-institutional declaration. The consultants analysed the situation in 2002 and the study was published in 2004.<sup>2</sup> The study was mainly based on analysis of replies to questionnaires sent to Member States and industry. The findings of the study can be summarised as follows:
  - The users of the European air transport system (airlines, air passengers, cargo shippers) are ultimately the main funder of aviation security.
  - The security costs for airports and States in 2002 for the then 15 Member States and Norway, Iceland and Switzerland were estimated at €2 billion. Including the costs to the airlines to comply with new European rules, total security costs were estimated to €2.6 to 3.5 billion, which at that time corresponded to between 1% and 2% of an average air fare.
  - The consultants did not find sufficient evidence to conclude that the increase in security charges reduced the demand for air travel. Although, the data available were insufficient to produce a solid economic analysis.

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<sup>1</sup> Interinstitutional Declaration accompanying Regulation (EC) No 2320/2002 of the European Parliament and of the Council of 16 December 2002 establishing common rules in the field of civil aviation security (OJ L 355 of 30.12.2002, p. 22).

<sup>2</sup> Study on Civil Aviation Security Financing, September 2004, Irish Aviation Authority and aviasolutions.

18. During the conciliation process on the new framework Regulation (EC) No 300/2008, the European Parliament reiterated its position on financing security. The Council and the European Parliament discussed the financial impact of more stringent measures imposed by some Member States that go beyond the minimum requirements. Article 6 of Framework Regulation (EC) No 2320/2002 provides for this. The European Parliament argued in particular that Member States should pay the costs of more stringent measures exceeding EU requirements from public budgets, at least in part. The Council, however, rejected this request for Member States to commit themselves to increased public financing for aviation security.
19. The Commission had already proposed establishing new European rules for levying security charges. The proposal for a Directive on airport charges, which was presented on 24 January 2007, addressed financing airport infrastructure in general and contained a provision on security charges.<sup>3</sup> The proposal was based on internationally accepted principles already endorsed by the International Civil Aviation Organization (ICAO).<sup>4</sup> However, the Council preferred to await this report before considering new EU legislation on the provision of security charges.

## SECURITY CHARGES AND COSTS

20. The first of the four issues in this report concerns the steps to be taken to ensure that security charges are used exclusively to meet security costs. This is an internationally accepted principle endorsed by the ICAO.<sup>5</sup>
21. In general, a charge, unlike a tax, is levied in return for a service provided to the user. The level of the charge should therefore correspond to the cost of providing this service. In the same way, revenues from security charges should only cover the total cost of aviation security services.
22. This principle is supported by EU rules on State aid. In the 2006 report on financing transport security, the Commission clarified that measures to protect European citizens against terrorist attacks are not primarily an economic activity as they are essentially a state responsibility.<sup>6</sup> Public financing of such measures therefore does not fall within the scope of the rules on State aid.<sup>7</sup> However this does not mean that Member States should cover all costs of aviation security.
23. Financing aviation security activities, be it through public financing or through charges levied on the users, must therefore be strictly limited to compensating for the costs to which they give rise.<sup>8</sup> Any overcompensation for aviation security services falls within the scope of the rules on State aid as it could constitute operating aid to the recipient.

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<sup>3</sup> COM(2006) 820 final of 24.1.2007.

<sup>4</sup> ICAO's Policies on Charges for Airports and Air Navigation Services (Doc 9082/7), 2004, point 15.

<sup>5</sup> ICAO's Policies on Charges for Airports and Air Navigation Services (Doc 9082/7), 2004, point 29.

<sup>6</sup> COM(2006) 431 final of 1.8.2006.

<sup>7</sup> See para.33, Community guidelines on financing of airports and start-up aid to airlines departing from regional airports, (OJ C 312 of 9.12.2005).

<sup>8</sup> See Case C-343/95 *Calì & Figli v Servizi ecologici porto di Genova* [1997] ECR I-1547. Commission Decision N 309/2002 of 19 March 2003, Aviation security — compensation for costs incurred following the attacks of 11 September 2001. Commission Decision N 438/2002 of 16 October 2002, Aid in support of public authority functions in the port sector.

24. The replies to the questionnaire confirmed that only very few Member States have legislation in force explicitly prohibiting windfall profits in conjunction with the mandatory imposition of security levies. Other Member States referred to legislation stipulating that security charges must be based on the actual cost of providing the service, which would imply that the level of security charges cannot exceed the cost of security measures. In some Member States security charges are approved by competent authorities before they enter into force.
25. Even though the replies to the questionnaire confirmed a general consensus that security charges should reflect security costs, the Commission is not convinced that this principle is respected at all European airports. For example, the Commission recently opened a State aid investigation at an airport where there were indications that the airport, as aviation security provider, was being overcompensated.

## **TRANSPARENCY**

26. The second aspect concerns the transparency of security charges. The Commission understands that the transparency of security charges relates to information on the components used to calculate the amount of security charges. This information is necessary to identify discrimination and thereby ensure consumer protection.
27. Transparency also makes it possible to ensure that revenues from security charges do not exceed the cost of aviation security. Passengers, cargo shippers and airlines can then verify that security charges only cover relevant costs. Similarly, transparency unveils potential discrimination among airlines or air passengers concerning security charges.
28. From the questionnaire it is evident that most Member States do not have measures in place which explicitly allow airlines or any other party to regularly scrutinise security charges or associated costs. A number of Member States rely on the consultation of airport charges with airlines. These consultations, however seldom, are regulated by national law. A few Member States replied that security costs are clearly separated from other airport costs, which would give Member States the information necessary to verify whether the correct amounts of security charges are levied.
29. The Commission takes the view security charges must be transparent and that minimum EU standards may have to be established to ensure this. This could be coupled with procedures to lodge formal complaints where the amount of security charges/taxes/fees is disputed.

## **IMPACT ON COMPETITION**

30. The third issue for this report concerns the principles necessary to safeguard undistorted competition between airports and between airlines. The European Parliament argues that differences between Member States with regard to aviation security may distort the European aviation market. These differences consist of either as different levels of public financing or additional measures imposed by some Member States.

31. The replies to the questionnaire and the 2004 study confirm that Member States do not provide the same amount of public financing for aviation security. Only a very small number of Member States finance a significant proportion of the overall security cost, while most Member States finance a smaller share from public budgets. Differences in the proportion of public financing translate into differences in the amount of security levies.
32. Competition between airports can be assessed in the light of airlines' criteria of choice, and in particular by comparing factors such as the type of airport services provided and the clients concerned, population or economic activity, congestion, whether there is access by land, and also the level of charges for use of the airport infrastructure and services.<sup>9</sup>
33. In the airport industry there are currently several different levels of competition between the different types of airport. Competition scenarios are evaluated case by case, based on the markets in question. However, research has shown that, generally, major international hubs are competing with similar airports in all the transport markets concerned, with the level of competition depending on factors such as congestion and the existence of alternative transport, or, in certain cases, with large regional airports.<sup>10</sup> Large regional airports may be competing not only with other large regional airports but also with the major international airports and land transport, especially if there is high-quality land access to the airport. This research has also shown that small airports do not generally compete with other airports except, in some cases, with neighbouring airports of a similar size whose markets overlap.<sup>11</sup> Consequently, security levies may in theory affect competition between airports. However, this impact is probably minimal because of the low level of these levies and the higher importance of other factors.
34. Competition between airlines may also be impacted by differences in the amount of security levies. However, the 2004 study did not find any evidence that security levies represent a deterrent to air travel demand. The overall level of security costs have also decreased since then and are therefore even less likely the impact competition between airlines.
35. Competition between airports and between airlines is therefore not likely to be significantly impacted by differences in the security levies between Member States, provided that such differences do not discriminate between airlines, air passengers or cargo shippers. Transparency of security costs is necessary to verify that security levies are non-discriminatory and therefore also important to ensure the security levies do not distort competition between airlines. However, the replies to the questionnaire made it clear that there is increasing evidence that security cost are not transparent to the airlines, air passengers and cargo shippers. Some replies argued that increased transparency would make to provision of airport security services more efficient with significant cost savings to the aviation sector as a result. In

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<sup>9</sup> See para. 38, Community guidelines on financing of airports and start-up aid to airlines departing from regional airports, (OJ C 312 of 9.12.2005).

<sup>10</sup> 'Study on competition between airports and the application of State aid rules' – Cranfield University, June 2002.

<sup>11</sup> See para. 11, Community guidelines on financing of airports and start-up aid to airlines departing from regional airports, (OJ C 312 of 9.12.2005).



addition, as confirmed by the replies to the questionnaire existing national procedures for ensuring adequate transparency of security costs in the EU are not satisfactory.

36. Competition between airlines and between airports may also be impacted by differences in the implementation of aviation security measures. Member States can choose to implement additional, more stringent measures than those required by EU laws on civil aviation security. Airlines and also airports operating in Member States which impose more stringent measures than required by the Regulation may be disadvantaged to other airports or airlines.
37. The most stringent measure with probably the greatest impact on the overall level of security costs is the requirement to re-screen transfer passengers and their luggage that have already been screened on departure from another EU airport. Not requiring re-screening of already screened transfer passengers is usually referred to applying "one-stop" security. This requirement also increases the total cost of aviation security. The Association of European Airlines (AEA), in the answer to the questionnaire, argued that airports applying "one-stop" security have significantly lower security charges.
38. The Commission's view is that re-screening transfer passengers may have been justified before the entry into force of the first framework regulation establishing mandatory standards to be implemented at all EU airports but is no longer required on security grounds. A further quality control layer was added in early 2004 when the Commission started inspecting airports and the relevant authorities of Member States. If these inspections were to find serious deficiencies at an airport deemed to have significant impact on the overall level of civil aviation security, then the implementation of "one-stop" security will be suspended through a Commission decision. This has so far been used 18 times, which illustrates the determination of the Commission to take the necessary action to ensure a high and uniform level of security controls at all EU airports.
39. Other more stringent measures implemented by certain Member states may also give rise to competition issues and considerations on the necessary level of security measures across the EU. However, Member States should have sufficient flexibility to cater for the consequences of higher security risks in some Member states. This is the rationale behind Article 6 of Regulation (EC) 300/2008, which explicitly confirms the right of Member states to implement, under certain conditions, measures more stringent than those laid down in Community law.
40. Consequently, the Commission is of the opinion that adequately screened passengers do not need to be re-screened when transferring, provided that the layout of the airport infrastructure allows for a strict separation of passengers screened at EU quality level and others.

#### **CONSUMER PROTECTION**

41. Article 22 of Regulation (EC) No 300/08 requires the fourth issue of this report to address consumer protection as regards the distribution of the costs of security measures between taxpayers and users.

42. As stated above, the provision of aviation security at European airports is essentially a state responsibility. Whether these measures are financed by a levy on the users or by the public budget does not necessarily impact consumer protection. It may actually be reasonable that security measures are financed, at least in part, by passengers, cargo shippers and airlines as they are best placed to scrutinise the cost implications of security measures, on condition, however, that such levies are exclusively used to meet security costs.
43. Sometimes airlines reveal the different components of the total air fare, including security charges, to passengers. There have been concerns as to whether the amount of security charges corresponds to the actual security charge levied on the airline. However, this issue is addressed in the revised third aviation package, which governs the economic aspects of the internal aviation market in the European Union.<sup>12</sup> The provision on charges, including security charges, obliges airlines that reveal the different components of the air fare to quote the correct amount.

## CONCLUSIONS

- Aviation security at European airports is essentially a state responsibility. This, however, does not necessarily mean that aviation security measures should be publicly financed. The user-pays principle also has its merits.
- The Commission takes the view that the following aspects are important for protecting consumer interest and for upholding the user-pays principle:
  - security fees, charges or taxes do not discriminate among operators and
  - security fees, charges or taxes are exclusively used to meet security costs.
- The Commission believes that new rules on the transparency of security costs are required to identify potential discriminatory security charges/taxes/fees. The bodies levying aviation security charges or taxes should therefore regularly provide operators with information on the components used to calculate these charges or taxes.
- The Commission carries out security inspections of European airports, which ensure the overall level of security across the EU. It may, therefore suffice to apply the appropriate security measures at the point of origin only, thereby removing the requirement to repeat these measures at the point of transfer. Re-screening passengers is evidently more costly than applying “one-stop” security. Intra-EU “one-stop” security could therefore be considered as obligatory at all European airports, provided the infrastructure separates passengers screened under EU requirements from other passengers.
- However, the aspects above require a further assessment on the basis of rules agreed between the EU institutions (impact assessment). The Commission intends to continue preparing a legislative initiative based on this assessment, in particular

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<sup>12</sup> Regulation (EC) No 1008/2008 on common rules for the operation of air services in the Community (OJ L 293 of 31.10.2008, p. 3).

on the impact of aviation security on consumers and the functioning of the internal aviation market.