COMMISSION OF THE EUROPEAN COMMUNITIES

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COMMUNICATION FROM THE COMMISSION

Developing a Community civil aviation policy towards Australia

1. INTRODUCTION

1.1 Traditionally, international air transport is governed by bilateral agreements between individual states. However, the so-called "open skies" judgements of 5 November 2002 of the European Court of Justice marked the start of an external aviation policy at Community level.

As outlined in the Communication of the European Commission "*Developing the agenda for the Community's external aviation policy*"[1], agreements between the European Community and certain third countries will have the substantial added value of creating new economic opportunities by opening up markets and promoting investment opportunities. Furthermore, such agreements will be the best way to ensure fair competition by promoting regulatory convergence.

Therefore, the European Commission has proposed to launch targeted negotiations seeking to achieve comprehensive aviation agreements in the major regions of the world, with the aim of strengthening the prospects for promoting European industry and ensuring fair competition, while at the same time seeking to reform international civil aviation.

1.2 In October 2003 Australia requested to start negotiations on an agreement on the liberalisation of air transport with the European Community. With its market-oriented economic and transport policy and high regulatory standards, Australia is an obvious and promising candidate for a new-generation of air transport agreement with the European Community.

This is why Australia was identified in the Commission's Communication "Developing the agenda for the Community's external aviation policy" as a possible key target country for a Community-wide agreement. In its Conclusions on external aviation relations, the Council has explicitly taken note of Australia as a potential candidate for a future request for comprehensive negotiating mandates.[2]

1.3 Furthermore, Australia has demonstrated its commitment to reforming the framework for air transport jointly with the European Community by initialling an agreement on certain aspects of air services with the European Community on 7 April 2005.

An agreement on the liberalisation of air transport with Australia will further strengthen the good relations with Australia that shares the Community's objectives of reforming the framework for international air transport. It will bring economic benefits to air carriers, airports, passengers, shippers, the tourism industry and the wider economy both within the European Union and in Australia. In addition and equally importantly, it will be a milestone on the path towards an international reform of the regulatory framework governing the air transport sector.

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1 COM(2005) 79 final, dated 11.3.2005.

2 Council Conclusions of 27 June 2005 on developing the agenda for the Community's external aviation policy.

1.4 With this Communication, the Commission therefore recommends that the Council authorises the Commission to negotiate a comprehensive agreement on an Open Aviation Area with Australia combining market opening with a parallel process of regulatory co-operation and/or convergence notably in priority areas such as aviation safety, security, environmental protection, protection of passengers and application of competition rules ensuring a level playing field and fair and equal conditions for competition.

Positive exploratory contacts between the Department of Transport and Regional Services of Australia and the services of the European Commission have been developed over the past few years, which may serve as a good basis for entering into formal negotiations with Australia.

2. THE EXISTING REGULATORY FRAMEWORK FOR AIR SERVICES BETWEEN THE EUROPEAN COMMUNITY AND AUSTRALIA

Bilateral air services agreements between EU Member States and Australia

2.1 Currently, air transport between Australia and the EU is governed by 15 bilateral air services agreements.[3] There is at present no legal basis for air services between Australia and the other 10 EU Member States.

The existing regulatory framework for air services between the Community and Australia does not allow airlines, passengers and shippers to take full advantage of the benefits of free markets. The existing bilateral air services agreements establish an imbalanced framework for air services between the EU and Australia as not all agreements are equally liberal with regard to freedoms and capacities available. These differences in the Member States' bilateral air services agreements with Australia lead to inequalities in the opportunities available to Community air carriers.

2.2 Like most bilateral air services agreements, the existing bilateral air services agreements between EU Member States and Australia contain nationality restrictions that have been found illegal by the European Court of Justice. In April 2005, the European Commission reached an agreement with the Australian aviation authorities on certain aspects of air services ("Horizontal Agreement")[4] that replaces these nationality clauses with a Community clause. This agreement allows all EU airlines in principle, subject to traffic rights available, to operate flights to Australia from any EU Member State where they are established. Due to the above-mentioned imbalances, it was necessary to include a "no-circumvention" clause in the recent "Horizontal Agreement" with Australia in order to avoid possible circumvention of the existing different bilateral restrictions on traffic rights.

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3 Austria, Czech Republic, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Malta, the Netherlands, Poland, Sweden and the United Kingdom have concluded bilateral air services agreements with Australia.

4 Proposal for a Council Decision on the signature and the provisional application of the Agreement between the European Community and the Commonwealth of Australia on certain aspects of air services, COM(2005) 264.

The regulatory framework for air transport in Australia

2.3 In recent years, Australia has introduced major changes to its aviation policy in order to promote travel, trade and tourism. The aviation policy that Australia has been pursuing includes liberalising international air services agreements, liberalising airline ownership and liberalising international aviation multilaterally.

2.4 Traffic rights that are available to Australian air carriers under the bilateral air services agreements are allocated to individual air carriers by the independent International Air Services Commission. The objective of allocation of traffic rights is to promote economic efficiency through competition in the provision of international air services.[5]

2.5 Australia has concluded "open skies" agreements with unlimited traffic rights for cargo-only flights with 22 countries.

Between Australia and New Zealand, a Single Aviation Market (SAM) was agreed in 1996 and completed in 2002. Following the establishment of the Single Aviation Market, the number of scheduled passenger airlines between Australia and New Zealand has increased to 12 carriers with significant increases in passenger traffic as a result. The Single Aviation Market gives Australian carriers access to domestic flights in New Zealand and vice versa.

Within the SAM, carriers of both countries may, provided that they meet for operating within the domestic market of either Australia or New Zealand and be at least 50% owned and be controlled by Australian and/or New Zealand nationals, operate any capacity, including cabotage, as it decides without any restrictions. The aviation safety authorities of the two countries have also agreed to mutual recognition of all aviation-related certification.

2.6 Following the deregulation of the Australian market in 1990, there are no foreign ownership limitations for domestic airlines except with regard to Qantas. Foreign persons, including foreign airlines, are allowed to hold up to 100% equity in an Australian domestic airline. However, foreign ownership in international airlines is limited to 49% to ensure that other countries will accept airline designation since most bilateral air services agreements are still based on the traditional national ownership requirements.[6] Specific ownership and control rules are set for Australia's main international air carrier in the Qantas Sale Act of 1992 which limits ownership by a single foreign investor to 25%. However, the Australian Government is currently considering a removal of the foreign ownership restrictions for Qantas.

2.7 Anti-competitive behaviour in the air transport sector is prohibited by the Trade Practices Act which is enforced by the Australian Competition and Consumer Commission.

The Civil Aviation Safety Authority is responsible for aircraft certification, licensing and safety oversight including inspections of foreign aircraft. Air carriers registered in Australia have an excellent safety record.

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5 International Air Services Commission Act 1992, Section 3.

6 Air Navigation Act 1920, Section 11A.

3. FURTHER STRENGTHENING RELATIONS BETWEEN THE EUROPEAN UNION AND AUSTRALIA

3.1 Australia is a close political partner of the European Union. The relationship between the European Union and Australia is characterised by common values and convergent global objectives.

The European Union and Australia have sealed their bilateral co-operation with a Joint Declaration in 1997, based on the common wish of promoting a sound development of the world economy based on free and open market principles.

3.2 In their economic relationship, the European Union is Australia's largest trading partner. Exports from the European Union to Australia have steadily increased and reached a value of € 18 billion in 2003. Imports to the European Union from Australia account for € 9 billion in 2003. Furthermore, the European Union is the largest trading partner in services for Australia. Trade in services between Australia and the European Union continues to grow and in 2003 trade in services accounted for nearly 40% of overall trade with a substantial share provided by transport services. The European Union is also the most important source of foreign investment in Australia and the second major destination for Australian investments abroad.

3.3 The Agenda for Co-operation between the European Union and Australia as reviewed in 2004 includes a close co-operation between the two partners aimed to promote liberalisation of air transport in the different international fora concerned. Furthermore, in line with the shared commitment to aviation liberalisation, bilateral discussions in the field of air transport are welcomed.

In February 2005, the Australian government confirmed its interest in an aviation agreement with the Community at the EU-Australia ministerial troika meeting. An aviation agreement would contribute significantly to further strengthening bilateral relations between the European Union and Australia.

4. ECONOMIC BENEFITS OF A COMPREHENSIVE AIR TRANSPORT AGREEMENT BETWEEN THE EUROPEAN COMMUNITY AND AUSTRALIA

4.1 Around one million passengers are carried annually on direct flights between the European Union and Australia. Direct passenger flights between the European Union and Australia are currently operated by Qantas and British Airways in a Joint Service Agreement and by Austrian Airlines and by Virgin Atlantic. However, due to the long distance, flights between Europe and Australia require one intermediate stop. As a consequence, indirect routes with connecting flights from South-East Asia or the Gulf region are a close substitute for direct one-stop flights between the European Union and Australia.

About 50% of all passengers flying between the EU and Australia are carried by Asian or Middle Eastern air carriers on indirect routes between the European Union and Australia.[7] The overall annual market size of air services between the European

[7] Source: Australian Competition and Consumer Commission (2004).

Union and Australia is therefore close to 2 million passengers. This makes Australia one of the largest long-distance air transport markets for the European Union.

4.2 Most flights between Europe and Australia are operated on a one-stop basis via intermediate points in Asia. Since the economic viability of such operations depends on the possibility of carrying passengers between the intermediate point and Australia, fifth freedom rights[8] between Australia and intermediate points are of substantial economic value for EU air carriers. The EU air carriers operating flights to and from Australia carry a substantial share of passengers and freight between Australia on the one side and Singapore, Thailand, Malaysia and Hong Kong on the other.

Benefits and added value of a Community approach

4.3 Even if the immediate economic impact of a liberalisation of air transport between the European Community and Australia might be moderate for the EU economy in the short term, given the limited share of direct flights in the EU-Australia market, the lifting of restrictions could enhance market opportunities for EU air carriers and increase the importance of direct flights in the total EU-Australia market. The removal of all restrictions between the EU and Australia would increase the ability of EU air carriers to compete with carriers from the Middle or Far East which have captured a substantial share of the EU-Australia market. This would give EU passengers an even wider choice of flights to Australia. It would allow EU air carriers to increase their market share on an important long-haul market.

An increase in (direct) air services would enhance trade and tourism flows between the EU and Australia and, hence, bring wider economic benefits to the EU economy. Airports and aviation-related industries as well as the aircraft manufacturing industry would also benefit from a further increase in air services between the EU and Australia.

4.4 With its modern regulatory framework and its market oriented economic and transport policy, Australia is an obvious candidate for deepening of aviation relations with the Community in an Open Aviation Area – both in terms of market access and in terms of regulatory co-operation and convergence. Enhanced regulatory co-operation between the EU and Australia would facilitate further the air services between the EU and Australia.

4.5 However, even more important than the short-term economic impact is the medium-term economic impact on other air transport markets. The economic benefits of open international aviation markets have been clearly identified in a study conducted on behalf of the European Commission on the economic impact of an EU-US Open Aviation Area.[9] Released from the existing restrictions on the number of weekly flights and flight routes, air traffic is likely to increase. With open market access, airlines will be able to take advantage of new market opportunities and offer air

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8 Fifth-freedom rights are the rights of an air carrier to carry passengers and freight from a country to a third country on services starting in its home country, e.g. the right of an UK carrier to carry passengers between Singapore and Australia on a flight starting in the UK.

9 The Brattle Group, The Economic Impact of an EU-US Open Aviation Area, Study prepared for the European Commission, December 2002.

services on the routes where their customers demand it. Cross-border investment flows will bring further efficiency gains.

A full liberalisation of air transport with Australia can only be achieved on a Community level. Since EU law sets the ownership requirements for EU carriers, a reciprocal liberalisation of ownership and control requirements needs to be done by the Community.

The wider impact on air transport relations with other third countries would bring significant economic benefits for the European economy. Due to the Single Aviation Market between Australia and New Zealand and the high level of integration already achieved between these two markets, the benefits of an Open Aviation Area with Australia would be reinforced as the combined market would be larger.

As a consequence of open aviation markets:

– airlines would further increase their efficiency and improve their international competitiveness,

– passengers and shippers would benefit from more choice,

– airports, aviation-related services and the aircraft manufacturing industry would benefit from an increase in air transport,

– the increase in traffic would facilitate a further increase in trade and tourism flows.

4.6 The clear potential benefits of an Open Aviation Area Agreement with Australia have been confirmed in an impact assessment study carried out by independent consultants. While the short-term economic benefits may be relatively limited due to the absence of non-stop flights between the Community and Australia and the already existing degree of market access, the economic impact of an agreement with Australia would nonetheless be considerable. The recent study has confirmed that the regulatory and policy framework for air transport in Australia would allow the Community to achieve a model agreement with Australia which would result in greater levels of regulatory convergence and new opportunities for EU industry and users. An OAA with Australia could increase the competitiveness of EU airlines vis-à-vis competitors from the Middle and Far East in the EU-Australia market. It could lead to an increase in direct flights between the EU and Australia and to a better distribution of air traffic which today is highly concentrated on London. It could lead to more one-stop services between EU cities and Australian destinations, thereby increasing the convenience for EU passengers. Furthermore, the study underlined the substantial economic benefits in the longer term for the European airline industry, air transport users and other economic actors, taking into account the implications for relations with other countries.

5. CONCLUSIONS: SUBSTANTIAL ADDED VALUE OF A FUTURE EU-AUSTRALIA AIR TRANSPORT AGREEMENT

5.1 A modernised framework for air transport between the EU and Australia offers significant new opportunities for strengthening air transport in a competitive and level playing field. In addition, it would further strengthen the already excellent commercial and political relations between the EU and Australia.

The model of an air transport partnership between the European Union and Australia is inspired by the ambition to take forward an agenda for reform at the international level. The resulting agreement on the liberalisation of air transport between the European Community and Australia would replace the existing bilateral air services agreements between Australia and EU Member States and establish a modern framework for air services between the EU and Australia, with market access as open as possible and regulatory standards as high as possible. It could thereby be the model for an extended air transport partnership with other third countries.

5.2 The negotiations of an Open Aviation Area agreement with Australia would aim at an opening of market access and an opening of investment opportunities. The opening of market access can not be limited to third- and fourth-freedom rights but need to include fifth-freedom rights.[10] Australia can not be served with non-stop flights from Europe. Therefore, air services between the EU and Australia are operated on a one-stop basis via intermediate points which are significant markets in their own right, e.g. Singapore, Thailand or Hong Kong. It would not be economically viable to operate the air service between the intermediate points and Australia without the respective traffic rights. Therefore, fifth-freedom rights via such intermediate points are essential in order to secure the potential benefits of the agreement.

The reciprocal opening of market access with Australia has already been implemented by some Member States. However, some Member States have not yet reached an advanced degree of market access in their relations with Australia. This imbalanced framework has led to inequalities in the opportunities of Community air carriers which are not consistent with the equal opportunities for all Community air carriers in the Single Market. A comprehensive air transport agreement on a Community level would make the Community's aviation relations with Australia coherent and would grant equal rights and opportunities for all Community air carriers for air services to Australia. Negotiations on a Community level could achieve full liberalisation. In recent bilateral negotiations with Member States, Australia indicated that a full liberalisation of market access, including seventh-freedom rights and eighth-freedom rights, could only be implemented with the Community and not with individual Member States.[11]

Furthermore, it would create new market opportunities for air carriers in those Member States that currently do not have any rights concerning air transport from and to Australia. An air transport agreement on Community level would also give smaller carriers the possibility to extend their network to Australia. While traffic demand between several Member States and Australia would not necessarily make

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10 Third-freedom is the right to carry passengers and freight from the EU to Australia. Fourth-freedom is the right to carry passengers and freight from Australia to the EU. Fifth-freedom is the right to carry passengers and freight from an intermediate point to Australia on a service starting in the EU.

11 Seventh-freedom is the right to carry passengers and freight between two countries outside the home country of the air carrier, e.g. an EU air carrier operating flights between Australia and New Zealand. Eight-freedom is the right to carry passengers and freight on domestic routes in a third country.

direct flights commercially viable, air carriers could pursue commercial benefits through code-sharing arrangements to and from Australia.

An EU-Australia agreement would allow the European airline industry to gain from more open market access to and from Australia. The removal of the existing restrictions would help the European airline industry to compete with the air carriers from the Middle and Far East which have captured a substantial market share on EU-Australia flights. The replacement of indirect flights via the Gulf region or South-East Asia with additional direct flights from the EU would benefit the EU airports. An EU-Australia OAA agreement would allow the European airline industry to invest in Australia and to benefit from capital originating from Australia. It would allow the European freight carriers to establish international freight lanes in the Asia-Pacific region and thereby to increase the efficiency of their operations and to enable services according to the needs of their global customers and no longer be constrained by the need to combine rights under bilateral agreements. Open markets and the resulting increase in competition on routes between Europe and Australia would bring additional benefits for European passengers and shippers.

5.3 Open aviation markets need a framework that ensures fair competition and high standards of safety, security and environmental protection. Therefore, an agreement would equally need to maintain and reinforce high standards of safety, security and environmental protection for air services between the European Union and Australia. It would establish a level playing field to avoid distortions of competition.

With respect to environmental issues, the agreement must be consistent with the EU's commitment to sustainable development. Apart from the economic benefits highlighted above, the expected growth in air traffic has also unwanted side-effects, notably on air quality and noise levels around airports and through the contribution to global climate change. It is important that the agreement does not restrict the EU's ability to apply regulatory or economic instruments to mitigate these adverse effects.

Safeguarding fair competition is another key issue in open aviation markets. By achieving greater levels of regulatory convergence, a comprehensive air transport agreement between the Community and Australia would ensure a competitive level playing field to avoid distortions of competition.

Australia is well prepared for a high level of regulatory convergence with the Community and the prospects for a high level of regulatory convergence between the Community and Australia are excellent.

Regulatory convergence can only be achieved at Community level. Bilateral agreements fall short of ensuring such an adequate regulatory co-operation. An EU-Australia agreement should establish co-operation mechanisms to ensure that the rules of the agreement are respected and further developed.

This partnership can be progressively developed towards an Open Aviation Area between the European Community and Australia. Exploratory talks have shown that Australia shares the ambitions of the Community to establish a modernised framework for international air services, free of existing restrictions and with the opportunity to provide services globally. The result of the proposed new partnership would send a clear signal to other third countries to join the trend towards a more flexible international framework for air transport.

5.4 The economic benefits of an air transport agreement with Australia would be further increased by similar agreements with countries in Asia that serve as main intermediate points. Hence, the new partnership between the European Union and Australia should be open for other countries that might wish to join.

5.5 The civil aviation sector offers significant new opportunities for strengthening transport sector co-operation and mutual benefits of Australia and the EU.

In light of the above, the European Commission therefore recommends that the Council authorises the Commission to open negotiations with Australia with a view to concluding a comprehensive air transport agreement.

5.6 The Commission will work closely together with Member States and all relevant stakeholders in further developing and achieving the objectives set out in the negotiating directives.