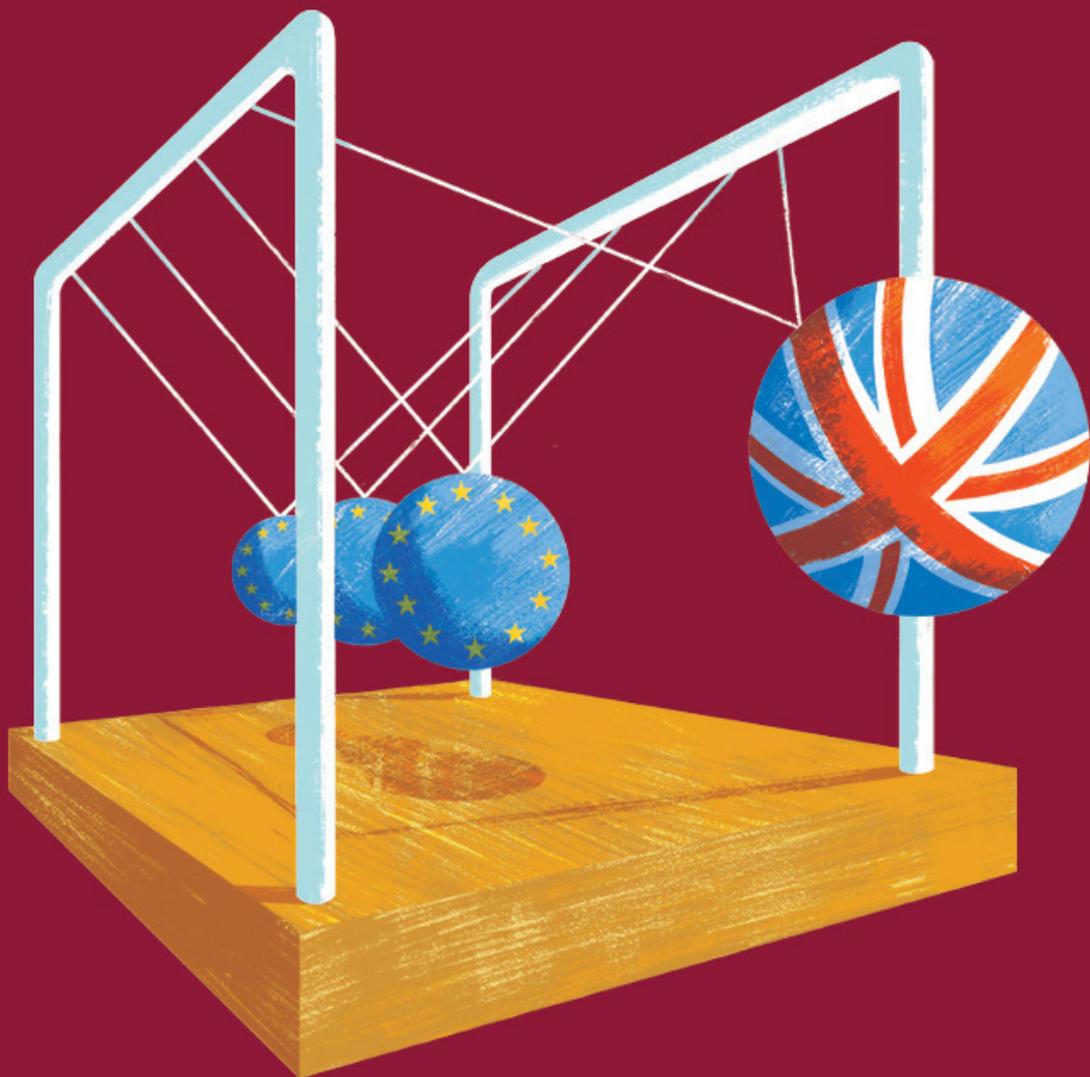


Brexit

An Overview of the Legal and Operational
Implications for the Aviation Industry



Introduction

Aviation is a strong driver of economic growth, jobs and trade in the EU and particularly in Ireland. Over the last 30 years, the EU has created the world's largest and arguably most successful example of regional market integration due to, amongst other factors, the liberalisation of air transport policies.

In March 2017, Article 50 was triggered by the UK Government, providing for a two year period to negotiate an agreement for the UK's exit from the EU.

We look at some of the legal and operational implications of Brexit on the air transport sector for Ireland, the United Kingdom and the European Union. We also identify some of the challenges to European external aviation policy in light of the UK's decision to leave the EU and areas where changes may arise.

EU External Aviation Policy

European aviation currently represents approximately 26% of the world's aviation market. It contributes €110 billion annually to the EU's Gross Domestic Product, and supports approximately 5.5 million jobs in the EU. With 918 million passengers travelling by air in the EU and more than 1.45 billion passengers departing or arriving at EU airports in 2015, aviation is vital to the connectivity of the EU globally and to its internal markets and to the daily lives of European citizens.

In late 2015, the EU Commission published a comprehensive Aviation Strategy for Europe. The Aviation Strategy is an ambitious plan. It set out to address and tackle the challenges facing the aviation industry as a key driver of the European economy. It is intended to be a constructive guide towards a more competitive industry.

The EU air transport market objectives include:

- promote consumer interests
- reduce barriers to trade
- maintain a level playing field for operators
- foster innovation
- maintain the highest levels of safety, and
- involve all stakeholders in the process.

These objectives are to be pursued in the EU and globally through the negotiation of new EU-level agreements with countries such as China, Turkey, United Arab Emirates, Kuwait and Qatar. The goal is to improve market access and to maintain the EU's position as a leading player in international aviation.

Brexit uncertainty is likely to lead to delays in implementation of the Aviation Strategy. It may divert the focus to internal issues in the EU rather than an outward focus towards the implementation of a global strategy for the EU. The negotiation of a flexible and innovative air transport agreement between the EU and the UK is necessary. It will benefit all in the context of the EU and access to the wider global markets for aviation.

Regulation of Air Transport

The aviation transport sector is a regulation intensive business. Aircraft, airlines, airports and staff engaged in the provision of services, on the ground and in the air, are required to be licenced, authorised and validated in the jurisdictions in which they operate. The international associations such as the International Civil Aviation Organization (ICAO) and the International Air Transport Association (IATA) play a significant role in global regulation and policy.

The European Aviation Safety Agency (EASA) was established in 2002 to harmonize safety, airworthiness and certification regimes across EU member states.

EASA is considered to be one of the world's leading aviation safety authorities. EASA is responsible for making recommendations and advising the EU Commission on the design and implementation of all aspects of civil aviation policy and regulation. Safety and security are crucial pre-requisites for public confidence in the aviation sector.

As an EU Member State, the UK participates in the management and legislative process of EASA. While it is not necessary to be an EU Member State or member of the European Common Aviation Area (ECAA) to be a member of EASA, as a non-EU Member State, the UK's current influence and ability to shape future legislation may be reduced in the aftermath of Brexit.

Under the Aviation Strategy, the EU Commission proposed a comprehensive revision of the Basic Regulation to give EASA greater power to define regulation by means of delegated acts. The UK's participation and influence in EASA as a non-EU Member State may be less when compared to the influence of the collective balance of EU Member States. The impact of total withdrawal by the UK from EASA, albeit unlikely, could be very significant.

There are precedents for non-EU participation in EASA, as is the case with Switzerland and the non-EU EEA states, Iceland, Liechtenstein and Norway. Perhaps the UK will participate in EASA in a manner similar to these countries post-Brexit, however the level of influence remains uncertain. To date, the UK together with Germany and France has been a prominent proponent of many European initiatives. As a result, the UK's continued involvement is important to ensure progress is made across a wide range of policy agendas. We will be monitoring future developments and progress of regulation in this sector.

Air Passenger Rights

In advocating a policy of uniformly protecting consumer rights, the EU introduced Regulation 261/2004. It provides air passengers with certain rights and remedies. These include compensation, assistance and re-routing in the event of flight delays, cancellation or where boarding is denied due to overselling of seats. Regulation 261/2004 has been a contentious issue for the air transport industry. The airlines have lobbied for the relaxation of compensation, especially when delays and cancellations are caused by extraordinary circumstances beyond their natural control. These circumstances can include weather related issues or the mandatory grounding of aircraft due to technical problems.

As a member of the EU and ECAA, UK airlines are currently bound by Regulation 261/2004. Airlines licenced in other countries are only bound by the regulation on flights outbound from EU countries. If the UK decides to repeal Regulation 261/2004, UK airlines would no longer be liable for claims relating to flights from the UK to the EU, or from the UK to third countries, reducing the costs of operating these services and potentially the airline ticket price.

Any savings to airlines and consumers has to be balanced against consumer reaction to reduced rights, compensation and protection and the overall customer service experience.

In October 2017, the public reaction to Ryanair's cancellation of numerous flights to and from the UK led to a PR media storm. It also precipitated the launch of an enforcement action by the Civil Aviation Authority of the UK. Given the significance of the UK as a connection point for international flights, including EU destinations, passenger rights is and will remain an area of concern for the travelling public.

EU Market Access for Airlines

The UK is likely to seek to retain access, equality and parity in the EU air transport market for its airlines and holders of air operating certificates. This could be achieved by entering into an ECAA Agreement post-Brexit. It is possible and foreseeable that an ECAA Agreement with the UK may contain a condition that it is subject to the full application of EU aviation law. It would also fall under the jurisdiction of the European Court of Justice (ECJ), and so would severely limit the UK's policy and regulatory freedom.

To date, the UK government has stated that it is not prepared to be subject to EU law post-Brexit in any area. It seeks to assert its authority and supremacy in law making and dispute resolution.

As an alternative, the UK may opt for a new form of bilateral agreement with the EU. This would emulate some aspects of the ECAA Agreement and other aspects of agreements in place with other countries outside of the geographical area of Europe, such as the US.

This issue could well become subsumed amongst the large volume of issues to be addressed and dealt with in the final exit agreement with the possibility of concessions and/or restrictions on UK airlines operating within the EU.

Moreover, market access considerations go beyond UK-EU routes. There is the question of whether or not UK airlines will be permitted to continue to operate as non-EU regulated airlines, operating to and from a non-EU member state before a bilateral agreement is concluded with that country.

The "Open Skies" judgements of 2002 marked the start of an EU external aviation policy. It established that in circumstances where the EU creates common rules, Member States are no longer competent to enter into obligations with non-member countries and the EU alone is entitled to assume these obligations. While the UK can replicate the open skies concepts, it may not be permitted to access or avail of any EU negotiated agreements in the post-Brexit era.

Following Brexit, the UK will have to replicate or originate new agreements with third countries. As a single country, the UK will not retain the same level of bargaining power, as a 500-million population trading bloc, which is the EU. Under EU law, the UK can neither strike nor begin to negotiate any trade agreement with countries outside of the EU until it has formally terminated its membership. This is expected to occur in March 2019.

Until March 2019, there is uncertainty for the sector which significantly impacts on future planning and scheduling of flights and route expansion for airlines.

EU Airline Ownership and Control Limitations

Currently, an airline seeking to obtain and/or maintain an EU air operating licence must satisfy the EU rules on ownership and control. EU Regulation 1008/2008 requires EU Member States or nationals of EU Member States to own more than 50% of an EU airline and effectively control it. Licence holders and applicants are required to provide evidence to the relevant licensing authority on the rights attaching to different classes of shares, as well as the ultimate beneficial owner of the shares.

Similar preconditions relating to nationality or qualified persons exist in non-EU jurisdictions. The restrictions apply, unless the EU agrees otherwise, with the third country concerned.

In the Aviation Strategy, the EU Commission highlighted that ownership and control requirements, included in Regulation 1008/2008, should be carefully scrutinised. This examination should consider the commercial and financial importance of airlines and the significant upfront financial costs to operate efficiently in a highly competitive environment. The EU Commission expressed a willingness, under certain circumstances, to pursue a policy in the EU of relaxation of ownership and control rules. This willingness to do so is on the basis of reciprocity through bilateral air service agreements. There is a longer term objective to do so at a multilateral level. In line with its Better Regulation agenda, the Commission is currently evaluating Regulation 1008/2008, including the provisions on ownership and control of EU carriers. The purpose of this evaluation is to ensure that EU rules remain relevant and effective in a fast-changing aviation market. However, no decision has been made yet.

Regulation 1008/2008 in its current form raises concerns for airlines fully or partially owned by UK nationals because of the application of thresholds outlined above to a post-Brexit world. If an airline is no longer (more than 50%) owned or effectively controlled by EU Member State(s) and/or nationals of EU Member States, it is not entitled to hold an airline license and cannot operate or continue to operate within the EU air transport market.

To maintain EU market access, airlines may need to consider relocating their operations within the territory of an EU Member State

and/or restructuring their share ownership to reduce or negate the impact of Brexit. The impact of Regulation 1008/2008 on larger airlines may not be significant having regard to the Commissions expressions referred to above, but are more likely to impact on significant number of UK regional jet operators, charter airlines and cargo airlines currently operating in the EU. We will continue to monitor this area.

What remains to be seen is how the European aviation industry will emerge from the Brexit negotiations, as the UK is one of the largest contributors to air passenger traffic volumes in the EU and across the globe. The application of the EU's aviation framework to a post-Brexit UK remains uncertain.

The availability and access of EU airlines including those licenced in the UK, throughout the EU is good for competition at European and global level, and supports economic trade and development. Airlines currently licenced in the UK and operating throughout the EU and elsewhere are likely to want to maintain their existing operations. Some larger UK airlines may consider establishing an EU subsidiary to ensure access to all relevant European markets post-Brexit. It is possible that some airlines are looking to hold an air operators certificate (or equivalent) in more than one jurisdiction. Britain's biggest low-cost airline, easyJet announced it plans to locate its post-Brexit EU base in Vienna. EasyJet plc is confident that it will be able to satisfy Regulation 1008/2008 to allow easyJet to continue operating in both the UK and EU markets post-Brexit.

One of the core principles in the EU is equality and reciprocity. It is unlikely that the UK will take a more liberal or restrictive stance in relation to ownership and control of UK airlines, unless the EU does not agree to endorse reciprocal arrangements.

Conclusion

Until the terms of the UK's exit from the EU are negotiated with the remaining Member States, there can be no certainty for now on the issues that are likely to impact the aviation industry. The exit process is expected to take considerable time and effort on the part of all participants. It is in the interest of the EU and the UK to negotiate an agreement which will preserve a level of unity and reciprocity. The agreement will need to ensure continuity of air transport services, harmonise security and safety measures, boost competition and maintain best industry standards, consumer rights and security for all users and stakeholders.

History has shown that international trade deals can take many years to yield results. Given the complexity and scope of the negotiations, the need to avoid transport disruption, as well as concerns for reduced service levels and passenger rights, it is important that the parties recognise the importance of and prioritise air transport in the areas outlined above. There are a number of areas which are or will come under review and will be monitored by the industry and its participants as we proceed towards the exit date in March 2019.

For more information on the likely impact of Brexit on your business, please contact a member of our Aviation, Leasing & Asset Finance team.

Key Contact



Christine O'Donovan
Partner, Head of Aviation
+353 1 614 5082
codonovan@mhc.ie

Christine is a partner, head of our Financial Services team and a member of our Management Committee. Christine leads our Aviation, Leasing & Asset Finance team. She has recognised as an expert in aviation by Who's Who Legal: Aviation 2018.

Christine's award-winning practice focuses on international transactions in areas of corporate lending, project and acquisition finance, asset financing, particularly aircraft, and cross-border leasing. She advises domestic and international corporate clients, domestic and international credit institutions and aircraft manufacturers, lessors and airlines.

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Chambers & Partners, 2017

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