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EU MANDATES CARBON CREDITS FOR FLIGHTS TO EUROPE – INITIAL REGISTRATION DEADLINE 8/31

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Beginning in 2012, the Emissions Trading Scheme (ETS) will require operators of commercial and business aircraft flying to, from or within the European Union (EU)¹ to offset their carbon dioxide (CO₂) emissions by purchasing (or otherwise acquiring) an equivalent amount of carbon credits. Compliance is mandatory and will require registering with the appropriate regulatory authority, monitoring CO₂ emissions on a flight-by-flight basis, and offsetting those emissions with carbon credits. Operators are required to register by August 31, 2009,² and should contact their management companies to initiate the registration process.

GENERAL DESCRIPTION OF THE ETS AND THE INCLUSION OF THE AVIATION INDUSTRY

The ETS is the world's largest and most developed emissions trading scheme. Carbon credits, which act as a license granting the release of a limited amount of CO₂ emissions, are distributed among emitters in a given industry as a percentage of an established baseline. Emitters may buy and sell carbon credits based on their business requirements, and over time, the ETS will systematically reduce the carbon credits available to the industry.

While the ETS has been primarily focused on energy intensive industries with fixed installations, the EU approved the inclusion of the aviation industry into the ETS in October 2008.³ The baseline for the aviation industry was determined based on its average annual CO₂ emissions from 2004 to 2006. Beginning in 2012, the ETS will provide the aviation industry with carbon credits for 97% of the established baseline. Of that amount, 85% will be allocated to operators who begin reporting their emissions in 2010 and 2011 (as described in more detail below), and the remaining 15% will be auctioned. From 2013 to 2017, the amount of credits allocated for the aviation industry will be reduced to 95% of the baseline.

¹ The EU currently comprises 27 member states. The ETS includes the member states as well as the European Economic Area which includes Iceland, Liechtenstein and Norway. For simplicity we will refer to all of the states participating in the ETS as the EU.

² On July 7th, 2009, the UK regulatory authority announced a delay of approximately 3 months for operators required to register in the UK. At this point, no other state has pushed back the August 31 registration deadline; however, commentators have speculated that additional states will follow the UK's lead.

³ Note: with few exceptions, the EU does not draft legislation for each state to follow. Instead, the EU approves general directives and individual states draft legislation to implement those directives, potentially resulting in implementation variances between states.

ACTIONS REQUIRED TO COMPLY WITH THE ETS

• **REGISTERING:** Operators must first identify and register with the appropriate regulatory authority. Based on flight operations in the EU in 2006, an initial list was created by Eurocontrol assigning individual operators to their respective states.⁴ Operators already assigned to a state should receive a letter from that state's regulatory authority providing the registration details. Operators who are not on the initial list have not yet been assigned a state; *however*, those operators are still required to comply with the ETS and must contact the regulatory authority of the state they operate in most frequently to register no later than August 31, 2009.⁵

• **MONITORING:** Once registered, the regulatory authority will provide the operator with additional information on the monitoring plan. The monitoring plan is mandatory and must follow a set template and guidelines. The operator is then required to complete and submit the monitoring plan to the regulatory authority. Upon approval, the monitoring plan serves as the emissions permit allowing the operator to operate in the EU.

• **REPORTING AND VERIFYING:** Beginning January 1, 2012, operators will be required to comply with the ETS on a flight-by-flight basis for all flights to, from or within the EU. For example, an operator conducting a business aviation flight from Los Angeles to London must offset CO₂ emissions for the entire flight, not just the portion of the flight within the EU. Each operator will need to first have the data verified by an independent auditor to confirm its reliability and accuracy before its annual report can be submitted to the regulatory authority.

• **ACQUIRING CREDITS:** Operators have several ways to acquire carbon credits. Free allowances will be available through the ETS for operators who (a) promptly register, (b) receive approval for their monitoring plan by December 31, 2009, and (c) submit annual reports in 2010 and 2011. While this may be a viable alternative for commercial operators, it is not yet clear if this is a practical alternative for business aviation operators. Credits will be made available for purchase through an auction process managed by the ETS. Credits may also be purchased from operators within the aviation industry or other participants of the ETS who have excess credits.

Commercial operators emitting less than 10,000 metric tons of CO₂ each year will be exempt from purchasing carbon credits, but are still required to comply with the ETS. While there is no equivalent exemption for business aviation, the EU is currently studying a plan to allow operators who emit less than 10,000 metric tons of CO₂ per year to estimate their fuel consumption with tools provided by Eurocontrol. However, until that plan is approved, all business aviation operators should be prepared to comply with the ETS as currently proposed.

Compliance is mandatory. For operators who fail to comply, regulatory authorities have the ability to assert liens on the aircraft and the worst offenders may have their aircraft impounded.

⁴ See http://ec.europa.eu/environment/climat/pdf/aviation/alloc_operators_110209.pdf

⁵ See <http://ec.europa.eu/environment/climat/pdf/aviation/contacts.pdf>

CONTROVERSY AND LEGAL CHALLENGES

Application of the ETS to the aviation industry has been controversial and may face significant legal challenges. The EU evaluated various international aviation laws and concluded the ETS does not violate those laws. However, the EU has received letters from the governments of the United States, Australia, China, Canada and others challenging the legal authority of the EU to apply the ETS to non-EU operators. Nations may yet appeal to the World Trade Organization. Aviation-oriented organizations including the NBAA and the EBAA are working with the EU to minimize the administrative burden of the ETS on business aviation, and ICAO has proposed that any type of emission reduction scheme should be global in nature.

The ETS does consider granting reciprocal credits for operators flying from a region with a comparable scheme. For example, if the United States were to implement a similar scheme, operators flying between the EU and the United States would not have each flight count against them twice. On the other hand, if the United States were to implement an additional carbon tax on jet fuel in lieu of a carbon trading system like the ETS, it is not clear whether the ETS would credit the carbon tax towards an operator's obligations under the ETS.

CONCLUSION

Although the aviation industry accounts for a small percentage of the total man-made global CO₂ emissions, EU policy makers have included business and commercial aviation into the ETS. While the cost of purchasing carbon credits is not forecasted to be excessive at this time, most business aviation operators will be affected by the administrative costs and burdens of compliance. The first step is identify and registering with the appropriate regulatory authority. Operators must start planning now.

Please contact us if you have any questions.

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