



COMMISSION OF THE EUROPEAN COMMUNITIES

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**REPORT FROM THE COMMISSION TO THE COUNCIL
AND THE EUROPEAN PARLIAMENT**

on transport security and its financing

1. INTRODUCTION AND AIM

Enhancing security has been a priority of the Commission directly in the aftermath of the attacks of 11 September 2001. The Commission's general views were set out in its Communication to the European Parliament and to the Council on "The repercussions of the terrorist attacks in the United States on the air transport industry"¹. The Commission followed this up with Regulations establishing common rules on aviation and maritime security. In addition, the Commission launched a European programme for the protection of critical infrastructure².

In view of the importance of financing security measures and the necessity to avoid internal and external distortions of competition, both Regulations were accompanied by requests from the European Parliament and the Council to undertake studies³. Those studies should in particular address the way the financing of security measures is shared between the public authorities in the Member States and the operators, without prejudice to the distribution of competencies between the Member States and the European Community. The Commission was requested to submit to the European Parliament and to the Council the results of its studies and make proposals if appropriate.

When preparing this report, the Commission asked the European Economic and Social Committee and the Committee of the Regions for an opinion on the question of transport security and financing⁴.

2. RESULTS OF STUDIES

2.1. Aviation Security

Following the Interinstitutional Declaration attached to Regulation (EC) N° 2320/2002, the Commission launched a study on European Civil Aviation Security Financing⁵.

The study, which covered 15 Member States plus Norway, Iceland and Switzerland, analysed aviation security expenditure, funding mechanisms and associated competition issues. As regards security expenditure the study revealed that in 2002, prior to the entry into force of the European regulations, total security related expenditure for the 18 states was between 2.5 and 3.6 billion euros. This is made up of 0,65 billion euros by the states, 1,32 billion euros by airports and between 0,52 and 1,66 billion euros by air carriers. Although one may argue that these costs are significant, the study showed that for example for intra-European travel, the combination of security taxes and airport charges represents between 1% and 2% of the average fare.

¹ COM(2001)574 final of 10.10.2001

² Programme "Prevention, Preparedness and Consequence Management of Terrorism and other Security and Safety Related Risks" for the period 2007-2013, adopted by Council on 2.6.2006

³ Interinstitutional Declaration accompanying Regulation (EC) N° 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. 12) and Recital 15 of Regulation (EC) N° 725/2004 of the European Parliament and of the Council of 31 March 2004 on enhancing ship and port facility security (OJ L 129 of 29.04.2004, p. 6)

⁴ TEN/217 - CESE 1488/2005 of 14.12.2005 and COTER-040 - CdR 209/2005 fin of 17.11.2005

⁵ http://europa.eu.int/comm/transport/air/safety/studies_fr.htm

As regards funding mechanisms, the study came to the conclusion that two basic models of financing exist within Europe:

- a centralised model, where the provision of the main security activities are primarily the responsibility of the State via a government body (Civil Aviation Authority, Ministry of Transport, police force, etc.)⁶
- a decentralised model, where the provision of the main security activities are provided by the airport authorities under the supervision of the relevant authority (Civil Aviation Authority, relevant Ministry, etc.). These activities could either be provided by the airport directly or outsourced to a third party⁷.

The study concluded that in both models the passenger was, ultimately, the main funder of security through State security taxes, airline security charges on tickets and/or airport charges. However, it also concluded that in the majority of countries and, irrespective of the model applied, funding from passengers during the year 2002 was insufficient to cover all security costs. This has to be seen in perspective, as actual passenger charges related to security may also be contained in general aeronautical charges at a number of airports and this lack of transparency distorts the overall understanding of revenue actually generated to fund security at airports across Europe. Differences appeared in relation to the funding of existing operating deficits, with 6 of the 18 States covering such deficits partly from general taxes and the remaining States leaving the burden of financing such deficits on the airports.

As regards the risk of external distortion of competition, the study showed significant differences in the approach to financing security measures between the EU and the US. In the aftermath of 11 September 2001, the US authorities granted significant financial assistance to its hard-hit aviation industry and ensured nationwide application of several major security measures. As an example, the US aviation industry from 2002 to 2004 benefited from public assistance amounting to almost 32000 million euro under the header of transport security. It is clear that such heavy public funding can create distortions of competition between European and American carriers.

2.2. Maritime Security

Recital 15 of Regulation (EC) 725/2004 stipulates that the Commission should undertake a study to address in particular the way financing is shared between public authorities and operators. Under recital 13 of Directive 2005/65/EC this study should also consider the funding of extra security measures for port security.

This study is currently being finalised. Preliminary results indicate that, similar to the case of aviation, security costs in maritime transport constitute a relatively low proportion of the overall investment and operating costs.

The European Union has more than 1200 seaports and about 4000 port facilities. The average cost of security is 464.000 Euro for investment costs and 234.000 Euros for yearly running costs. The fleet under flags of the EU Member States account for about 9000 vessels, and

⁶ The approach in Austria, Finland, Germany, Iceland, Italy, Luxembourg, Norway, Portugal, Spain, Sweden, Switzerland is closest to this model.

⁷ The approach in Belgium, Denmark, France, Greece, Ireland, The Netherlands, United Kingdom is closest to this model.

operators have to bear an average investment cost of around 100.000 Euro per vessel and 25.000 Euros running costs per year. Investments are mainly in equipment and compliance certification, whereas more than 50% of the running costs represent the cost of specialised personnel.

Those average figures have to be seen in comparison to the global costs that shipping activities have to face. Whilst an investment of an average of 100.000 Euro is necessary per vessel in terms of security, this represents only 0.0015% of the total price of a new-build 8000 TEU Container ship and 0.0006% for a 110,000 GT LNG tanker. Although the study was unable to determine equivalent percentages in respect of port facilities, it shows huge differences between types of port facilities ranging from 798.000 Euro for Multi-Purpose facilities to 79.000 Euro for container facilities. This can primarily be explained by the fact that depending on their specific activities, some types of facilities already had equipment and measures in place because of safety requirements or to counter theft, which can be used for security purposes as well.

According to the study the costs are essentially financed directly or indirectly by the port authorities and the operators themselves. As far as port facilities are concerned, the sources for cost recovery of the security measures appear on average as follows: increase of tariffs 19%, separate security charge 55% and subsidies 23%. Competent authorities in Member States were rather discreet on the resources they devote to maritime security.

However, the EU maritime security regime has not yet come wholly into effect - full implementation in accordance with the relevant provisions of both Regulation 725/2004 and Directive 2005/65 is required by 1st July 2007. This may mean that in order to achieve a high level of compliance, additional resources could be needed. Distortion of competition may exist as long as a uniformly high level of compliance is not reached.

As in the case of aviation security, there is also the question of external distortion by competitors from third countries which may benefit from subsidies by their governments for covering maritime security costs. This could be valid for port facilities in competition with neighbouring non-EU ports, and to a lesser extent for ships.

3. ISSUES TO BE CONSIDERED

3.1. Structure of costs

Several types of costs relating to transport security can be identified:

- Costs of administrating security rules, including compliance monitoring
- Costs resulting from applying legislation
 - Fixed costs, such as capital investment in security equipment, and selection and initial training of security staff;
 - Operating costs, such as maintenance of security equipment (including technology upgrades), the wages of security staff, recurrent training costs;
 - Exceptional costs, such as those of additional temporary measures to raise security levels during periods of higher risk.

– Costs resulting from terrorist attacks

These costs are only partially related to transport and can include the cost of repairing damage to the target itself, ancillary costs resulting from the disruption caused by the attack and damage claims of victims, both direct and indirect. Indeed, even in the case that the transport medium (e.g. aircraft, ship, train) is the object of a terrorist attacks and is not used as a weapon, the damage may go by far beyond the transport sector. It is difficult to estimate the scale of such costs, but it is quite possible that they may be of such an extent that no single transport operator could be in a position to finance them. Also, the cost of damage may go significantly beyond what insurance may be able to cover at a reasonable price. In addition, depending on its nature, the consequences of a terrorist attack may extend beyond the territory of a single Member State and may be of such a scale that even the Member State where the terrorist attack has taken place cannot bear the costs.

3.2. Financing

3.2.1. Financing of administering security rules, including compliance monitoring

The transposition of Community legislation into national law and its application to national monitoring activities are tasks that are typically those of a public authority.

This holds also true for inspections to verify the correct application of security measures in the aviation, maritime and land transport sector. Although the Commission may also carry out such inspections, this in no way replaces the Member States' obligations to implement efficient quality control programmes on the national level.

Such activities fall within the public policy remit and as such are in principle financed in full by the Member States. They do not give rise to State aid, even if the Member States rely upon private undertakings for assisting them, provided (in the latter case) that the financing is limited to a compensation of the costs incurred and a reasonable profit, and does not give rise to any overcompensation. .

On the basis of its inspection results, the Commission calls upon the Member States to make available sufficient resources to ensure the full application of security rules and control of implementation of security legislation.

3.2.2. Financing of the implementation of security measures

The financing by Member States of the implementation of transport security measures by Member States raises the question whether it constitutes State aid in the sense of Art. 87 (1) EC Treaty and if so, under which conditions it can be declared compatible with the common market.

The European Court of Justice and the Court of First Instance have at several occasions held that there are three distinct categories of activities which are financed by the State: activities of public authority, economic activities, and non-economic activities. Only economic activities are subject to European competition law, whereas activities of public authority and non-economic activities are excluded from its scope.

In the *Eurocontrol*⁸ case, the Court found that *Eurocontrol's activities, by their nature, their aim and the rules to which they are subject, are connected with the exercise of powers relating to the control and supervision of air space which are typically those of a public authority.*⁹ Accordingly, they are not of an economic nature justifying the application of the Treaty rules of competition.

In the *Porto di Genova* case, the Court found that *“the anti-pollution surveillance for which SEPG was responsible in the oil port of Genoa is a task in the public interest which forms part of the essential functions of the State as regards protection of the environment in maritime areas. Such surveillance is connected by its nature, its aim and the rules to which it is subject with the exercise of powers relating to the protection of the environment which are typically those of a public authority. It is not of an economic nature justifying the application of the Treaty rules on competition”*¹⁰.

In the *Aéroport de Paris* case, the Court of First Instance found that *“a distinction must be drawn between, on the one hand, ADP's purely administrative activities, in particular supervisory activities, and, on the other hand, the management and operation of the Paris airports, which are remunerated by commercial fees which vary according to turnover.”*¹¹

It can be seen from this jurisprudence that the financing of transport security measures which form part of essential functions of the State and which are connected with the exercise of powers which are typically those of a public authority does not constitute State aid in the sense of Art. 87 (1) EC Treaty.

The Commission has confirmed this in its decision “N 309/2002 France, Sûreté aérienne – compensation des coûts à la suite des attentats du 11 septembre 2001”. In this decision, the Commission analyses the security measures which the French government had put in place after the attacks of September 11. In point 22 and 23 of the decision, the Commission comes to the following conclusions:

The abovementioned security tasks are functions traditionally performed by the police or the airport manager in accordance with instructions from the public authorities. They are provided for in laws or regulations. The bodies performing them do not have any discretionary margin.

The bodies responsible for these security tasks receive no revenue of any kind from passengers. Indeed, the French authorities have indicated that the airport taxes paid by passengers remain at the disposal of the airports and are used, in part, to cover the security costs of these airports alone. These functions can therefore in principle be considered to be the responsibility of the public authorities.

As a general rule, it can be concluded that the financing of transport security measures which are imposed by law and which are connected with the exercise of powers which are typically those of a public authority do not constitute economic activities. This position has recently

⁸ Eurocontrol is an international organisation in charge of establishing and collecting the charges levied on users of air navigation services.

⁹ Arrêt du 19/01/1994, SAT Fluggesellschaft / Eurocontrol (Rec.1994,p.I-43), point 30.

¹⁰ Arrêt du 18/03/1997, Cali & Figli / Servizi Ecologici Porto di Genova (Rec.1997,p.I-1547), point 22

¹¹ Arrêt du 12/12/2000, Aéroports de Paris / Commission (Rec.2000,p.II-3929), point 112.

been re-affirmed in the Community guidelines for State aid to regional airports.¹² The financing of these measures must, however, be strictly limited to compensation of the costs to which they give rise and may not be used to fund other economic activities.¹³

The State can delegate the exercise of these powers to private undertakings; this was for example the case in *Porto di Genova*. The State may also decide that the users of a certain facility have to bear, at least partially, the costs of these security measures, as it was the case in *Porto di Genova*, *Eurocontrol* and the aforementioned security measures in the French airports. In these situations, the Commission will however scrutinize very closely whether the private undertakings do not receive overcompensation for their help to the State, and whether the charges levied are strictly confined to what is necessary for financing the security measure. If the State delegates the exercise of its powers to private undertakings, it must also ensure that EC public procurement and non discrimination rules are fully respected, as far as they are applicable, and ensure that there is no discrimination.

3.3. Transparency in levying security taxes and charges

The studies on the financing of transport security have found that there is little transparency as regards what money was raised for security, the levels of charges or taxes levied, and how the money was actually spent.

It is desirable to achieve greater transparency as regards security taxes and charges. This could take the form of rules on the hypothecation or ring-fencing of money collected for transport security so as to ensure that it is spent solely and wholly on security. A second option would be that security taxes and charges are explicitly explained to passengers where fares are broken down in order to show users what they are charged for. This would be particularly relevant for airline passengers where security costs are bundled into a much higher figure covering overall taxes and charges.

3.4. Potential distortions of competition

The Commission is of the opinion that the pursuit of a sufficiently level playing field in terms of access to public financing is a valid concern raised by stakeholders, both within the internal market and in relation to major external markets.

As the different studies have borne out, different approaches exist within the EU to the involvement of Member States in the funding of the implementation of security measures, reflecting the different philosophies Member States may have on the role of the State in this matter. The heterogeneity of approach and the lack of transparency in generating revenue that is wholly for the implementation of security measures means that there is a possibility of some distortion of competition. This is particularly relevant in cases where Member States require additional, more stringent measures than those imposed by Community legislation.

However, distortions may also arise on a global level due to different approaches towards the funding of security measures around the world. This issue needs to be addressed, so as not to disadvantage the Community's transport industry in comparison with its competitors from outside the European Union, with its consequential negative effect on EU economic growth.

¹² Official Journal C 312 of 9.12.2005, p.1.

¹³ Case C-343/95, *Cali* [1997] ECR I-1547 (“*Porto di Genova*”)

It should therefore be ensured that similar principles are being applied to the European transport industry's competitors in third countries by the Governments responsible for them, preferably in the form of agreements in international fora such as ICAO or IMO or, failing that, bilateral agreements between the European Union and the Governments of the States where the main competitors are based.

4. CONCLUSIONS

- According to studies on aviation and maritime security, security costs can be significant and are currently largely borne by the users.
- Increased transparency relating to security taxes and charges would give users of transport services better information and provide a clearer insight into possible effects on competition. The current lack of transparency increases the difficulty to identify potential distortions.
- The heterogeneity of approach to the funding of the implementation of security measures means that there is a possibility of some distortion of competition. This is particularly relevant in cases where Member States require additional, more stringent measures than those imposed by Community legislation.
- The Commission's general views set out in its Communication to the European Parliament and to the Council on "The repercussions of the terrorist attacks in the United States on the air transport industry" remain valid. In particular, the Commission considers that, in view of the fact that the protection of European citizens against terrorist attacks is essentially a State responsibility, public funding of the actions to prevent such acts which are connected with the exercise of powers that are typically those of a public authority does not constitute State aid.