International Air Passenger Adaptation Levy

A proposal by the MALDIVES on behalf of the
GROUP OF LEAST DEVELOPED COUNTRIES (LDCs)
within the framework of the Bali Action Plan

12 December 2008

Executive Summary

Following the very successful example of the French 'Leading Group' solidarity levy to combat HIV/AIDS, the LDCs Group proposes an *adaptation solidarity levy on international air passengers* to provide more adequate funding for adaptation activities in the poorest and most vulnerable countries and communities.

In line with the French levy, the LDC Group proposal is to establish a small passenger charge for international flights − differentiated with respect to the class of travel − *to raise between $8bn and $10bn annually* for adaptation in the first five years of operation, and considerably more in the longer-term. This will constitute a significant step *towards ensuring adequate financing for developing country adaptation* costs.

The levy is to benefit the Kyoto Protocol *Adaptation Fund*, which currently is replenished by a two percent solidarity levy on the share of proceeds from the Clean Development Mechanism. It is to be universal in the sense of covering all international air travel and collected by airlines at the point of ticket sale. Being international and dependent only on the evolution of the air travel demand − and not on bilateral replenishment – the funds raised will truly be *new and additional*, as well as *significantly more predictable* than traditional funding mechanisms.

The levy will also be able to provide individual people and businesses who have the means to fly internationally with the opportunity to take on their responsibilities and express their solidarity with those fellow human beings who are much less capable to deal with, the impacts of the international passenger flight emissions. The levy provides for an *equitable mechanism for victim compensation* in a sector which – due to the non-national character of the emissions – eludes the traditional interpretation of common but differentiated responsibilities in terms of national (historic) emissions.

The proposed levy will have no significant effect on passenger numbers – less a tenth of the expected annual growth rate – and hence *minimal to no negative impact on tourism dependent economies*. By contrast, it will have *significant positive impacts on the development of the poorest and most vulnerable countries and communities*, by avoiding climate change impacts through timely and adequate adaptation measures funded by the revenue raised through the levy.

The LDC Proposal

Background. In light of the fact that adaptation to climate change impacts is crucial to development, especially for the poorest and particularly vulnerable countries and communities, and given the inadequacy of existing adaptation funding, the proposed solidarity adaptation levy on international air passengers will provide a *development life-line* for these countries. The proposed levy is therefore not only in line with the idea underlying the French Leading Group on Solidarity Levies to Fund Development, but it has the added advantage that the purpose of the levy – to fund adaptation in particularly vulnerable countries – is directly linked to the activities being levied in accordance with the *polluter pays principle*, a feature which will be *key to the public acceptability* of the proposed levy.

The proposed levy also conforms to the idea of *common but differentiated responsibilities and respective capabilities*, but because of the non-national nature of the activities this conformity is not with respect to the responsibilities and capabilities of countries, but with respect to (i) the personal responsibilities of passengers due to the international emissions produced and (ii) their capability revealed by the ability of flying internationally. Indeed, given the international character of the activities in question and of the resulting emissions, *the only equitable way* deal with these non-national responsibilities for these activities is at the personal level, which – given the price levels of international flights – also respects the idea of respective personal capabilities.

Operational Details

- The revenue of the levy will go to the Kyoto Protocol Adaptation Fund to fund its activities.
- The level and travel class differentiation of the levy is to be according to the *tried and tested formula* of the French levy, at present \$6 (€4) per economy trip, and \$62 (€40) per business/first class trip.
- The levy is to be collected by airlines from their passengers at the point of sale and transferred by the airline to a dedicated account of the Adaptation Fund.
- The airlines will be compensated by the Adaptation Fund for reasonable administrative costs incurred in the course of collection.
- The Board of the Adaptation Fund will be requested to operationalise the collection mechanism for the levy, if necessary in consultation with the relevant international bodies concerned with the aviation sector.

Revenue. The calculations of the near-term revenue estimates of \$8bn to \$10bn are based on a travel class differentiation in line with the French solidarity levy, as well as IATA figures and estimates for current international passenger numbers (760m) and annual demand forecasts (5.1% p.a.). The calculations also assume 93% coverage of all international scheduled air traffic – i.e. reflecting International Air Transport Association (IATA) membership − and 99% collection efficiency.

This revenue, by its very nature, will be *new and additional* to the traditional flows of bilateral funding for adaptation. Given its nature, the revenue will also not be subject to the problems of bilateral replenishment, and it will be *predictable* due the stability of the airline sector.

Potential Impact on Development. Understandably, many poor and vulnerable countries which rely heavily on air passengers in their development aspirations might be worried about the impact on their economic development of the proposed solidarity levy. As it happens, the sensitivity of international air travel demand, particularly long haul, to price increases is very low. Given average price elasticities of passenger demand of -0.66 and -0.60 for short and long-haul travel demand,[1] respectively, an average price increase of 0.8% – equivalent to the levy of \$6 to a \$750 economy class ticket – would result in a drop in demand of 0.52% and 0.47% for short and long-haul flights, respectively: an order of magnitude less than the expected growth of air travel of 5.1% per annum. Given this, and the considerable benefits in terms of avoided impacts that will accrue to the recipients of the funds raised, the proposed solidarity levy will have substantial positive effects on the development of the poorest and most vulnerabile countries and communities.

Potential Impact on Airline Business and Competition. As a passenger levy is borne by passengers directly and as the cost of collection is reimbursed to the airlines, the only impact of the proposed levy will be through its demand implications, which as noted earlier, will be minimal with respect to the expected demand growth. With respect to potential competitiveness implications, the universality of the levy will insure that unfair distortions are avoided.

[1] InterVISTAS Consulting Inc (2007) **Estimating air travel demand elasticities**, Report prepared for IATA.