Europe Economics

Bonding of the Irish travel trade industry

Interim Report

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1 Introduction

The core objectives of this study are to answer the following three questions:

1. Does the current travel trade scheme (i.e. bonding plus the Travellers' Protection Fund (TPF)) continue to meet the objective of ensuring consumers are fully protected in the event of future collapses?
2. If yes to Q1, does the current scheme represent the most efficient way of achieving this objective?
3. If no to either Q1 or Q2, what feasible options for a reformed scheme can be considered?

1.1 Consumer protection under the travel trade scheme

The current travel trade licensing and bonding scheme seeks to provide financial protection to consumers should their travel agent or tour operator be unable to fulfil its obligations under contract. In such circumstances, consumers can make claims for a refund for the costs of trips not yet taken, and for repatriation costs in the event that the collapse occurs while they are abroad.

Currently, if a licensed travel agent or tour operator collapses, the costs of claims and associated administrative costs of processing those claims are paid from the bond that the travel trade firm will have posted when getting a licence. Since the scheme was introduced in 1982, the size of companies' bonds has been set at 4 and 10 per cent of projected licensable turnover for travel agents and tour operators respectively. Should the bond be insufficient to fund all claims, the TPF is used to fund the remainder. The TPF was originally funded by a levy on tour operators, but this levy was stopped in 1987 on the basis that the TPF had sufficient funds to provide financial protection to customers. To date, it has not been deemed necessary to reintroduce the levy with the Fund always being deemed sufficient.

1.2 Purpose of the study

A review of the current scheme is appropriate. The original legislation dates back to 1982, and it is almost a decade since the last consultation with stakeholders on possible changes to the travel-trade legislation. Moreover, the collapse of Lowcostholidays.ie in summer 2016 has depleted most of the remaining money in the TPF.

This report focusses on whether the current scheme actually provides the consumers covered with the financial protection that is intended. In particular, whether the current bonding arrangements and TPF are adequate to meet likely claims should travel agents or tour operators be unable to fulfil their obligations. It does not look at whether the scope of the current regime is appropriate, or whether it should be extended to cover customers of airlines or relaxed so fewer packages are covered. The many seeming anomalies with the coverage provided by the existing scheme identified in the Commission's 2008 review remain, many attributable to the major developments in the market since the legislation was introduced, namely:

- The share of trips purchased via a travel trade firm had declined, as consumers increasingly purchase flights direct from airlines, a development aided by new technology (most notably the Internet).
- The growth of low-cost airlines, preferring to sell direct to customers rather than through travel agents. For many popular destinations in Europe, the costs of a flight from Ireland represent a considerably

smaller share of income than in the early 1980s, arguably lessening the value of having a financial protection scheme in place for all trips outside Ireland.

- The evolution of payment systems, with greater use of cards and a trend towards real-time payments. Travel-trade firms are no longer holding customers' money for as long as had been the case in the past.

These developments have not been reversed and, other than new European directives, we are not aware of any other significant market developments that might be relevant. We understand that the Commission is separately reviewing how best to implement the new package travel directive.

1.3 Methodological approach

With our focus on the adequacy of current arrangements to protect those customers that the scheme intends to be covered, we adopted the following methodology:

- Analysis of industry data, including data on industry trends and past collapses. Data on past collapses has been used to evaluate the effectiveness and efficiency of the current scheme, as well as that of potential options for reform. This is a backward-looking approach insofar as it uses data on past collapses to make inferences about the suitability of the scheme moving forwards in providing consumer protection against unknown future collapses. Where relevant we have also drawn on the data to look at relevant industry trends and understand their implications for the effectiveness of the current scheme and potential reforms moving forward.
- Interviews with various members of the industry. Interviews were held with a number of key stakeholders including travel agents, tour operators, airlines, trade bodies, merchant acquirers and government. Discussions were structured around three areas: key industry trends since scheme inception and looking ahead; the effectiveness and efficiency of the current scheme (and how the key industry trends may have affected this); and potential options for reform.
- An analysis of other national schemes in place in Europe. Five national case studies were conducted to understand the corresponding consumer travel trade protection schemes in place in these economies. The focus was on understanding the aspects of these schemes that were perceived to have worked well and not so well so as to inform the discussion of potential reforms to the Irish scheme.

The rest of this report presents our findings, and assesses possible options for reform.

2 Analysis of other national schemes

As part of this study, we have investigated the types of insolvency protection schemes in place elsewhere in Europe. Does the experience in other countries have lessons for the design of the Irish scheme for protection of consumers buying package holidays?

For five national schemes – Denmark, France, Netherlands, Norway and the UK – we summarise:

- the history of the scheme(s);
- recent and proposed changes (and any associated impact assessments);
- the structure of the travel trade industry; and
- the structure and performance of the consumer protection scheme.

All five countries will need to comply with the new EU directive on package travel 2015/2302/EU (EU PTD2). This directive provides more details on the obligation for Member States to organise insolvency protection and a security fund in case a tour operator working in their territory goes bankrupt. While Ireland will have to comply with EU PTD2, we have not focused our review on how the other countries intend to ensure compliance.

2.1 Denmark: Rejsegarantifonden

Historic overview

Denmark created its Rejsegarantifonden (RGF, Travel Guarantee Fund) in 1979 as a private, independent, non-profit organisation. The RGF was established in response to a major bankruptcy in the organised travel industry. The regulatory scope of RGF changed over time to reflect regulatory challenges and EU PTD1. The current status of the RGF is defined by the 1997 Travel Guarantee Fund Act and the subsequent amendments, with the most recent one in 2015.[1] Table 2.1 summarises the RGF history.

[1] The English version of the consolidated Travel Guarantee Fund Act in is available here [accessed on June 26, 2017]: https://www.rejsegarantifonden.dk/fileadmin/user_upload/Om_os/Lov_1101_03092015_ENG.pdf

Table 2.1: Summary of the Danish RGF development

Date	Event
1979	The RGF created in response to a large company failure in the organised travel industry
1993	Implementation of EU PTD1. The RGF scheme is expanded because of new definition of package holiday.
1997	Following several major failures, the new Travel Guarantee Fund Act is adopted. The RGF get more power to ensure better financial oversight of travel providers, in particular, the RGF could ask for company's financial documents and, if necessary, ask to increase the amount of guarantee
2000	The RGF can remove a company from the register if the guarantee is deemed to be insufficient. Since the tour operator licence is conditional on the RGF registration, the removal from the RGF register means revocation of the licence.
2004	The RGF get the rights to conduct an inspection if the company is suspected of irresponsible economic behaviour that increases the risk of failure
2008	The RGF appeal board receives the same status as other approved private appeals
2009	The travel guarantee scheme is extended to airline companies that operate between Danish airports and other countries.
2012	After the legal dispute between the RGF and Norwegian Air, the air flight guarantee is required only for airline companies that have a physical presence in Denmark (branch, sales office or representative office)
2015	The RGF separates the fund equity into the package travel fund and the air transport fund.

Source: Based on the Consultation on the air transport fund (2014). [2]

Recent and proposed changes and impact assessments

The most recent change of the RGF regulation in 2015 resulted in the separation of the air transport guarantee scheme as a sub-fund. In the accompanying consultation, the Danish Ministry of Industry, Business, and Financial Affairs established that the air transport fund should be equal to DKK 100 million (approximately €13.4 million at current exchange rates) based on the estimated cost of repatriation of stranded travellers.[3] This target was at the lower end of estimated potential costs and losses. The cost estimates were taken from the confidential submissions to the consultation by the Danish Transport Agency, the Danish Air Transport Association and the RGF. The consultation also referred to the failure of a mid-size regional Danish airline company called Cimber which had total prepayments of DKK 250 million, and some of the published consultation submissions stated that an airline company failure could result in even higher losses, between DKK 450 million and 1.1 billion.

The air transport guarantee introduced in 2010 applied initially to all airlines that operated between Danish airports and other countries. However, after multiple disputes between the airline companies and the RGF, the most notable one being the legal battle between Norwegian Air and the RGF in 2012, the air transport protection is now compulsory only for companies that have a physical presence in Denmark, i.e. a branch, a sales office or a representative office.[4] This excludes companies that offer online sales of flights to/from Denmark only. A desk counter at the airport that deals with passengers and cargo en route is not considered a physical presence.

[2] Udvalgsrapport om lov om en rejsegarantifond (September 2014). Available online at [accessed on June 26, 2017]: http://em.dk/publikationer/2014/02-09-14-udvalgsrapport-om-lov-om-en-rejsegarantifond

[3] Annex 9 of Udvalgsrapport om lov om en rejsegarantifond (September 2014).

[4] For more details, see pp. 72-74 in Udvalgsrapport om lov om en rejsegarantifond (September 2014).

The structure of the travel trade industry

In 2015, the Danish households spent approximately DKK 14.3 billion on package holidays, of which the bulk (over 97 per cent) was spent on international packages.[5] The expenditures on air transport amounted to DKK 4.5 billion, of which 85 per cent was spent on international flights. The spending on package holidays more than doubled between 2003 and 2008 increasing up to DKK 17 billion but then fell amidst the overall economic recession. Since 2012, the trend has reversed upward.

According to the Association of Travel Agencies in Denmark (Rejsearrangører i Danmark, RID), the largest tour operators in the country are Spies (part of Thomas Cook Group), TUI, Bravo Tours and Apollo. Jointly, they supply around 80 per cent of the package travel market.[6]

The structure and performance of the consumer protection scheme

The RGF publishes annual reports that provide details of bankruptcies, net losses, the fund equity and the overall financial situation.

As of 2016, the RGF had 549 travel providers in its register. This number includes tour operators, travel agents and airline companies.

The licence for organised travel business is conditional on providing a guarantee to the RGF. The amount of guarantee depends on the turnover (see Table 2.2). The same guarantee threshold applies to tour operators and airline companies. As the guarantee amount is based on turnover forecast, the RGF monitors the companies' sales on a quarterly basis and, if necessary, might ask the company to increase the guarantee amount or remove the company from the register. The demand for an increased guarantee is especially common for newly established travel providers.

Table 2.2: Turnover and corresponding guarantee, DKK million

Turnover	Guarantee amount
Below 0.25	0
From 0.250 up to 5	0.3
From 5 up to 10	0.5
From 10 up to 15	0.75
From 15 up to 50	1
From 50 up to 100	1.5
From 100 up to 250	2
At 250	2.5
Above 250	The guarantee amount increases by 1 million for each 100 million of revenue

Source: The Travel Guarantee Fund Act 2015, Section 8.

To cover management expenses of the RGF, travel companies have to pay an annual fee. This fee has a fixed part and a variable part that depends on the company's turnover. The fee structure is defined such that 30 per cent of the management expenses is covered by the fixed part and 70 per cent is covered by the variable part.[7]

Both sub-funds, for package holidays and for air transport, have target levels of equity. When the equity falls below a certain amount, the RGF introduces a temporary levy per package or passenger, respectively, to replenish the corresponding sub-fund up to the target amount.[8]

The target level for the package holiday sub-fund is DKK 50 million, based on the two largest failures since 1997. The levy is re-introduced if the RGF deems the fund equity to be low after a given failure i.e. there is

[5] Source: Statistics Denmark and own calculations.
[6] Source: RID and own calculations.
[7] RGF Annual Report 2008.
[8] The information in this and the two following paragraphs is based on RGF annual reports 2008-16.

no fixed threshold value below which the levy is automatically reinstated. For the package holiday sub-fund, the most recent case of a temporary levy of DKK 20 per package was in 2009. This followed several major company failures in 2007-8 with a total net loss of nearly DKK 27 million. The target level was reached within a year so the levy was removed in 2010. By contrast, in 2013 net losses of approximately DKK 20 million, did not trigger the levy as the fund management considered that the remaining equity of DKK 63 million (not yet separated into the two sub-funds) reflected properly the risk faced by the travel companies.[9] For reference, the annual net losses in other years between 2009 and 2016 varied between DKK 0.17 and 3.15 million.

The target level for the air transport fund is set at DKK 100 million. As the air transport fund has been recently established, the temporary levy of DKK 20 per passenger was in place between 2010 and 2014 to build the fund equity. The levy was reduced to DKK 2 in 2015, with the separation of the air transport sub-fund. The levy currently remains in place as the equity is still below the target, with 44 million at the end of 2016 financial year. In the future (after the target equity is built), if the air transport fund equity falls below DKK 75 million because of a failure, the DKK 2 levy would be re-introduced until the equity reaches the initial target of DKK100 million. Should there be a large company failure and the fund equity fall below DKK 25 million, the levy would be DKK 4 per passenger.

2.2 France: Atout register

Historic overview

Since 2010 travel agents and tour operators have to obtain their licence from Atout France (not local administrations as before), the national agency for promoting France as a tourist destination. The change in licence rules was part of larger legislative changes in the tourism industry.[10]

As part of the licence application, the travel operators should provide a financial guarantee obtained from an industry trade association, a bank, or other approved organisation. The largest industry association that provides guarantees is l'Association Professionnelle de Solidarité du Tourisme (APST, Professional Association of Solidarity in Tourism). Initially, the guarantee had to be at least €100,000 for new companies and was calculated as a percentage of turnover for existing industry participants, but no more than 10 per cent.[11]

The values were increased subsequently to €200,000 and 20 per cent, as the French financial guarantee rules were heavily modified by the 2015 Décret.[12] The changes were to ensure better protection of customers and responded to a ruling by the European Court of Justice (ECJ). In 2013-14, a Hungarian case was referred to the ECJ concerning the amount of travel cost covered by the financial guarantee.[13] The ECJ order accompanying the final decision stipulated that Article 7 of the EU PTD1 on the financial guarantee should be interpreted such that the guarantee must cover the full cost of advance payments made and repatriation costs and not a specific percentage of travel company's turnover as was the case in the Hungarian legislation. Since the French rules also limited the value of guarantee, the French legislation had to be modified to reflect the ECJ's interpretation of Article 7.

[9] RGF Annual Report 2013.

[10] See the French Law n° 2009-888 on the development and modernisation of tourism services (Loi n° 2009-888 du 22 juillet 2009 de développement et de modernisation des services touristiques).

[11] Arrêté du 23 décembre 2009 relatif aux conditions de fixation de la garantie financière des agents de voyages et autres opérateurs de la vente de voyages et de séjours.

[12] Décret n° 2015-1111 du 2 septembre 2015 relatif à la garantie financière et à la responsabilité civile professionnelle des agents de voyage et autres opérateurs de la vente de voyages et de séjours.

[13] European Court of Justice, Order of 16 January 2014, case C-430/13, Ilona Baradics and Others v QBE Insurance, [2013] EU:C:2014:32.

Recent and proposed changes and impact assessments

There is no comprehensive impact assessment of the financial guarantee scheme (e.g. on market players or consumers). In the French legislation, impact assessments are only compulsory for projects concerning national laws and not for those concerning administrative decrees.[14] The relevant regulation on the financial guarantee was implemented in a series of decrees, two Arrêtés in 2009 and 2014 and a Décret in 2015, and not as a law.

That said, there is a high-level impact assessment document (Fiche d'impact) for the 2015 Décret which describes qualitatively the net financial benefits of the proposed legislative for different stakeholders, companies, local and central governments, etc., as neutral or reduced cost and risk.[15]

The structure of the travel trade industry

In 2015, French citizens bought 23.8 million package holidays.[16] Package holidays outside France totalled 9 million, equating to 37.8 per cent of all outbound trips. Travellers spent €9.7 billion during outbound package holidays, or 38 per cent of all expenditures in outbound trips. Similar percentages for outbound package holidays were observed in 2013 and 2014.

The French agency Atout France maintains the register of licenced tourism companies. As of May 2017, there are 6,749 companies registered.[17] About half of them are tour operators and travel agents, the rest being accommodation providers, passenger transport companies, recreational activity companies, non-profit and local tourism organisations, and producers of gift boxes (i.e. selling vouchers, not actual reservations, for accommodation and leisure activities).

The structure and performance of the consumer protection scheme

Following the 2015 Décret, a company selling package holidays in France is now required to obtain a financial guarantee from a single entity, either the APST, an appropriate financial institution, or an approved non-profit organisation. The financial guarantee has to cover the full cost of sold package holidays and be renewed annually.

Since the financial guarantee can be obtained from different sources, there is no single fund that accumulates all guarantees and pays out compensations. As a consequence, there are no comprehensive industry statistics on the performance of the financial guarantee scheme in France, e.g. the total value of fees paid by travel companies and the obligations of all failed companies.

However, the APST as one of the largest guarantors (70 per cent of all travel agents and tour operators) publishes annual reports on the performance of the association and its guarantee fund. In 2015, the APST provided approximately €1.55 billion in nominal guarantees to its members of which €0.97 billion was matched by counter-guarantees provided by the companies (e.g. a personal or bank guarantee).[18]

According to the APST, in the industry as a whole 148 companies filed bankruptcy cases in 2015, of which 51 were members of the APST. In the same year, the APST processed 32 cases that involved claim refunds with nearly 13,200 travellers affected (the cases were opened in 2014-15). Nearly 80 per cent of all customers were clients of one failed tour operator, Consult/Destination Privilèges.

[14] For more details, see e.g.: https://www.legifrance.gouv.fr/Droit-francais/Etudes-d-impact

[15] Fiche d'impact : Décret n° 2015-1111 du 2 septembre 2015. Available online at [accessed on May 15, 2017] https://www.legifrance.gouv.fr/content/download/9233/112399/version/1/file/fi_EINI1509560D_11_05_2015.pdf

[16] Directorate General for Enterprises, Ministry of Economy, France (2016) "Le tourisme des Français en 2015" (The tourism of the French in 2015). Available online at [accessed on May 15, 2017] http://www.entreprises.gouv.fr/etudes-et-statistiques/4-pages-57-tourisme-des-francais-2015

[17] Source: https://registre-operateurs-de-voyages.atout-france.fr/web/rovs/accueil

[18] APST (2015) Annual report, page 5.

The value of claims submitted to the APST in the same year reached €6.1 million, of which €2.9 million was covered by the collapsed companies' counter-guarantees. The remaining €3.1 million thus represents the expected net cost to the APST of providing guarantees to failed companies for that year. Looking further back in time, over the past decade the expected total value of uncovered claims for all failure cases between 2006 and 2015 is €5.1 million. The final net cost for uncovered claims will only be known once the settlement process for all the collapses is complete, a process that can take several years for some collapses.

The APST maintains and develops control systems to detect signs of failures and minimise the risks. The system is based on:

- Financial documents of the company members and analysis of the resulting document database.
- Requirements for professional indemnity insurance.
- Analysis of legal and administrative changes.

2.3 The Netherlands: SGR and GGTO

Historic overview

The Dutch Stichting Garantiefonds Reisgelden (SGR, Travel Compensation Fund Foundation) was established in 1983. The new fund replaced the existing voluntary protection fund created by the Dutch Association of Travel Agents (Algemene Nederlandse Vereniging van Reisbureaus, ANVR) in 1971. The SGR claims it was the first compulsory travellers' protection fund among the then EU Member States. The SGR would accept guarantees from travel companies and provide excess cover in the event of company's failure when the guarantee was not sufficient.

The SGR regulation was codified in the Dutch Civil Code in 1992 following the EU PTD1.[19] Since January 2017, the SGR protection extends to foreign customers buying package holidays from Dutch travel companies, to comply with the EU PTD2, and to business customers. As of early 2017, the SGR was also considering mutual agreements and/or recognitions with other national funds in the EU.

In 2012, a separate fund Garantiefonds voor Gespecialiseerde Touroperators (GGTO, Guarantee Fund for Specialized Tour Operators) was established. It offers protection for customers of small specialised tour operators, e.g. selling holiday trips to remote destinations. These companies must be registered in the Netherlands, act as direct sellers (i.e. no agents or re-sellers) and deal with domestic consumers only (i.e. no sales to foreign customers).

Recent and proposed changes and Impact assessments

The SGR legislation remained relatively stable, without major changes or revisions of the SGR principles. Partly as a consequence of this stability, there have been no impact assessments of the existing SGR scheme or ex post evaluations of the SGR performance. Furthermore, no impact assessment was conducted prior to the start of the GGTO fund.

The structure of the travel trade industry

In 2014, the Dutch consumers made nearly 47 million trips for personal reasons, of which 40 per cent were outbound trips.[20] Package holidays were not common, accounting for only 22 per cent of all foreign holidays. The travellers spent in total around €21.5 billion on tourism and related activities abroad, of which approximately 31 per cent were linked to package holidays. A large share of trips, flights and accommodation was booked via the internet, often directly with the service provider.

[19] See the Dutch Civil Code, Book 7, Title 7A "Travel Arrangements".
[20] Source of figures: Eurostat and own calculations.

According to Eurostat, there were approximately 3,900 travel agents and tour operators in the Dutch travel industry in 2014.[21] The largest four companies are TUI Netherlands, BCD NV, Corendon and Thomas Cook.[22]

The structure and performance of the consumer protection scheme: SGR

The SGR publishes annual reports that summarise failures in the travel industry and the SGR financial performance.

As of December 2016, the SGR had 786 registered members which represents a decline of over 100 members in three years from the total of 894 members there were in 2013. The number of members is less than 3,900 as some travel agents and tour operators might be registered as sales branches or affiliates of SGR members. Further, some travel companies are registered with the GGTO rather than the SGR.

Each SGR member must provide a bank guarantee that covers 1.5 per cent of turnover, or at least €5,000. The bank guarantee must conform to the general requirements of the European Central Bank. The members may voluntarily supply an additional bank guarantee. Alternatively, the SGR may ask to increase the guarantee based on an assessment of the company's financial results.

In case of failure, the amount of individual claim is limited to €10,000 per customer per travel.

The number of company failures varies greatly from year to year, with only 1 case in 2015 and 17 cases in 2013. The latter figure includes the failure of OAD Reizen in September 2013, one of the largest bankruptcies on the Dutch travel market in the recent years.

Travel company failures have a different financial impact on the SGR. Some failures do not lead to financial losses as the value of claims is covered by the respective bank guarantees. In other cases, the SGR meets some of the claims from a captive insurance company that it has created and for which it owns 100 per cent of the capital. The SGR equity has fluctuated between €80-87 million in the last 4 years. The net cost, if any, results from the main SGR activity, i.e. payment of claims and recovering the amount via the guarantee, insurance or legal action. Revenue comes from annual membership fees, fines for cases the appellant loses in the Appeal Committee and the SGR's investment activity.

In a small number of cases which the SGR believes are due to mismanagement, it considers legal action against travel companies' management to cover the fund losses.

The annual membership fee is differentiated by company turnover and by turnover realised on the national and foreign markets (see Table 2.3).

Table 2.3: The SGR annual participation fee

Turnover, € million	Annual fee, €, for domestic turnover	Annual fee, €, for turnover abroad
Below 0.25	270	250
From 0.25 up to 2.5	870	500
From 2.5 up to 12	1,440	1,000
From 12 up to 50	2,160	2,000
Above 50	4,980	
Affiliate / sales branch *	28	not applicable

Note: * The affiliate / sales branch pays the fee of €28 irrespective of size class.

The above fee structure has been in place since January 2016. The previous fee schedule had only two classes based on the sales realised under the company's own name, namely, €1,422 and €284 for turnover above and below €150,000, respectively. As more companies offer re-sale, i.e. effectively acting as retail units, the SGR believed that the two-tier structure did not reflect the market risks and the SGR workload, hence, the

[21] The Eurostat data on Structural Business Statistics (number of enterprises, turnover, etc.) typically lags 2-3 years.

[22] Source: TravMagazine (November 2016) "Top 50 Reisondernemingen (Top 50 Travel companies)."

new five-class fee structure.[23] Some companies questioned the new schedule as their fees increased five-fold, from €284 to €1,440.[24] According to a media source quoting the SGR director, "one third of [SGR] participants moves from a higher to a lower rate, a third remains the same, while a third moves from a lower to a higher rate."[25]

The structure and performance of the consumer protection scheme: GGTO

The GGTO membership is limited to small specialised tour operators with the maximum annual revenue of €1 million. The GGTO has 240 members as of July 2017.

The GGTO does not publish annual reports, but it does provide some information on its website. The GGTO is still building up its equity but has not publicly specified the target amount.

The annual membership fee is 0.125 per cent of turnover. Given the limit on turnover, the fee can be at most €1,250. There is also a levy per booking of €15.

The GGTO members have to meet specific requirements for solvency and liquidity. The company is deemed solvent if its equity is at least 15 per cent of total tangible assets. The company has enough liquidity if it has sufficient amount of cash, including a credit line, to cover one-month fixed cost. If the company cannot meet these requirements it can obtain a loan and keep it as a deposit, or provide a bank/private guarantee.

There have been no failures since the GGTO establishment in 2012 yet. In principle, in case of failure, the amount of individual claim is limited to €10,000 per customer per travel (as in the SGR case).

The GGTO operates on the principle of solidarity. If there is a failure and the fund loses less than 50 per cent of its equity the fund would absorb the loss. However, if the fund loses more than 50 per cent of its equity the loss in excess of 50 per cent would be divided between the existing members in proportion to their turnover and treated as a loan to the fund. When the fund rebuilds the equity in subsequent years it would pay back the loan (compensate the excess loss) to the members at the interest rate of 2.5 per cent.

2.4 Norway: Reisegarantifondet

Historic overview

Norway created the Reisegarantifondet (RGF, Travel Guarantee Fund) in 1982. The travel guarantee scheme was implemented in 1995 by the Package Travel Act.[26] In principle, the guarantee provided by a travel company to the RGF should cover the company's obligations in case of failure and the RGF would act as the excess in case the guarantee turned out to be insufficient.

Between 2006 and 2009, the Norwegian tourism industry saw a series of bankruptcies that depleted the RGF and necessitated a revision in the funding rules. Supplementary regulations on the RGF were adopted in 2007 and 2009. Further regulation came into force in March 2017.

The 2007 Regulation introduced a formula for calculating the value of guarantee.[27] The formula includes, among other parameters, the expected turnover for the peak month in the coming year, the number of travellers in that month and a charge per travellers. The value of guarantee was further differentiated into

[23] SGR Letter, December 22, 12015 "Participant contribution (Deelnemersbijdragen)". Available online at [accessed on July 17, 2017]: https://www.sgr.nl/~/media/files/sgr%20deelnemersbijdrage.ashx

[24] https://www.travmagazine.nl/13724-2/

[25] https://www.travmagazine.nl/14135-2/

[26] The 1995 Package Travel Act is called: Lov om pakkereiser og reisegaranti (pakkereiseloven). Available online [accessed on May 15, 2007] https://lovdata.no/dokument/NL/lov/1995-08-25-57

[27] The 2007 Regulation is called: Forskrift om reisegaranti og stiftelsen Reisegarantifondet (reisegarantiforskriften). Available online [accessed on May 15, 2007] https://lovdata.no/dokument/SF/forskrift/2007-01-03-3

four classes, depending on the company turnover. The Regulation also introduced an annual flat fee of NOK 2,000 (approximately €210 at current exchange rates) to maintain the fund's equity.

By 2009, following several major company failures, the RGF equity dropped by almost one half. The 2009 Regulation replaced the flat fee of NOK 2,000 with a differentiated fee, according to company class.[28] The fees were calculated so that the total amount collected would be sufficient to restore the RGF equity to a suitable amount (which was defined during the consultation, see below). The fee for the smallest companies (class 1) increased to NOK 3,500 while the fee for the largest operators (class 4) increased to NOK 70,000. Once the fund equity stabilised by 2012, the fee was reduced for the first three classes and remained unchanged for the fourth class.

Finally, the 2017 Regulations introduced an annual differentiated fee to finance the Disputes Resolution Committee (the business classes are different to those for the annual fee).[29] The Committee deals with customer complaints to travel organisers. The latter would be required to pay a fee of NOK 1,000 for each case lost in the Committee (in addition to the annual financing fee).

Recent and proposed changes and Impact assessments

Two important consultations on the RGF regulation dealt with, respectively, the introduction of the differentiated annual fee in 2009 and implementing EU PTD2 into Norwegian Law.

The consultation accompanying the 2009 Regulation summarised the history of bankruptcies in the tourism industry and explained the principles for calculating the differentiated fee schedule.[30] As laid out in the consultation paper, the RGF equity reduced between 2003 and 2009 from NOK 30 million to approximately NOK 12 million as a result of several major bankruptcies. The Consultation paper referred to the principle of the Danish guarantee scheme that the RGF equity should be enough to cover the two largest bankruptcies that occurred in the last 10 years. The Consultation paper also proposed to add a buffer to that amount. Together, this meant that the RGF equity should be equal to NOK 15 million. Given the existing equity of RGF of NOK 12 million (in 2009), that meant the fund needed an additional NOK 3 million to restore its financial position to the new level.

The consultation paper proposed to differentiate the fee by the company class using the ratio of 1:2:5:20. Table 2.4 summarises the proposed fee schedule, the number of companies in each class, and the expected cost and revenues. Overall, the new fee schedule was expected to generate NOK 1.4 million of net revenues per year which should be enough to restore the fund equity within three years to the target amount (NOK 15 million). As an alternative to the differentiated fee, the paper suggested a flat fee of NOK 8,933 would generate the same total fee revenue.

Table 2.4: Proposed fee schedule for the RGF

Fee class	Turnover, NOK million	Number of companies	Fee, NOK	Total, NOK million
1	Less than 0.25	150	3,500	0.525
2	From 0.25 up to 1	477	7,000	3.339
3	From 1 up to 100	120	17,500	2.1
4	At 100 or above	3	70,000	0.21
			Total fee revenue	6.174
			RGF operating expenses	3.4
			Expected (forecast) losses per year	2
			Expected net revenue per year	1.4

Source: The Consultation paper (2009).

[28] The 2009 Regulation is called: Forskrift 13 okt 2009 nr. 1275.
[29] The 2017 Regulation is called: Forskrift 25 jan 2017 nr. 97.
[30] For details on the 2009 Consultation, see: https://www.regjeringen.no/no/dokumenter/horing---forslag-til-endringer-i-reisega/id571331/

Some large tour operators criticised the proposed fee structure insisting that it is the smaller companies that go bankrupt more often and, therefore, should bear the cost.[31] However, the new fee schedule was adopted in the 2009 Regulation.

The other consultation took place between 2013 and 2016 in relation to the EU PTD2.[32] The consultation summary stated that the new Directive would affect more market players, but would also lead to more fees being collected by the RGF, so that it should not have a substantial effect on public finances or the RGF equity. The consultation summary noted mixed views from stakeholders, with some parties in favour of the new Directive stating, in particular, that it would provide a level playing field for Norwegian and foreign companies. Others, however, were critical of the expanded definition of tour package, or argued that the new Directive would reduce certain aspects of protection available to Norwegian customers.

The structure of the travel trade industry

Norwegian households spent approximately NOK 16 billion on services offered by tour operators and travel agents annually between 2012 and 2015.[33] This include flights, accommodation etc. sold through tour operators. The spending on package holidays constitutes about one third of all tourism expenditures on transport, accommodation and leisure activities.

According to RGF reports, there are over 800 tour operators and travel agents working in the industry. The three largest tour operators are Ving (owned by Thomas Cook), Star Tour (owned by TUI Group) and Kuoni Group trading under the brand name Apollo.

The structure and performance of the consumer protection scheme

The RGF publishes annual reports on the fund activities, bankruptcies and fund financial performance.

As of 2016, there were 839 members covered by the RGF. The three largest tour operators, Ving, Star Tour and Kuoni, accounted for 63 per cent of the guarantee volume.

After the fee increase in 2009, the RGF rebuilt its equity up to nearly NOK 19 million by 2012. The fee was then reduced and, as a result, the amount of revenue raised through the fees dropped by almost one half (NOK 3.7 million in 2014 versus 6.2 million in 2012). However, as there have been no major failures since 2012, the fund equity has remained relatively stable since then fluctuating between NOK 19 and 22 million.

Only one bankruptcy case in 2016 resulted in substantial losses to the RGF, as a result of a mismatch between the value of the guarantee and the compensation paid to travellers. As explained in the RGF annual report, the customers paid for the travel much earlier than the guarantee for the corresponding travel period was provided to the RGF by the company, hence, the loss to the fund.

2.5 The UK: ATOL Scheme

Historic overview

The Air Travel Organiser's Licence (ATOL) scheme was introduced in the early 1970s to support the growing market for organised tourism. The ATOL arrangements underwent a series of transformations, mostly in response to failures of major tour operators.

Prior to the ATOL scheme, the protection was provided voluntarily by tourism trade associations. When introduced, the ATOL scheme covered repatriation only but not advanced payments (for holidays that had not started by the time of failure). However, after the failure of Court Line Group, the then second largest

[31] See, for example, an article here: https://reiselivsnytt.wordpress.com/2009/08/11/apollo-sier-ja-ving-sier-nei/

[32] For details on the EU Directive Consultation, see: https://www.regjeringen.no/no/sub/eos-notatbasen/notatene/2013/nov/pakkereisedirektivet/id2434724/

[33] Source: Statistics Norway (Statistisk sentralbyrå, SSB)

tour operator, in August 1974, the ATOL scheme introduced levies as a per cent of turnover to protect advanced bookings. After a failure of International Leisure Group in 1991, the UK's Civil Aviation Authority (CAA) took responsibility over the fund from the trade associations. The EU PTD1 adopted around the same time affected the definition of package holidays and, hence, the amount of protection available to travellers.

By April 2008, the bond and levy as a percentage of turnover were replaced by a single flat charge based on number of bookings. The initial charge of £1 was soon increased to £2.50 after the then third largest tour operator XL Leisure collapsed in August 2008.

Recent and proposed changes and impact assessments

The latest major revision of the ATOL scheme was implemented in 2012 to increase consumer clarity and reflect the changes in the way people book and organise package holidays nowadays (i.e. increased Internet sales and personalised packages). The two measures finally chosen for implementation were:

- Protecting flight-plus arrangements under the ATOL scheme, i.e. when flight and accommodation/car hire are booked within 24 hours from the same provider.
- Introduction of an ATOL certificate issued to the consumer at the time of booking or first payment.

As part of the 2012 consultation, the UK's Department for Transport (DfT) conducted an impact assessment of the two measures in 2012. The study concluded that the new arrangements would provide the total net benefit ranging from –£24 to +£35.4 million depending on the scenario.[34]

Another consultation on the ATOL scheme was held in 2014 in light of the then proposed EU PTD2.[35] The consultation considered a number of changes for the ATOL fund. Table 2.5 lists some of the potential measures discussed and opinions about them summarised in the consultation paper (note that none of the measures were considered for implementation before adoption of EU PTD2).

Table 2.5: Potential changes to the ATOL scheme

Measure	Summary of consultation opinions
Industry-led scheme	Concerns about bias and impartiality.
Insurance-based scheme	Difficulty in assessing the risks and concerns about potential fraud.
Co-existence of multiple guarantee schemes and/or funds	Some schemes might be more selective than others and companies with higher risk of failure might concentrate on one, less selective fund.
Modify or withdraw protection provided by the credit card issuers	Credit card protection applies to any product not just package holidays so not feasible.
Separate funds for repatriation and refund	Refund claim could shift to merchant acquirers and banks increasing their cost.

Source: own elaboration.

The structure of the travel trade industry

Table 2.6 summarises 2015 data on UK personal holidays and inclusive tours. Package holidays constitute 35-37 per cent of all trips to North America and Europe (including non-EU countries) and 55 per cent of trips to other countries. Similar percentages are observed for the number of nights and the amount of spending.

[34] Department for Transport (2012) "Reforming ATOL Scheme: Impact Assessment DfT00092." Available online at [accessed on May 15, 2017] http://webarchive.nationalarchives.gov.uk/20160809232630/https:/www.gov.uk/government/uploads/system/uploads/attachment_data/file/3430/dft-ia-00092-reforming-atol-scheme.pdf

[35] Department for Transport (2014) "Response to the call for evidence on the review of Package Travel Directive and ATOL implementation and funding arrangements" Available online at [accessed on May 15, 2017] https://www.gov.uk/government/consultations/atol-call-for-evidence

Table 2.6: Holidays and inclusive tours: visits, nights and spending, 2015

	All holidays (millions)			Inclusive tours (millions)			Inclusive tours as percentage of all holidays		
	Visits	Nights	Spend, £	Visits	Nights	Spend, £	Visits	Nights	Spend
North America	2.4	32.9	3.2	0.8	10.1	1.2	35%	31%	38%
Europe	34.5	281.6	17.5	12.9	98.9	7.3	37%	35%	42%
– of which EU	32.2	261.7	16.2	11.9	90.3	6.7	37%	35%	41%
Other Countries	5.3	78.5	5.6	2.9	34.4	3.0	55%	44%	53%
Total World	42.2	393.0	26.3	16.7	143.3	11.4	40%	36%	44%

Source: UK's Office of National Statistics (ONS) and own calculation. The total might not add up due to rounding.

As of January 2017, there are just over 2,000 ATOL holders who jointly cover approximately 26 million passengers. The top 30 companies account for nearly three-quarters of licensed passengers.[36] The top five largest ATOL holders are TUI UK, Thomas Cook, Jet2holidays, Expedia, and On The Beach.

The structure and performance of the consumer protection scheme

The current ATOL scheme covers travel that is booked with a single company and includes flight plus at least one other major service, such as accommodation, car hire. The ATOL scheme differentiates the licence by business type (standard, small, franchise, etc., see Table 2.7) but the actual levy (ATOL protection contribution) is the same £2.50 per passenger for all companies.

Table 2.7: ATOL licence types

Business type	Type definition	License fee - fixed part, £
Standard	No trading restrictions	1,918*
Small Business	Max 500 passengers and £1m licensable revenue per annum for minimum three years	1,132
ABTA Joint Administration	ABTA members with estimated licensable turnover of £1.5m or less	721*
Franchise	Max 1,000 passengers per annum	721
Accredited Bodies	Accredited Body's conditions of membership	20,300**

Notes. * The Licence fee for Standard and ABTA Joint licences also have a variable part of 12.03 pence per passenger/seat.
** The Licence fee applies to an Accredited body as a whole, not to individual members.
Source: CAA.

The ATOL fund is administered by the Air Travel Trust (ATT) that publishes, in its annual accounts, statistics on the amount of funds collected and the list of company failure cases together with the amount of compensation in each case. In 2016, the ATT collected £62.9 million of passenger levies and spent £4.7 million (about 8 per cent) on compensation to customers of 19 failed companies.[37]

To protect against company failures, the ATT holds insurance against situations where the costs arising from refunds and repatriation exceed £75 million in the case of large operator failure and £10 million in case of small operator failure. There were no claims on the insurance in 2016.[38]

[36] Source: CAA ATOL Authorisations database and own calculations. The database is available online at [accessed on May 15, 2017] https://www.caa.co.uk/ATOL-protection/Check-an-ATOL/ATOL-data-download/
[37] Air Travel Trust "Annual Report & Accounts 2016/17", page 6.
[38] Air Travel Trust "Annual Report & Accounts 2016/17", page 20.

2.6 Key findings

A review of five national schemes shows that:

- There is no universal solution or principle for organising the travellers' protection scheme.
- Many countries have experienced sizeable failures in the travel industry in recent years, which in some cases prompted changes to their scheme.
- The schemes tend to include a mix of individual company guarantees and an industry-wide fund to meet claims when the company guarantee is insufficient
- In some countries, there is a (temporary) industry-wide levy to build up or replenish the industry-wide fund.
- Each scheme uses some form of monitoring companies' accounts, possibly with the varying frequency of reporting based on the company's size. The available evidence suggests that the information being monitored is similar to the data that the CAR monitors.

3 Assessment of existing scheme

In this chapter we draw on the findings of the desk-based research, data analysis, interviews with stakeholders and comparisons with other national schemes to evaluate the performance of the current consumer insolvency protection scheme in Ireland. The assessment considers

- The effectiveness of the scheme in achieving it objective of consumer protection in the event of insolvency for those consumers who are covered by the scheme; and
- The efficiency with which this objective is achieved.

In Chapter 4, we set out and assess possible options for scheme reform using these same criteria.

3.1 Structure of the current scheme

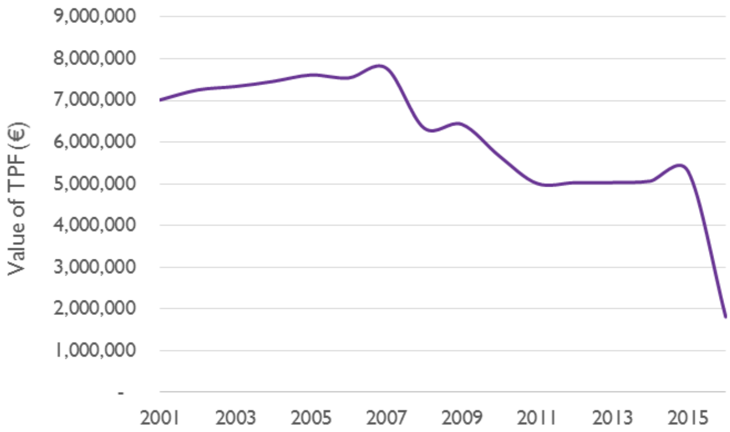
The original legislation underpinning the current scheme dates back to the Transport (Tour Operators and Travel Agents) Act 1982. The legislation was updated by the Package Holidays and Travel Trade Act 1995, which incorporated EU PTD1.

The scheme provides financial protection to consumers, for refund and repatriation, in the event that their licensed travel agent or tour operator collapses and is no longer able to fulfil its obligations to that customer. The scheme provides protection to consumers who have bought foreign travel only or travel packages (e.g. travel plus accommodation). It does not cover purchases directly from service providers, e.g. airlines and bed banks, or packages which do not include a travel component.

The 1982 Act requires that any tour operator or travel agent buying, selling or arranging foreign travel originating in Ireland must be licensed and correctly bonded. Travel-trade companies must apply for a licence every year and to do so must submit financial information, provide evidence of the appropriate bonding and pay the relevant licence fee. Legislation specifies that travel agents and tour operators must maintain bonding equivalent to 4 per cent and 10 per cent of projected licensable turnover respectively. Bonds can take several forms: a cash deposit with the Commission or IFSRA-registered bank or financial institution; a bank or insurer guarantee; or a collective agreement.

The bond is the first source of funds to cover refunds and repatriations in the event of a collapse. Where the funds from the bond are insufficient to cover the claims costs, the Commission will draw on the Travellers' Protection Fund (TPF). The TPF is held by the Department of Finance and administered by the Commission. It was originally funded by a levy on customers of tour operators during the 1980s. The levy was stopped in 1987, when the TPF was considered to have met a sufficient level to provide adequate consumer protection based on analysis of past collapses. Figure 3.1 below shows the evolution of TPF since 2001.

Figure 3.1: Evolution of TPF turnover over time



In the last decade, the volume of package holidays covered by the scheme has declined, based on the trends in projected licensable turnover used to calculate the volume of bonds that travel agents and tour operators have to post. In 2007 it was €2.4bn while in 2016 it was €1.2bn. This decline in licensable turnover is observed both across travel agent and tour operators. That said, as seen in Figure 3.2, the total licensable turnover has actually seen a small recovery since 2011, driven by growth in travel agent licensable turnover.

Figure 3.2: Licensable turnover over time

3.2 Effectiveness of current scheme

At the most basic level the current scheme has been effective: consumers who have bought packages covered by the current regime from licensed and bonded Irish travel agents or tour operators have enjoyed financial protection. On occasions when a travel-trade firm has ceased trading and been unable to meet all its obligations, customers overseas have been repatriated and those yet to travel have had (valid) claims for refunds paid out in full.

In the 35 years since the 1982 Act introduced the scheme, almost 11,000 claims totalling €15 million have been paid to customers of licensed travel-trade firms that were unable to meet their obligations. The claims have been spread across 58 separate instances of licences travel-trade firms being unable to meet their obligations – 49 travel agents and 9 tour operators. This is less than two "collapses" per year. To provide some context, in 2016 there were 277 licensed travel agents and tour operators. Moreover, in the past 10 years alone more than 250 firms have exited the industry (i.e. not renewed their licence) without any customer needing a refund or repatriation. The bonding arrangements only prove necessary for a small number of firms.

Figure 3.3: Number of collapses by year and type of organisation

3.2.1 Coverage of past collapses under the current scheme

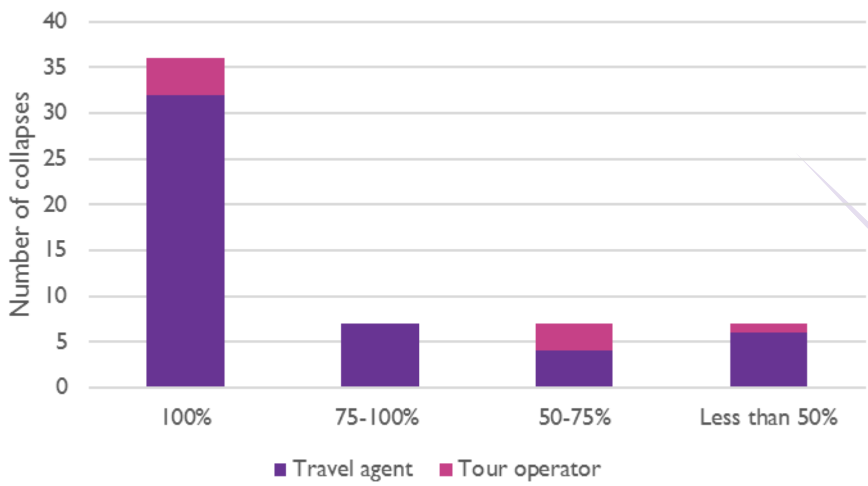
Claims have primarily been covered by bonding

Claims resulting from past collapses have drawn on a combination of bonding and the TPF. This is true both in the case of travel agents and tour operators collapsing.

Evidence shows that for the majority of past collapses claims were fully covered by the bond (36 of the total 58 collapses, or 62 per cent). Several industry members we met stressed that because of the way their business operates the current bonding requirement is excessive, since either they will always be able to fulfil their contractual obligations or, if they do get into difficulties, the resulting claims that could arise would be a fraction of their bond (perhaps because they forward payments onto suppliers immediately after receiving customer money). The experience of travel-trade collapses to date, as depicted in Figure 3.4 shows that most firms that collapse prove to have had a bond in excess of what was necessary to meet the claims arising, i.e. with the benefit of hindsight, a lower bond would have sufficed for these firms.

Where bonding is insufficient, the remaining value of claims is met through the TPF. Only in seven cases (12 per cent) has the bonding covered less than 50 per cent of the total claims.

Figure 3.4: Percentage of claims covered by bonding requirement



Average claims for travel agents and tour operators exceed current bonding levels

Separate analysis for travel agents and tour operators shows that

- Claims as a percentage of projected licensable turnover were 6.5 per cent for travel agents and
- Claims as a percentage of projected licensable turnover were 14.3 per cent for tour operators,

This compares with the findings of CAR's 2008 review, which showed that bonding requirements of 3 per cent and 10 per cent for travel agents and tour operators would, on average, have been sufficient to cover claims.[39] The more recent collapses do not support the contention that claims as a percentage of licensable turnover will necessarily be lower now than they were in the past because of a change in the way the industry operates, albeit the number of recent collapses constitutes a small sample.

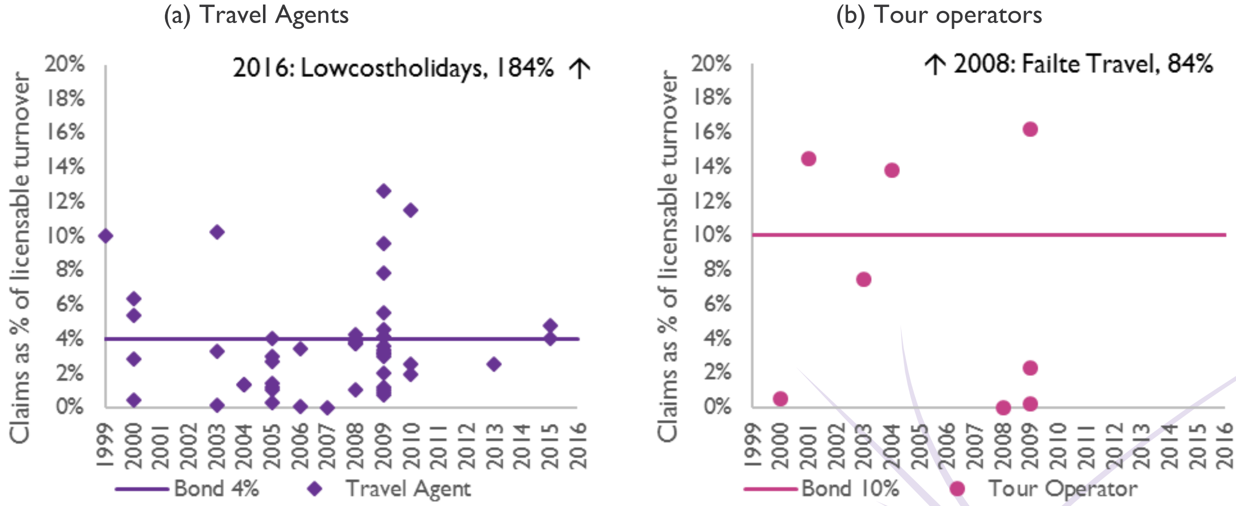
But this finding is driven by the collapses of Lowcostholidays and Failte Travel

There have been two collapses that gave rise to claims totalling in excess of 80% of projected licensable turnover, Failte Travel and Lowcostholidays.ie. These are unusually large. If we excluded them from the analysis, claims as a percentage of projected licensable turnover would be 3.1 per cent for travel agents and 5.7 per cent for tour operators.

More generally, there is notable variation around these average claims…

The variation in claims following a collapse is significant, as illustrated in Figure 3.5. Even for those firms where the bond proved adequate, there is a marked variation in how much of the bond was required. In those cases where the bonding covered 100 per cent of the claims resulting from the collapse, the percentage of the total bonded amount required to do so was on average 49 per cent. In some cases, the bonding was only just sufficient, while in other cases less than 10 per cent of the total bonded amount was drawn upon (in the case of one travel agent collapse, less than 1 per cent of the bond was drawn upon). This variation is found for collapses of both travel agents and tour operators – thus with hindsight it is possible to find examples of travel agents and tour operators who were over-bonded in the sense that their bond exceeded the value of claims arising.

Figure 3.5: Claims as a percentage of licensable turnover for individual collapses by year



Note. The left figure for travel agents excludes Lowcostholidays Spain SL (TA) with 184 per cent value. The right figure for tour operators excludes Failte Travel Limited Travel Operator with 84 per cent value.

However, there have also been cases where the claims have significantly exceeded the bonding amount, particularly in 2009 for travel agents.

[39] Page 39, CAR (2008) "Review of Travel Trade Legislation in Ireland. CP5/2008. https://www.aviationreg.ie/_fileupload/Image/2008-09-11_CP5_TTReview_Revision.pdf

… and changes in bonding rates would have had a significant impact on draws on the TPF

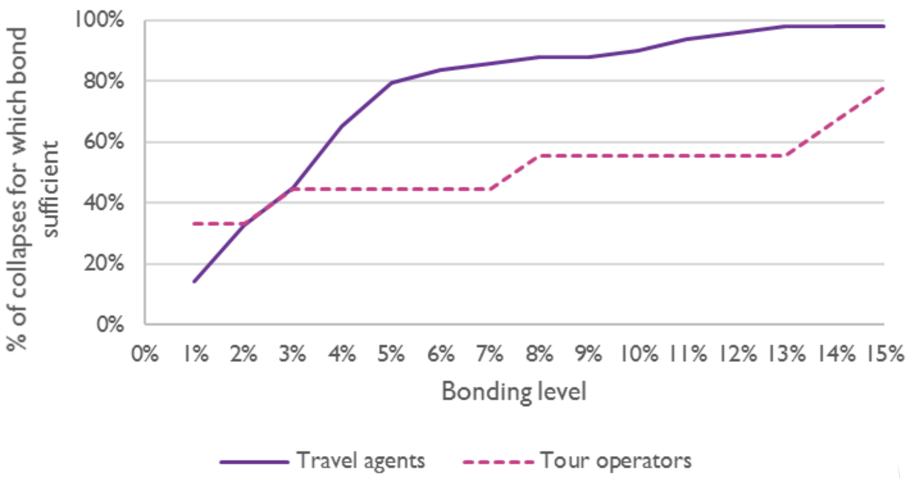
Analysis of past collapses can be used to understand what the impact would have been had the bonding requirements differed from the current levels of 4 per cent and 10 per cent for travel agents and tour operators respectively. The analysis, as presented in Figure 3.6, shows that a change in the bonding requirement has a significant impact on the adequacy of the bond, particularly for travel agents.

The analysis shows that had travel agents had a bonding requirement of 3 per cent, only 45 per cent of travel agent collapses would have been completely covered by the bond (compared to 65 per cent under the current scheme). At 2 per cent bonding this falls to 33 per cent, and at 1 per cent bonding only 14 per cent. With the exception of Lowcostholidays, a 13 per cent bonding requirement would have been required to fully cover all past travel agent collapses (i.e. without a need to draw on the TPF). Lowcostholidays would have needed a 184 per cent bonding requirement to avoid drawing on the TPF.

In the case of tour operators, a bond of 8 per cent would have had no effect on the percentage of collapses covered entirely by the bond (albeit it would have of course affected the total drawn on the TPF, as we shall come onto discuss). However, bonding requirements lower than this would have resulted in less than half of tour operator collapses being covered fully by their bond. With the exception of Failte Travel, a 17 per cent bonding requirement would have been required to fully cover all past tour operator collapses. Failte Travel itself would have required bonding of 90 per cent.

Given events since the Commission's 2008 report, the figures for bonding requirements capable of covering all collapses (as provided above) are significantly higher than those reported in the Commission's 2008 report. The 2008 report found that bonds of 10 and 15 per cent for travel agents and tour operators respectively would have been sufficient to have funded all the claims from bonds without recourse to the TPF.

Figure 3.6: Percentage of collapses for which bond sufficient at different bonding levels



By determining the amount of funds that must be held in a bond by each firm, the bonding requirements also affect the subsequent draw on the TPF. Figure 3.7 below shows that, as the bonding requirement falls, the draw on the TPF obviously increases. This is particularly marked for travel agents below the 4 per cent bonding requirement. Indeed, had the travel agent bonding requirements been 2 per cent or less over this period, then the TPF would already be fully exhausted. At 3 per cent bonding, there would have been about €800,000 now left in the TPF. A similar, though less marked, picture can be seen for tour operators.

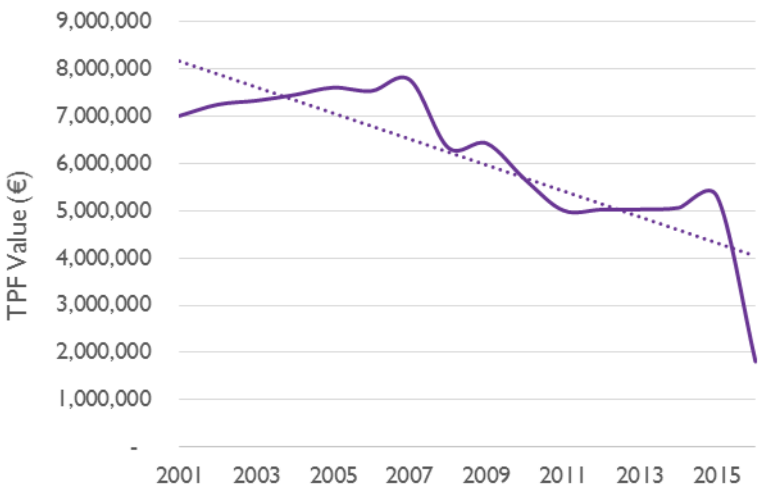
Figure 3.7: Total draws on the TPF at different bonding levels

The TPF would be at risk in the event of another major collapse or market-wide downturn…

If there is no replenishment of the TPF, i.e. no new levy, it is difficult to predict exactly how long the TPF will remain in credit. This is because, as shown in Figure 3.8, the TPF goes through periods of relative stability (1998-2007 and 2009-2015), but has also suffered sharp collapses. The sharp collapses in 2008 and 2015 can be attributed to two specific collapses, the tour operating arm of Failte Travel and Lowcostholidays respectively. The sharp decline in 2009 is the result of a number of losses triggered as a result of the 2007-8 financial crisis and the global recession that followed.

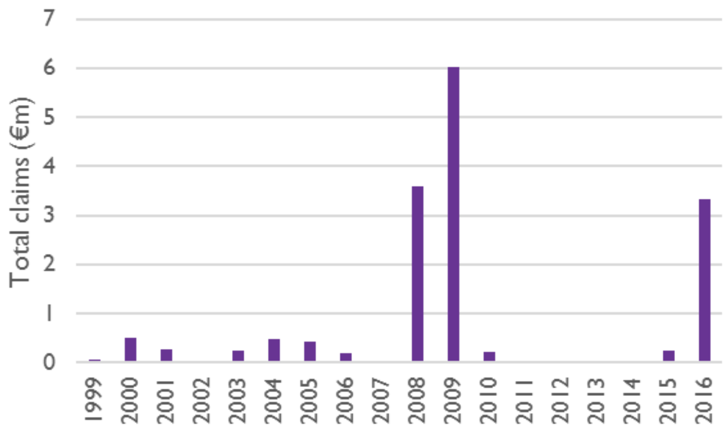
Taking the average value of decline per year over the 1998 to 2016 period and simply projecting this value forward suggests that the TPF would only last another five full years. However, in reality, it is somewhat naïve to put an expected timeframe on the longevity of the TPF (without further intervention), given the unpredictable timing of any significant draws upon it. The TPF would be at risk of failing to cover a future collapse of the ilk of Failte Travel or Lowcostholidays, or a general market downturn affecting a number of firms concurrently (as in 2009). If the combination of bond and the full TPF was insufficient to cover all claims, payouts would need to be prorated, resulting in only partial protection for customers.

Figure 3.8: Evolution of TPF over time



Moreover, although projected licensable turnover is materially lower than a decade ago, it is important to recognise that the TPF could still be subject to large draws against it. Lowcostholidays collapse last year is evidence of this. Figure 3.9 shows no clear evidence of a downward trend in the absolute value of claims over time to reduce the burden on the TPF.

Figure 3.9: Total claims



Claims primarily relate to refunds for upcoming holidays rather than repatriation

In the event of collapse, the majority of claims costs relate to refunds for upcoming holidays (rather than repatriation for holidays currently in progress). Since 2008, there have only been repatriation costs incurred in three of the collapses.

Of the three cases that involved repatriation since 2008, only one of those cases required draw down on the TPF. This was the collapse of the tour operator Failte Travel which generated claims of €1.7m against a bond of only €200,000. That said, client refunds alone accounted €1.4m of the total €1.7m, thus meaning that the bond was inadequate even in absence of any repatriation costs.

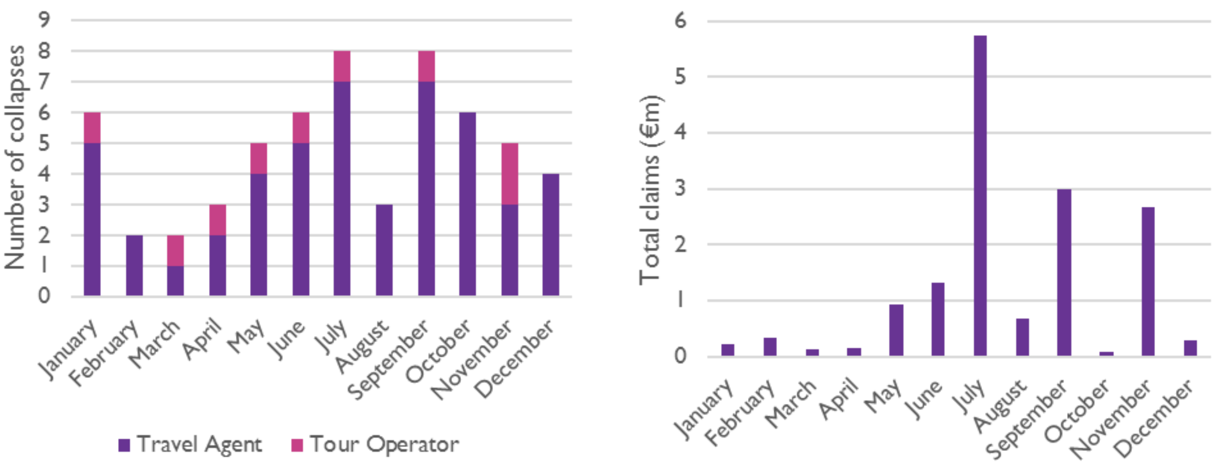
Firms are often cash rich in summer, but this does not lessen the likelihood of collapse

The seasonality of a firm's business model may also be relevant in determining the likely claims that will arise should the firm be unable to meet its contractual obligations. For example, the costs associated with repatriating passengers for a firm specialising in ski holidays should differ considerably depending on whether the collapse happens in February or August. However, under the current regime, this firm is required to have the same sized bond in both months.

Stakeholder discussion suggested that many travel agents and tour operators experience higher cash flows in the run up to and during summer. The maximum exposure of a typical travel firm should therefore be higher during this period relative to the rest of the year. However, although maximum exposure would be higher, stakeholders suggested that the likelihood of collapse is actually lower as a result of being more cash rich. However, analysis of past collapses does not suggest that collapses are less likely during the summer, as shown in Figure 3.10.

Figure 3.10: Number of collapses by month

(a) Number of collapses (b) Total value of collapses

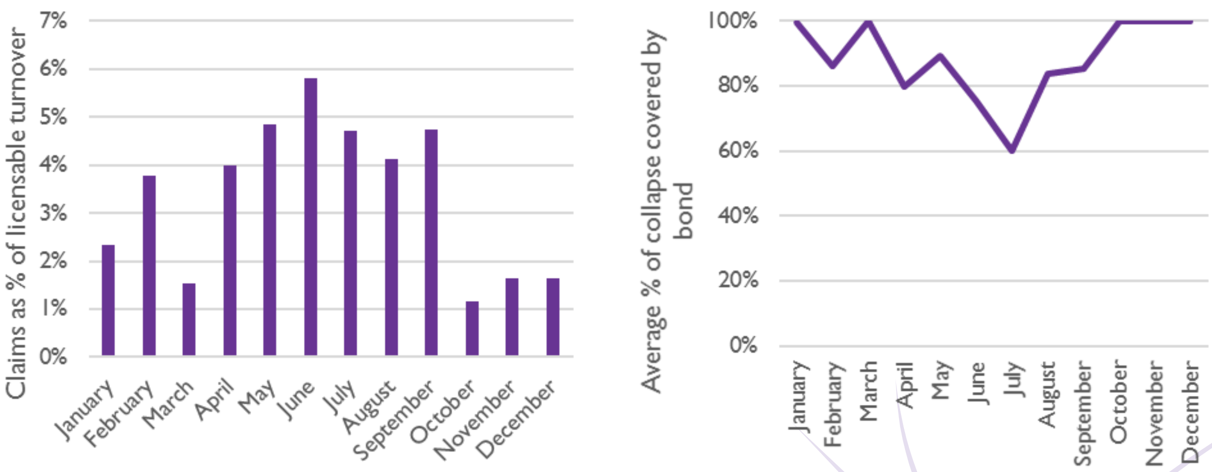


… with claims against turnover higher for summer collapses, thus drawing more on the TPF

The above observation that collapses are no less likely in the summer months is of particular concern given that claims in summer months are, on average, greater as a percentage of licensable turnover (Figure 3.11a). By extension this means that during summer months the bond is less likely to cover the total cost of the collapse (Figure 3.11b). This is consistent with a view emerging from stakeholder interviews that there are certain times of the year when the bonding requirement would not be sufficient, while there are other times when it is excessive.

Figure 3.11: Relative size of claims and bond coverage by month

(a) Claims against licensable turnover average (%) (b) Average percentage of collapse covered by bond



While claims are typically found to be more material and bonds less sufficient during summer months, this will of course not be true of all licensed firms. The extent to which any given travel firm matches this market average will depend on the precise business model (e.g. the types of holidays offered and the payment terms specified).

Initial turnover projections are in general accurate, but some firms repeatedly underestimate

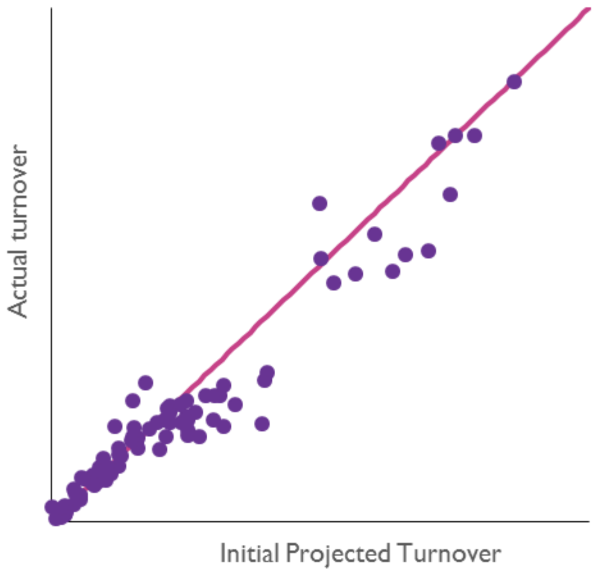
Putting aside the issue of appropriate bonding percentage, bonding requirements based on projected turnover are only useful to the extent that projected turnover is a close reflection of actual turnover. If actual turnover significantly exceeded projected turnover then in the event of a collapse there is a greater risk of the bond being insufficient.

We analysed data for five consecutive years (2012 to 2016) for a sample of travel-trade firms to assess the accuracy of initial turnover projections against actual realised turnover. [40] We find that firms' initial turnover projections are generally in line with their actual realised turnover. Across the sample, we found that one-third of initial turnover projections underestimated actual turnover. Therefore, if initial turnover projections were taken at face value by CAR, then around one-third of companies may end up under bonded. However, in practice, bonding levels may not reflect original turnover projections for two main reasons: firstly, because CAR may challenge the projections and require the travel trade firm to revise projections before granting a licence; and, secondly, because firms may have had to increase bonding during the course of the year (e.g. by adding a supplementary cash bond) as a result of turnover exceeding expectations.

Among those cases where initial projections under estimate actual turnover, these are mostly on a one-off basis (i.e. for an individual year), with initial turnover projections for the following year either in line with or exceeding actual turnover. However, for a small number of firms initial turnover projections that underestimate actual turnover are found for two or more consecutive years. This may have given them an unfair competitive advantage over travel-trade firms that were adequately bonded, had their initial projections been taken at face-value by CAR.

Figure 3.12 illustrates the relationship by plotting the actual versus initial projected turnover for all companies and all years in our sample. The dots above the 45-degree line represent companies for which actual turnover exceeded its initial projected value. As can be seen, companies are on average fairly accurate in their initial predictions of turnover, with in fact a general tendency to overestimate turnover (i.e. there are more dots lying below the 45-degree line than above). However, there are nevertheless some companies whose initial projections under-estimate their actual turnover which would raise concerns about the adequacy of their bond, if these projections were not challenged by CAR and no revisions to the bond were made during the course of the year.

Figure 3.12: Actual versus initial projected turnover



[40] In some cases, it is not a perfect like-with-like comparison, as some firms' financial accounting years do not align with the licensing for which they provided initial turnover projections. However, while this may affect the accuracy of the estimated ratio of actual to projected turnover, our focus is on the order of magnitude of any discrepancies, and this is unlikely to be affected by such a misalignment.

Firms with both TA and TO licences typically project higher proportions of TA turnover

For firms wishing to operate in both the travel agent and tour operator space, the legislation requires that these firms have a separate licence and bond in place for each. Thus, a firm must project its licensable turnover as a travel agent and have a bond in place equal to 4 per cent of this, and likewise project its licensable turnover as a tour operator with a bond amounting to 10 per cent of this. Given that the bonding requirements are greater for tour operators, and therefore likely to be more costly, firms with both licences may have the incentive to over-project travel agent licensable turnover and under-project tour operator licensable turnover. If this were the case and the firm collapsed, then the bonding in place may not be sufficient to cover the claims generated.

Analysis of 2016 data for firms which have both a travel agent and tour operator licence finds that the bulk of projected licensable turnover is typically on the travel agent side. While this may be entirely legitimate given each firm's specific business model, it may raise warning signs about the potential for firms with both licences to be under bonded.

The biggest risk regarding projections might be overstatement of non-licensable turnover

Another possible risk with the way bonds are currently calculated is that a firm will require a smaller bond if it reports more of its turnover as non-licensable turnover. It is possible that firms will project and record low levels of licensable turnover as a share of turnover; should they collapse, it may turn out that in fact a much larger share of the turnover related to transactions for which the customer is entitled to a refund.

This may be relevant in the case of the Lowcostholidays collapse, where projected licensable turnover constituted a very small proportion of its total projected turnover. In 2014, its projected licensable turnover was 3 per cent of its total projected turnover, with this figure falling to 1 per cent for 2015 and 2016. As such, its bond would have constituted a very small fraction of its total projected turnover – in the order of 0.04 per cent (i.e. a 4 per cent bond on projected licensable turnover which is 1 per cent of total projected turnover). Thus problems may have in part arisen when Lowcostholidays collapsed, as some of the packages sold may not have been recorded as licensable turnover, resulting in claims that far outstripped projected licensable turnover.

Data from 2016 on projected licensable and non-licensable turnover shows that of the 234 companies for which full data were available, 36 (15 per cent) had projected licensable turnover as a proportion of projected total turnover of 10 per cent or less. There are a further 23 firms (10 per cent) for which projected licensable turnover is 20 per cent less. Therefore, Lowcostholidays was not unique in projecting turnover that is overwhelmingly non-licensable. If any of these firms are wrongly treating some turnover as non-licensable, then claims could vastly outstrip their bonds in the event of collapse.

Speed and transparency of the refund process

Consumer protection can be judged not only in terms of whether the consumer receives a full refund (and, if necessary, repatriation), but also in terms of the speed and transparency of the refund process. In the event that a collapse does occur, for some consumers it may not be possible to book an alternative holiday (or alternative accommodation, in the event that airline tickets were already paid for) until this refund has been received. For these consumers, the speed and transparency of the refund process is particularly crucial. Taking the collapse of Lowcostholidays.ie as an example, this generated a total of 4,174 claims which were all processed within six months of the collapse.

3.2.2 Market changes and their implications

Significant growth in direct bookings with airlines and accommodation providers

As was made clear in our discussions with industry, one of the major changes experienced is the huge increase in the number of individuals who now book flights and accommodation directly from the provider, rather than through a travel agent or tour operator.

This assessment of the scheme's effectiveness has no regard to the financial protection in place (or its absence) for those who do not buy packages from licensed travel agents or tour operators. A frequent criticism of the scheme that we have heard is that it only covers around 15 per cent of trips – a minority of all travellers. Depending on the critic's viewpoint, this may be considered evidence that the scheme is now *ineffective*, since many packages bought today are not covered. Alternatively, the critic may cite this as evidence that the scheme is *inefficient*, imposing a regulatory burden that customers have revealed exceeds any associated benefits by increasing the purchase of trips not covered by the scheme. This relates to a wider debate about who should enjoy what protection when purchasing travel, which is beyond the scope of this report.

Proliferation of credit and debit card payments

Credit and debit card use has increased significantly since the scheme's inception, but because the first port of call is still against the bond and the TPF, this has not changed anything (directly at least) in terms of the scheme's effectiveness. A travel-trade firm's consumers would only enjoy full protection if all of them used cards, or the combination of bond and TPF was adequate. That said, the proliferation of credit and debit card payments may have indirectly affected the scheme's effectiveness through its impact on cash flows.

Travel agents are holding onto customers' cash for much shorter time periods

Discussions with industry suggested that there have been major reductions in the length of time for which travel agents are holding onto their customers' cash.

One of the reasons for this is the move away from chartered airline services to predominantly scheduled airlines services, e.g. through Ryanair and AerLingus. Payment for scheduled airline flights is required much quicker than for chartered services, typically being executed by direct debit at most within two weeks of receiving customers' funds. Discussions with industry suggested that airline costs constitute on average about 50 per cent of the total package cost.

For accommodation services there is typically a longer period between receiving customers' funds and forwarding the payment to the provider. The large majority of accommodation is booked through accommodation only suppliers, i.e. bed banks. Given that they are not bonded and the crowded nature of the bed-bank market, they are generally perceived as riskier. As such, discussions with industry suggested that it is common practice for travel agents not to forward money onto the bed bank until the customer is checked-in or even departed. Consequently, accommodation funds can sit with the travel agent from the period at which full payment is due until the point of departure.

Even if booking directly with hotels, competition in this market has meant that the balance of power usually lies with the travel agents in determining payment dates (which are typically set as the date of customer arrival). However, travel agents specialising in lower volume, higher value business niches are likely to book directly with hotels (or other accommodation providers), fulfilling payments 4-10 weeks in advance rather than on customer arrival. Such specialisation is a growing phenomenon in the Irish travel agent industry, but the large majority of accommodation bookings are still done through bed banks.

Drawing on the above evidence, it is possible to generate worked examples of what a travel agents' maximum exposure might be. In the worked example below, we assume no seasonality in turnover at this stage. Introducing seasonality would increase the potential maximum exposure (but also returns us to the debate about whether travel-trade firms are likely to collapse in periods of their year when they are relatively cash rich holding lots of clients' monies).

Worked example of a travel agent's expected exposure (assuming no seasonality)

Travel agent licensable turnover: €2million

Airlines:
- Expenditure share: 50%

- Of which scheduled: 80%	- Of which chartered: 20%
- Payment received: Week 0	- Payment received: Week 0
- Payment made: Week 0	- Payment made: Week 2

Accommodation:
- Expenditure share: 50%

- Of which bed banks: 80%	- Of which direct: 20%
- Payment received: Week 0	- Payment received: Week 0
- Payment made: Week 7	- Payment made: Week 2

Weekly turnover: €38,462 (assuming no seasonality)

Maximum airline exposure: €7,692
i.e. 38,000 * 50% expenditure share * [(80% scheduled share * 0 weeks) + (20% chartered share * 2 weeks)]

Maximum accommodation exposure: €115,384
i.e. 38,000 * 50% expenditure share * [(80% bed banks share * 7 weeks) + (20% direct share * 2 weeks)]

Maximum total exposure: €123,077 (€7,692 airline exposure + €115,384 accommodation exposure)

Percentage of licensable turnover: 6.2% (€123,077 total exposure / €2,000,000 turnover)

3.3 Efficiency of current scheme

Good regulatory practice dictates that public policy goals should be realised as efficiently as possible: any additional costs associated with realising the policy goal should be kept to a minimum. The importance of keeping the regulatory burden low is perhaps especially important in the case of the Irish travel trade regime, if licensed travel agents and tour operators are not to be put at an undue competitive disadvantage when there are alternatives available to consumers wishing to purchase trips overseas that do not offer the same financial protection since their providers do not need to be licensed and bonded.

Over the years, the Commission has taken steps to address the administrative burden of the scheme. It ended the requirement that firms qualifying for an audit exemption from the Companies Registration Office nevertheless had to produce audited accounts to qualify for a licence, a recommendation arising from the 2008 review of the travel trade regime. Also, in 2010 and in 2017, the Commission's internal auditors reviewed how claims were being processed.

The efficiency assessment in this study is confined to an assessment of the costs for licenced entities. It, therefore, does not account for cost differences vis-à-vis firms (and potential competitors) that are not required to have a licence.

To assess the efficiency of the current scheme, as a starting point we considered the following:

- The costs of licensing, bonding and processing claims.
- The scheme's administrative complexity and the difficulty of monitoring adherence to it.

- The implications of the existing scheme for issuing licences and monitoring licence holders.

Licensing costs do not appear to be material

Most, but not all, firms we have spoken with do not think that the costs of the current scheme are excessive. To a travel trade firm, there are the costs of paying a licence fee to the Commission and the costs associated with spending time preparing a licence application. The latter should only be viewed as an incremental cost of the scheme to the extent that there are additional costs that would not be incurred in producing standard audited accounts. The Commission's 2008 Review of Travel Trade legislation assumed that for those already producing audited accounts, which they assume to comprise around 20 per cent of travel agents and 50 per cent of tour operators, the additional cost would primarily relate to producing an audited projection of licensable turnover for the following year. This is expected to cost approximately €500. For smaller firms who would not be required to produce audited accounts in the absence of the licensing requirements, the estimated cost was around €4,000.

The current structure of licence fees means that the larger tour operators pay a significantly larger sum than travel agents. There is a flat fee across travel agents irrespective of size, but a tiered structure for tour operators with licensing fees increasing with licensable turnover.

Table 3.1: Licensing fees

Licensable Turnover	Travel Agent	Tour Operator
Less than €635,000	300	300
€635,001 to €1,2700,000	300	600
€1,2700,001 to €3,810,000	300	1,550
€3,810,001 to €6,350,000	300	2,150
€6,350,001 to €12,700,000	300	3,100
€12,700,001 and €25,400,000	300	7,800
For every €1,2700,000 or part thereof in excess of €25,400,000	-	+300
Additional fee for new application	300	300
Amendment to licence	30	150

In 2015, the Commission received €188,000 in licensing fees. From a societal perspective, the licence fee is not a cost; instead the cost is the time and resources the Commission spends administering the scheme. The earlier data on CAR staff expenditures by type of activity suggests that the travel trade workstream is labour-intensive. The staff cost, and hence the total administrative cost, on travel trade depends, to a certain extent, on the number of licences and claims, if any, processed. In 2009, the total travel trade administrative cost comprised 39 per cent of total CAR costs. This was a higher share than in any of the previous five years (all of which, except 2008, had a corresponding figure of less than 20 per cent), and most likely motivated by the relatively high number of collapses in 2008/2009. More recent comparisons are not possible as no cost data by activity type is available since 2010 (nor prior to 2004).

Costs of bonding are more material, albeit still a very small fraction of turnover

In terms of the costs of the scheme, industry expressed concern about the costs associated with getting a bond (albeit still for several firms this is not seen as particularly burdensome). Bonds can take the form of a guarantee secured with an insurance company or a bank, or a sum of money held by the Commission deposited in an IFSRA registered bank. The legislation also provides for a collective bonding scheme underwritten by an insurance provider or any other scheme acceptable to the Commission. There are currently no approved collective bonding schemes, but for many years the ITAA ran one.

The burden associated with bonding varies by business. Some entities have suggested that posting a cash bond does not represent a significant cost to them; their organisation has the cash in place, so there is only the inconvenience of completing paperwork and the option value that the cash would have if they were not required to use it as a bond. For other firms, a cash bond is not an option and they have to rely on bank or insurance guarantees for their bond. The cost of such bonds is typically around 3-4 per cent of the value of the bond (but may vary from 0.5-5 per cent), which for a travel agent with turnover of €2,500,000 equates to an annual bonding cost of €3,000-4,000. For some this is not an immaterial amount for an annual bonding fee and can mean significant time is spent shopping around for a better deal.

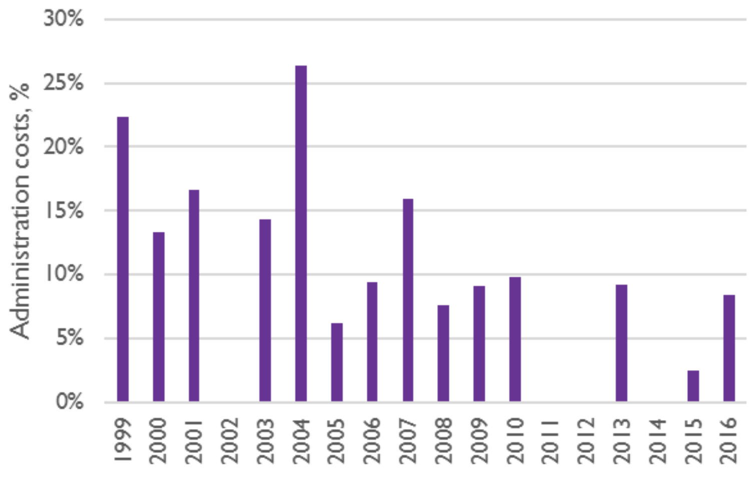
To the extent that the expected claims from each firm are known in advance and vary by firm, a relatively more efficient scheme would impose larger costs on firms that have the higher expected costs of claims. While not perfect, the current scheme partially meets this requirement. Firms projecting larger licensable turnover have to purchase larger bonds. Moreover, the costs of acquiring a bond are likely to be greater for firms in poor financial health – they may not have a large pool of working capital to call upon to serve as the cash bond, and are likely to find the banks and insurance companies wanting to charge a higher premium than would be the case if their financial position was healthier.

However, the relationship between the burden of the scheme's costs and those firms most likely to fail is not perfect. This is partly because the required bond does not vary according to the business model that the travel-trade firm uses. Two firms with the same projected licensable turnover will have the same bond requirement even if one never holds onto customers' cash instead forwarding payments to suppliers immediately, while the other does not pay any suppliers until after the holidays have been taken. These differences may lead to different premiums being charged if the firms seek a bank or insurance bond, but if both fund the bond via a cash bond then the firm with a safer business model from the perspective of the customer does not enjoy a cost advantage in terms of bonding costs. Nor will the administration costs be different, unless one of the firms attracts additional monitoring by the Commission.

Administration costs represent a small portion of total claims costs

Using data on past collapses from 1999 to 2016 shows that administration costs have on average constituted 13 per cent of the total costs associated with a collapse. Administration costs, as a percentage of total collapse costs, have declined over this period, averaging 19 per cent from 1999-2004, 12 per cent from 2005-2010 and 6 per cent from 2011-2016. For reference, on the Irish non-life insurance market, overall management expenses comprise about 20 per cent of total claims paid. In particular, for motor insurance and liability insurance each this share is approximately 22 per cent.

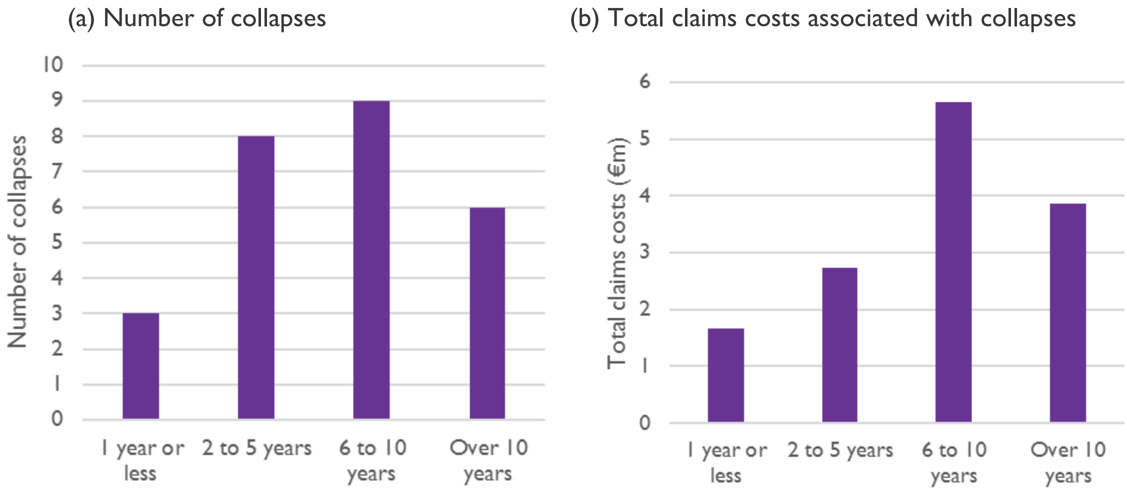
Figure 3.13: Administration costs as a percentage of total collapse costs



Increased scrutiny of new entrants does not appear necessary

As discussed above, for any firm that continues trading hindsight suggests that the scheme was inefficient, but the problem is identifying a priori which firms will get into difficulty. The available evidence does not support a claim that the Commission should focus its scrutiny on new licence applications. As Figure 3.14 shows, between 2008 and 2016 most collapses were by firms that had been trading for a number of years.

Figure 3.14: Prevalence of collapses for different aged firms



Since the introduction of more regular financial reporting requirements by the Commission in 2010, there have been six firms that have failed, only one of which was required to provide quarterly management accounts. Given such a small sample, it is difficult to conclude with evidence from the Irish scheme alone about the relative benefit of more regular monitoring of accounts. Evidence from the review of other national schemes (see Chapter 2) suggests that the CAR monitoring requirements (frequency and types of documents requested) are in line with those in other countries.

Limited efficiency concerns today, but nevertheless a key factor in assessing potential reforms

There is limited evidence to raise any immediate concerns about the efficiency of the current scheme (setting aside any discussion of whether financial protection is needed, or whether it should apply to all travellers or only those of travel agents and tour operators, which are beyond the scope of this study). This is true both from the perspective of individual firms and the Commission. The costs of licensing, bonding and processing claims appear relatively small. Taking typical cost estimates from above for licensing fees and completion of the licensing application, as well as annual bonding fees (assuming a 4 per cent bond cost), means that a travel agent with turnover around €2,500,000 would pay a total of €8,300 each year to cover licensing and bonding. The corresponding figure a tour operator with the same turnover would be slightly higher at €9,550. Assuming an average gross industry margin of 10 per cent, these costs represent about 3 per cent of total margin.

From a more top-down perspective, the actions of travel-trade companies established elsewhere in Europe might be cited as evidence that the current Irish regime is not overly burdensome administratively. In its latest annual report the Commission reported that no-one had availed of the exemption available to retailers and organisers established in other Member States of the European Union more than a year after the State Airports (Shannon Group) Act came into force. Instead, firms were choosing to remain within the Irish licensing regime.

While there are no apparent efficiency concerns with the current scheme, it is nevertheless still crucial to consider the efficiency implications of any scheme reforms (in Chapter 4). Therefore, although arguably reforms are focused on making the scheme more effective rather than addressing efficiency concerns, it is critical that the efficiency implications of any reforms are taken into account. As reforms to improve the scheme's effectiveness may come at costs to efficiency, a key judgement to make shall be whether or not any additional efficiency costs are justified by the greater consumer protection offered.

3.4 Summary of issues with current scheme

The current scheme cannot provide effective consumer protection without reform

The current situation with the TPF means that we cannot state with confidence that the current scheme will be effective in the future in repatriating travellers and refunding those yet to travel who have bought valid packages from bonded travel agents or tour operators. Indeed, past collapses have resulted in claims against the TPF in excess of the current value of the TPF. In particular, a collapse on a similar scale to Lowcostholidays would yield claims against the TPF that could not be met in full.

… and consumers with valid claims may start to suffer as a result

We suspect that it will be people with valid claims that may suffer. The detriment will be felt in two ways:

- First, the Commission is likely to delay paying out claims until it has received sufficient information about the total claims bill to be in a position to know what percentage of each claim it can meet given the size of the collapsed firm's bond and the value of the TPF. For those customers for whom a travel package represents a significant financial outlay relative to their wealth and income, such delays may mean that they are unable to take a holiday overseas that year.
- Second, where the Commission concludes the available funds are insufficient, claimants will only receive a fraction on each Euro of their claim.

The scheme could continue to provide satisfactory protection in the event of repatriation

The current scheme is likely to remain effective in repatriating passengers. It will not be practical for the Commission to delay repatriating passengers until it knows the total costs of claims from refunds and repatriation. Since 2008, only three collapses have resulted in repatriation costs, and in two of these cases the bond was sufficient to cover both the costs of refunds and repatriation. Given current industry practice, it seems unlikely that future collapses will generate repatriation costs that cannot be covered by the scheme. In particular, as most holidays now use scheduled flights which require the travel agent or tour operator to pay the airline at the time of the booking, a customer overseas should have a valid flight ticket home even if the firm they made a booking with has collapsed while they are on holiday. Repatriation costs could however still arise if the customers' accommodation has not been paid for. In these circumstances, decisions will have to be made about whether it is more cost effective to pay for accommodation such that the client returns on their scheduled flight, or whether to pay for a new flight so as to repatriate the customer immediately. If there is a prospect that claimants will only receive a fraction on each € claimed, that may persuade some consumers that their interests are best served by seeking immediate repatriation rather than joining the pool of people making claims.

… but full refunds for upcoming holidays could not be guaranteed with the status quo

As explained above, there have been cases of past collapses where the bond put in place by the firm was insufficient to cover all claims (at the current 4 and 10 per cent requirements), thus resulting in significant draws on the TPF which could not be sustained again given the TPF's current level. On average, current bonding levels fairly accurately capture the expected exposure of a firm in the event of a collapse based on its turnover. However, there have been significant 'tail' events in which the individual bond has been hugely inadequately and for which the draws on the TPF are not sustainable. Thus, while the scheme functions well in refunding customers for a 'typical' collapse, reforms should look to how the scheme can be reformed to ensure effective consumer protection in the event of any 'tail' events. This could be both by limiting the potential for such events occurring, but also by ensuring consumers are fully protected were such events still to arise.

There are no material efficiency concerns with the current scheme, but efficiency is a crucial factor in any proposed reform

Our assessment of scheme efficiency was restricted to an analysis of the costs of licensing and bonding for both the industry and the Commission, as well as the costs arising in the event of collapses. We find no material shortcomings with the scheme's current efficiency of operation that would warrant intervening on efficiency grounds alone (i.e. in the absence of failings of the scheme's effectiveness). However, given the clear mandate for intervention on effectiveness grounds (as set out above), it is important that the implications for scheme efficiency relative to the status quo are assessed in each case.

As there are clearly risks to consumer protection if the scheme remains unchanged, restoring guaranteed full consumer protection is clearly the priority of any suggested scheme reforms, but their implementation should not come at the expense of undue or avoidable costs to the industry (which have the risk of damaging the viability and competitiveness of their businesses).

4 Assessment of options for reform

There is a wide gamut of possible changes to the scheme that might be considered. We set out a number of them in Annex 2 and set out reasons for not taking forward some of those options. In this section, we provide a more detailed assessment of five reform options that we think the evidence and our discussions with industry warrant consideration as possible reforms which aim to restore the effectiveness of the scheme in providing consumer protection in the event of travel trade firms collapsing.

In thinking about the question of what constitutes an effective consumer protection scheme, attitude to risk is important. Short of shutting the travel-trade industry down or full government guarantee, we do not think that there is a travel-protection scheme that could be robust to all possible claims that may arise from collapses. The goal instead should be to design a scheme that is robust to as many collapses as practically possible, given the experience of collapses to date.

We have recognised in Chapter 3 that the existing scheme is sufficient for dealing with most travel-trade firm collapses, and so if the scope is restricted to purely covering typical collapses then no reform would be necessary.

Instead, the options for reform considered below are driven by the need to fully protect consumers in the event of atypical collapses. The options are driven by the motive that even in these more extreme cases customers still have the right to be fully refunded or repatriated. Indeed it is large collapses leaving many in need of refunds or repatriation that arguably motivated the scheme in the first place, as a way of providing customers with confidence that they were not taking undue financial risks when they bought package holidays from the travel-trade industry. Anticipating ex ante all of the possible events that could give rise to a large collapse will never be possible. For this reason, it is unrealistic to expect that the Commission will always be able to prevent large collapses from happening.

It also means that it is not possible to have complete confidence about the upper bound on what costs future collapses might generate. As such, we have developed options for reform by examining how the impacts of past collapses would have differed under alternate schemes. In particular, we have applied two thought experiments when thinking about this issue:

- What would be needed to have met all claims given the experience in Ireland to date?
- What would be needed to survive two collapses in quick succession that generate claims in line with the two collapses that gave rise to the largest claims in the past 10 years?

This is backward-looking approach, as only after the event will it be known if it is possible to have larger claims following a collapse than have been observed in the past. Indeed, the scale of the claims arising following the collapse of Lowcostholidays would not have been anticipated given collapses in the previous 30-plus years of the travel protection scheme in Ireland.

Each option is assessed in terms of the following three criteria:

- The need for legislative change in order for the proposed reform to take place.
- The impact on scheme effectiveness (in terms of the level of consumer protection offered).
- The impact on scheme efficiency (in terms of the costs of the scheme to the industry and regulator).

4.1 Option A: a bond only scheme capable of covering past collapses

Details of reform

This option would be a bond-only scheme, with no TPF to back up any claims in excess of the bond. The percentage bonding requirements would be set on the basis of past collapses, by estimating what bonding levels would have been needed to be in place to have resulted in no draws on the TPF. Based on past collapses in Ireland, this would suggest approximate bonding requirements of 200 per cent for travel agents and 100 per cent for tour operators (as evidenced in Section 3.2.1).

Requirement for legislative change

This option would require no changes in the current legislative landscape. The Commission has the power to determine bonding levels for both travel agents and tour operators. As such, this option could be implemented relatively quickly (at least from a regulatory perspective), which is desirable as the current scheme is deemed insufficient for consumer protection.

Impact on scheme effectiveness

This option speaks to the question posed earlier of what would be needed to have met all claims given the experience in Ireland to date. In other words, had this option been in place (instead of the current system), it would have provided full consumer protection in the event of all past collapses.

The question, of course, is to what extent its ability to cover all past collapses is indicative of an ability to cover future collapses. There are certain (extreme) scenarios in which it may not prove sufficient:

- In the event that all payments (for a year) had been collected from consumers but yet to be paid out to the actual service providers. In this scenario, refunds would be equal to actual turnover, as no onward payments to airlines or accommodation providers would have been made. In the case of tour operators, this would mean that refunds would exactly equal the bond (since a bond equal to 100 per cent of licensable turnover is required). However, once the costs of administration are added to this, total claims costs would exceed the value of the bond and consumer claims would need to be pro-rated. Of course, this is an extreme scenario, both because firms are likely to take payment from customers at lots of different times throughout year and because make payments are made to service providers on an ongoing basis (and in the case of airline payments typically immediately), such that only a fraction of total turnover should ever be exposed.
- In the event that the collapse occurs while a significant portion of a travel-trade firm's customers are away and need repatriating. In such circumstances it is difficult to predict what the total claims costs may be, as this will depend on the costs of providing a consumer with alternative accommodation or with an earlier return flight. Evidence has shown that there has only been three collapses since 2008 that have resulted in repatriation costs, and in only one of those cases was the bond insufficient (covering just less than 75 per cent of repatriation costs when a 10 per cent bond was in place). As such, it appears extremely unlikely that a collapse could generate repatriation costs in excess of 100 per cent or 200 per cent of turnover in the case of tour operators and travel agents respectively).
- In the event that actual turnover significantly exceeds projected turnover, then the bonding levels may be insufficient. However, given that a travel-trade firm is typically only exposed to a fraction of its turnover at any one time, the bonding requirements should mean that there is sufficient buffer in place (unless actual turnover exceeds expected turnover several-fold).
- In the event that a significant portion of total turnover is wrongly designated as non-licensable turnover. As with the previous scenario, this could result in the bonding based on projected licensable turnover being insufficient, although again the fact that typically only a small fraction of turnover is exposed at any given time should mean that 100 and 200 per cent bonding requirements provide sufficient buffer for such an eventually.

Overall, while any one of the above scenarios in isolation appears extremely unlikely (and even entirely infeasible), some combination of the above scenarios could conceivably see a collapse that generated claims in excess of a 100 per cent bond in the case of tour operators or 200 per cent in the case of travel agents. In other words, although Failte Travel and Lowcostholidays are the most extreme cases observed to date (in terms of insufficiency of bond), some combination of the above factors could in theory result in an even more extreme outcome in future (that even 100 and 200 per cent bonding levels are insufficient for).

This finding is of course inherent to any proposed change to bonding levels, because it effectively seeks to address the outcome of the problem (i.e. an ineffective consumer protection scheme due to claims significantly exceeding bonding levels), rather than the sources of that problem (i.e. the factors which have led to collapses where claims have significantly exceeded bonding levels).

Impact on scheme efficiency

This scheme would impose **material costs** on travel trade firms relative to the status quo. For a typical travel agent with licensable turnover in the order of €2,500,000, a bond of 200 per cent would equate to an absolute bond value of €5,000,000. Many firms that currently post a cash bond may no longer be able to rely on that option and instead have to seek a bank or insurance bond. Assuming a bank or insurance bond cost of 3-4 per cent, the annual bonding costs would be in the region of €150,000 to €200,000. For a tour operator operating at the same turnover, a bonding requirement of 100 per cent would equate to an annual bonding cost of €75,000 to €100,000. These estimates probably overstate the likely cost as the premiums charged are unlikely to increase linearly as the bonding requirement for a given business model increases.

Nevertheless, the change would be a considerable cost to the industry that could put licensed firms at a **significant disadvantage**, both to non-licensed domestic competitors and to foreign licensed firms. It could also act as a significant barrier to entry for the industry. Taking a prospective travel agent entrant who may project licensable turnover of €500,000 for their first year of operation, this would require a bond of €1,000,000. This additional start-up cost could have a material impact on entry. Even aside from the initial sunk cost, it may reduce the appetite for entry given an expectation of lower margins due to the on-going bonding costs.

There is no strong reason to expect that this option would have a material impact on the costs to the regulator.

Overall

We do not think that this option is a sustainable long-run option. Yet if there was an unwillingness to replenish the TPF then eventually the scheme's effectiveness would depend on bonds being suitably sized.

Even as a short-run solution, we do not think increases in the bonding level alone will be the most efficient way of ensuring the scheme is effective. It would be possible in the short-run to take advantage of the fact that the TPF has not been fully run down and impose a smaller increase in bonding requirements. However, even with the current TPF, the required bond increases would have to be large if the scheme is to protect against the possibility of a collapse similar to the scale of Lowcostholidays.ie. A one or two per cent increase in the bonding levels would not be sufficient for the scheme to be effective in those circumstances.

Table 4.1: Summary of Option A against key evaluation criteria

Criteria	Assessment
No need for legislative change	✓
Impact on scheme effectiveness	✓✓✓
Impact on scheme efficiency	✗✗

4.2 Option B: increase the TPF through a tour operator levy and leave bonds unchanged

Details of reform

This option would involve replenishing the TPF to a level that would be capable of surviving two collapses in quick succession that generate claims in line with the two collapses that gave rise to the largest calls against the TPF in the past 10 years. Once restored to this level, the reform would be structured so as to sustain the TPF at this level, based on the expected value of annual claims against the TPF.

Based on an analysis of past collapses, a TPF capable of surviving two extreme collapses in one year would need about €6 million at the start of the calendar year. Given the TPF's current level of €1.3 million, this would require reintroducing a levy to raise €4.7million of additional funds for the TPF if there was no change in bonding levels.

The two worst collapses since the scheme's introduction in terms of absolute value of claims against the TPF, Failte Travel and Lowcostholidays, generated costs net of the bonds in place of €5,156,000. This latter figure is significantly larger than the TPF, consistent with our earlier contention that the current arrangements should not be seen as effective in providing full protection to customers of travel agents and tour operators in the event of such a firm ceasing to trade.

When the levy was originally introduced to build up the TPF, it was a levy applied to tour operators only. Currently the legislation is such that the Commission only has the power to levy tour operators in order to build up the TPF. For this option we consider the levies necessary to replenish the TPF without any legislative changes, i.e. by levying tour operators only.

The levy could be raised per licensed tour operator sale on either a fixed or percentage basis to raise the required funds. Based on 2016 licensable turnover for tour operators of €188million, a fund raising requirement of €4.7million could be met by imposing a one-off levy of 2.5 per cent per transaction for one year. On a fixed-fee basis, given that the average package cost is around €550 per person, this would equate to a one-off €13.75 levy per person booking with tour operators for the first year. Raising the funds over a longer timeframe would obviously require a lower percentage or fixed levies per transaction, but would mean that the TPF remains insufficient for a longer period.

Once restored, in order for the TPF to be sustainable over time, a levy contributing €350,000 on an annual basis would have sufficed to cover the average annual absolute fall of the TPF from 2001 to 2016. This would require an ongoing levy on tour operators of approximately 0.2 per cent per transaction, equivalent to just over €1 per person. The Commission would need to keep the size of the levy under review, taking into consideration the size of the TPF and the more recent history of collapses. Rather than imposing an ongoing levy, the Commission could choose to reintroduce the levy periodically when the TPF needs restoring to a sufficient level.

Requirement for legislative change

As with Option A, this option to levy tour operators only would require no legislative change.

Impact on scheme effectiveness

This scheme would provide full consumer protection in the event of a repeat of the two worst collapses experienced over the last 10 years occurring in the same year. This scheme is sustainable on an ongoing basis to the extent that the claims against the TPF each year moving forward are on average equivalent to those seen from 2001 to present, i.e. an average fall of €350,000 per year.

However, given the uncertainty with which extreme events occur, there is still inherent uncertainty about the sustainability of such a scheme. Indeed, the fact that the Lowcostholidays collapse occurred only last year does not reduce the chances that a similar scale of collapse occurs in the forthcoming year. As such, if a major collapse, or collapses, like this happen in the near-term then the funds in the TPF could quickly be deemed insufficient once more, meaning claims would need to be pro-rated. This may require a temporary hike in the levy (similar to that set out above) until the TPF is restored to a level of €6 million, after which the levy can revert to a lower ongoing level once more.

For the above reason, the pure bonding approach set out in Option A can be considered more sustainable from a consumer protection perspective insofar as a large collapse in any one year does not affect the level of consumer protection available the next year (as firms are always required to post the same percentage bond). This is in contrast to Option B where a collapse in any one year influences the maximum level of consumer protection available in the next year (due to the fall in the level of the TPF).

Impact on scheme efficiency

This option would impose no costs on travel agents (except for those also holding a tour operator licence). Travel agents would actually benefit in terms of an improved competitive position relative to tour operators, especially in the first year when levies are imposed for tour operators – the scale of which is dependent on the approach to replenishing the fund. This could encourage consumers to seek alternatives (e.g. booking through a travel agent, a foreign licensed travel trade firm or direct with airlines and accommodation providers). This competition effect may be particularly pronounced today (relative to when the scheme was first introduced), as the distinction between tour operators and travel agents has become increasingly blurred.

Tour operators could adapt to the levy in two ways:

- If tour operators choose to absorb the cost of the additional levy then they would see margins per package sold fall, but should maintain current sales volumes (other things being equal).
- If tour operators choose to pass on the cost of the additional levy to consumers, then they could sustain existing margins but this may be at the expense of lower sales volume, as consumers substitute to cheaper alternatives (travel agents, direct booking etc.).

In both cases, profits would fall for tour operators. The choice between the two would depend on consumer elasticity of demand for tour operator services. The more elastic demand is (i.e. the more price sensitive consumers are), the more of the cost increase that tour operators should absorb, as the volume effect would outweigh the price effect.

If the impact on tour operator margins were sufficiently material then some tour operators could exit the market (or else scale back their tour operating activities in preference for travel agent business). To the extent that this occurs, the burden on remaining tour operators would need to increase so as to ensure sufficient funds are still raised for the TPF. As such, there could be a vicious circle, whereby high levies lower tour operator licensable turnover, which requires levies to be increased, which further reduces tour operator licensable turnover and so forth.

Overall

This option, as with Option A, would allow an appropriate level of consumer protection to be quickly restored, without the need for legislative change. This option does not present as sustainable a solution to consumer protection as in Option A, as periodic increases in a levy may be required following major future collapses which put the TPF at risk of depletion.

Option B can be seen to come at less of a cost than Option A when considered for the industry in aggregate, albeit tour operators would see a noticeable impact on their cost margins and competitiveness.

Table 4.2: Summary of Option B against key evaluation criteria

Criteria	Assessment
No need for legislative change	✓
Impact on scheme effectiveness	✓✓
Impact on scheme efficiency	✗

4.3 Option C: increase the TPF through a levy on tour operators and travel agents and leave bonds unchanged

Details of reform

Instead of introducing the levy on only tour operators, as described in Option B, the TPF could be replenished through a levy on both tour operators and travel agents.

One rationale for originally levying just tour operators was that, at the time, most travel agents were selling tour operators' products, so all travellers enjoying the protection of the scheme were effectively bearing the cost of funding the TPF. However, that is no longer the case and the distinction between travel agents and tour operators is increasingly blurred. Given these industry trends, a system that more fairly distributes the cost burden across those who enjoy the benefits of that protection should look to levy both travel agents and tour operators.

The levy could be raised per licensed sale on either a fixed or percentage basis to raise the required funds. Taking 2016 total licensable turnover across travel agents and tour operators of €1.2billion, this would require a percentage levy per transaction of 0.35 per cent to raise the required €4,200,000 over one year. Raising the funds over a longer timeframe would obviously require lower percentage levies per transaction. On a fixed fee basis, and given that the average package cost is around €550 per person, a €2 levy per person is likely to be sufficient to raise the required funds in one year.

On an ongoing basis, in order to ensure the TPF was topped up by €350,000 per year (as in Option B), this would require a percentage levy of 0.03 per cent per transaction or a fixed levy of €0.16 per passenger. The corresponding figures for Option B were 0.2 per cent and €2. As in Option B, the Commission would need to keep the size of the levy under review, based on the size of the TPF and the more recent history of collapses. It may then need to impose higher levies in certain periods to restore the TPF to a sufficient level.

Requirement for legislative change

This option would require legislative change. Currently, the Commission only has the power to levy tour operators, but not to levy travel agents. Given the time that such legislative change may take, and given that the current scheme is already ineffective from a consumer protection perspective, some transitional arrangements may be needed in order to ensure consumer protection in the short-term before the relevant legislative changes have been made.

Impact on scheme effectiveness

The impacts on scheme effectiveness would be the same as those set out in Option B. In short, this scheme should provide full consumer protection in the event of a repeat of the two worst collapses experienced over the last 10 years occurring in the same year. We discuss the potential limitations of this approach in Option B above.

Impact on scheme efficiency

There should be no material impact on the competitiveness of travel agents or tour operators relative to each other, as both parties are subject to the levy in this option. However, tour operators and travel agents may lose out to other potential competitors, e.g. consumers choosing to book directly with airlines and accommodation providers, or choosing to book through foreign-licensed travel agents or tour operators. Travel-trade firms would be detrimentally affected to the extent that any pass-through of costs to their customers, resulting in customers switching away to alternative products.

Our discussion with industry suggests that any such passenger levy would be passed directly onto the consumer as part of the package. There were concerns among industry about the potential competitive implications of this, as several stakeholders said that consumers do not value the protection the scheme provides ex ante (in other words it is only valued if the collapse were to occur). As such, customers would face a small rise in costs, with many perceiving no corresponding rise in benefits (the majority would perceive the package as unchanged, but more costly). This may be particularly true for those customers who purchase by credit or debit card and believe that they are already protected by chargebacks.

That said, as the burden of replenishing the TPF is shared across both travel agents and tour operators, the levy per transaction (in fixed or percentage terms) is significantly lower than in Option B. In particular, this is because total travel agent licensable turnover is more than five times that of tour operators. As a result, fixed levies would need to be about €2, or percentage levies of about 0.35 per cent, compared with €13.75 or 2.5 per cent in Option B. The ongoing levy would also be materially lower for the same reason. As such, although some consumers may substitute to alternative products, the limited change in overall package price should mean that such an effect is limited.

Overall

Option C would require legislative change as travel agents cannot be levied under current legislation. The impact on scheme effectiveness should be similar to that in Option B, but the impacts on scheme efficiency should be less material as the burden is now shared across both travel agents and tour operators.

Table 4.3: Summary of Option C against key evaluation criteria

Criteria	Assessment
No need for legislative change	✗
Impact on scheme effectiveness	✓✓
Impact on scheme efficiency	~

4.4 Option D: redefine licensable turnover

Details of reform

Currently, the bonding requirements are defined as a percentage of projected annual total licensable turnover. However, our analysis in Chapter 3, suggests that one-size-fits-all approach does not reflect the underlying risk of different business models.

Through our discussion with industry, we were made aware of three scenarios where sums currently included in the calculations of licensable turnover could be excluded from the calculations and sums eligible for claims with little or no risk to the customer:

- Immediate payments to suppliers – these are payments when the incoming customer funds are immediately forwarded to the service provider, such that the travel agent or tour operator does not hold the customer's funds. Discussions with industry suggest that most airline payments today fall into this category, with travel agents and tour operators typically paying immediately for seats on scheduled flights as customers make the booking. Airfares typically constitute 50 per cent of the total package price.
- Trips paid for after the event – for corporate customers in particular, travel agents and tour operators may have long-standing relationships and invoice their client in arrears rather than requiring up-front payment prior to each package sold. As a result, licensed travel firms may pay the relevant airline and accommodation providers in advance of receiving the funds from their corporate customers meaning that the customers' money is never at risk.
- Card payments – as evidenced in Chapter 3, an increasing number of customers are now paying by credit and debit card. Although customers have no statutory protection in the event of a product or service failing to be delivered when purchased by card, in Ireland current MasterCard and Visa scheme rules (which constitute the vast majority of transactions) mean that an issuer will refund the customer in the event of such a failure. The card issuer then seeks redress from the merchant acquirer through the chargeback process. As such, with the existing scheme, customers purchasing on credit or debit card are doubly protected – first by the travel protection scheme, and second by the card scheme rules. The scheme could be changed such that card payments were excluded from the calculation of licensable turnover, and instead the money were to be reclaimed through chargeback.

Of these scenarios, perhaps the one which poses the greatest risk is card payments because customers could lose financial protection altogether if the current chargeback arrangements in Ireland were to change. Furthermore, we recognise that re-assigning liability from the travel-trade scheme to the card schemes may not realise cost savings for travel-trade firms, since the merchant acquirers may increase the charges they levy on travel-trade companies accepting card payments.

Given the above reservations we focus here on redefining licensable turnover for the purposes of setting the bond to exclude payments immediately made to suppliers and trips paid for after the event. This could be seen as an administratively simple version of a risk-assessed bonding requirement, with the risk assessment for each firm based on three simple criteria: total projected licensable turnover (as defined under old scheme); projected turnover from corporate clients invoiced after the trip; and projected turnover related to airline bookings. When devising its final proposal, the Commission may want to vary these criteria for the purposes of calculating licensable turnover, perhaps including just one of these factors we have suggested or adding others parties identify.

In this scenario, percentage bonding requirements would need to be adjusted because the remaining licensable turnover is riskier than licensable turnover as originally defined. On the basis that immediate payment to suppliers (i.e. payments to airlines) typically constitute 50 per cent of package costs, the redefined licensable turnover for a typical tour operator or travel agent should approximately halve.[41] Thus, in order to retain the current absolute level of bonding for the typical travel-trade firm would require the bonding rate to double (from 4 to 8 per cent for travel agents, and 10 to 20 per cent for tour operators), Of course, some travel-trade firms would see absolute bonding levels rise (if they have a high proportion of non-immediate payments), while others would see absolute bonding levels fall.

Under this scheme the absolute level of bonding should be broadly unchanged. Even though bonding requirements are more targeted at the risks of each individual travel-trade firm, they would still be by no means capable of covering collapses in the manner of Failte Travel or Lowcostholidays. Therefore, the TPF would still need topping up to be capable of surviving two similar extreme collapses in one year. As described earlier, this would require the TPF to be replenished to €6million, through a 0.35 per cent (or €2 per person) levy on travel agents and tour operators for the first year, followed by lower ongoing rates of 0.03 per cent or €0.16 per person. The size of the levy would need to be kept under review by the Commission.

Requirement for legislative change

This option would also require legislative change to permit the Commission to collect a levy from travel agents. Moreover, work will be needed to redefine licensable turnover for the purposes of setting the bonding requirement.

Impact on scheme effectiveness

This option would offer marginally more protection than Options B and C because the bonding requirements are more targeted, with riskier travel-trade firms (i.e. those holding onto customer money for longer) required to hold larger bonds. This may reduce the number of collapses for which the TPF needs to be called on (e.g. those collapses where the bonding was only marginally insufficient in the past). However, tail risks would still need to be covered by the TPF, which is set at the same level as under Options B and C. As such, from a consumer perspective (who would not care about whether protection is provided by bonding or the TPF), Option D is largely comparable to Options B and C. It is the impacts on scheme efficiency where differences are more marked.

Consumer protection may also improve indirectly to the extent that lower bonding costs for less risky firms can be reflected in lower prices to the end consumer. For riskier businesses, the higher bonding costs may lead to higher prices and customers switching to less risky providers, or else the business itself de-risking its business model in order to reduce bonding costs and maintain existing prices; either way consumer protection should improve.

This option will only be effective if the Commission is able to satisfy itself that firms claiming to make immediate payments to suppliers are actually doing so. Otherwise, the revised basis for setting the bond will be based on a false premise and some firms may post bonds that do not reflect the riskiness of their business model.

Impact on scheme efficiency

Redefining licensable turnover and the corresponding bonding percentages in the way described would reward less risky travel-trade firms and penalise riskier firms. In that way, this scheme may be seen as more equitable, as a riskier business model comes at a higher price in terms of bonding. For many this may be more desirable than the current scheme, or Options A to C, which do not make any adjustments for the riskiness of a particular business. There was discontent among several industry members that, with the existing scheme, any levy would effectively mean they were cross-subsidising risk-taking by others.

[41] Adjustments for trips paid for after the event are not made in this calculation, as by our understanding they are quite a rare and would thus typically constitute a very small proportion of total licensable turnover.

For the typical travel-trade firm, absolute bonding and thus bonding costs should remain unchanged, as they would typically have half the amount of licensable turnover but double the bonding requirement on that turnover. Others may see bonding requirements, and by extension bonding costs, rise or fall.

Travel-trade firms could in theory suffer a loss of competitiveness (e.g. to the direct providers of services, or travel-trade firms licensed outside of Ireland), although (as explained in Option C) we would expect any such impact to be very marginal.

This scheme would impose incremental costs in terms of licensing, although the intention is that these should not be material. As part of their audited licensable turnover projections, travel-trade firms would need to provide audited projections for immediate (airline) payments and trips paid for after the event. Since they are already required to provide an audited overall projection for licensable turnover, these extra submissions should not add materially to the costs of licensing. If firms thought that providing this extra information was unduly burdensome, then they could be allowed the option of posting a bond (at a higher percentage rate than now) on the basis of the existing definition of projected licensable turnover.

This option would impose some extra burden on the Commission when processing licences and monitoring performance. However, there is a clear framework under which bonding requirements are determined for all firms. It is more practical than requiring the Commission to determine bonds on a case-by-case basis with no framework, while still better aligning bonding levels with the riskiness of the business model. It also has the advantage that it is transparent and treats all firms alike.

Overall

Option D would require legislative change. It would restore consumer protection, such that consumer claims could be fully met in the event of two major collapses in one year. Scheme efficiency should improve, with riskier firms penalised through higher bonding costs while less risky firms are rewarded. The administrative costs of implementing this option should be manageable.

Table 4.4: Summary of Option D against key evaluation criteria

Criteria	Assessment
No need for legislative change	✗
Impact on scheme effectiveness	✓✓
Impact on scheme efficiency	✓

4.5 Option E: redefine licensable turnover and prevent travel trade firms trading above projected licensable turnover

Details of reform

Option D can be extended, by preventing firms trading above projected licensable turnover. This would, in the worst-case scenario mean that claims could not exceed 100 per cent of project licensable turnover. As such, a collapse in the ilk of Lowcostholidays should not occur under such a scheme.

As part of this option, we propose industry education in promoting a thorough understanding of licensable turnover, including what is included under licensable turnover and what is not. Travel-trade firms would also be required, when selling package holidays, to issue a certificate to their customer identifying whether or not that package qualified as a licensed travel trade product and thus afforded the customer the protection offered by the scheme. This should make it easier to track a firm's licensable turnover and, should the need arise, administer claims.

If a travel trade firm were to reach their projected licensable turnover (based on a summation of licensable products sold to date), then it would be illegal to carry out trading further in that licensing year. The travel-trade firm can continue to honour existing packages but could not sell any new ones until they have provided a revised projection and increased their bond accordingly.

Under this scenario, bonding requirements would be the same as under Option D, i.e. bonding would be 8 per cent and 20 per cent for travel agents and tour operators respectively applied to a firm's newly defined licensable turnover.

The TPF would need to be restored such that it could have covered the two major collapses in the last ten years, but adjusting for the fact that claims could only have reached 100 per cent of projected licensable turnover in either of these cases. Such a restriction would have meant that had Lowcostholidays collapsed, claims costs could not have exceeded €2million – whereas they actually reached just over €3.3million. Assuming no change in administrative costs, this would have meant that the maximum draw against the TPF could have been €2.2million, rather than €3.5million. In this scenario, therefore, the TPF would need to be replenished to €4.5million (rather than €6million as set out in Options B-D), an increase of €3.2million from its current level.

A €3.2million increase in the TPF would require a temporary one-year levy on travel-trade firms of about 0.25 per cent or €1.50 per passenger. On an ongoing basis, the TPF would need to be topped up by approximately €260,000 (compared with €350,000 under earlier scenarios), which equates to ongoing levies of 0.02 per cent or €0.11 per passenger. The size of the levy would again need to be kept under review by the Commission.

Requirement for legislative change

This scheme would require legislative change to be made for three reasons, i.e.: to levy travel agents; to redefine licensable turnover; and to prevent trading above projected licensable turnover.

Impact on scheme effectiveness

The implication of this change is that the TPF can be lowered while still affording the same degree of consumer protection as in Option B for those consumers that have been issued with a certificate. This assumes that the travel-trade firm acts honestly in issuing these certificates to the consumers who are protected.

As with Option D, the higher bonding requirements for riskier travel-trade firms may reduce the number of collapses for which the TPF needs to be called on. However, tail risks would still need to be covered by the TPF. Of course, there could still be significant calls on the TPF if the travel-trade firm has a very large projected turnover or continues selling packages even after actual licensable turnover has reached the level projected. In the latter case, there should be a real prospect that the Commission will be able to initiate successful legal actions, with firms' directors and auditors on notice that they may be held personally liable if the TPF has to fund claims arising because the firm's actual licensable turnover exceeded what their licence permitted.

We would expect that this scheme would encourage firms to be 'optimistic' in estimating their licensable turnover. Otherwise they face the possible inconvenience of having to provide updated turnover projections and topping up their bond, or even the possibility of having to cease trading temporarily. As such, travel-trade firms would tend to be over-bonded.

As explained in Option D, consumer protection may also improve indirectly to the extent that lower bonding costs for less risky firms (with a low licensable turnover) can be reflected in lower prices to the end consumer. By similar logic, riskier businesses may see consumers substitute away, or look to de-risk their business models to reduce costs and ultimately prices.

A further benefit to consumer protection is that, in the event of collapse, consumers will have much greater clarity on whether or not their package is covered by the scheme – based on whether or not they received a certificate from their travel agent or tour operator stating such. This may speed up the time taken to process, administer and ultimately pay-out on claims.

Impact on scheme efficiency

The impacts on scheme efficiency outlined in Option D would also apply in the case of this option.

Option E goes a stage further by ensuring individual travel-trade firms have sufficient bonding requirements given actual (rather than projected) turnover. By doing so, it also reduces the burden on collective levies to build up the TPF.

However, it may be contested that this option penalises businesses that perform better than expected during the year, in terms of the costs imposed by a period of ceased trading, as well as the costs of producing a newly audited projected licensable turnover and the corresponding bond increase. The onus would be on the travel agent or tour operator to decide what was the most viable course of action:

- Take a more pessimistic view of projected licensable turnover and, as a result, secure a lower bonding requirement and a lower bonding cost. However, the firm then runs the risk that this projected licensable turnover may be reached during the course of the year and thus impose the additional costs of ceased trading, providing newly audited projected licensable turnover figures and increasing bonding.
- Take a more optimistic view of projected licensable turnover, at the expense of a higher bonding requirement and bonding cost, but with diminished risk of having to cease trading during the course of the year. For a typical travel agent with expected turnover of €2,500,000, a 20 per cent 'buffer' on top of expected licensable turnover would only cost around €600 to €800 more for a typical travel agent (and €1,500 to €2,000 more for a typical tour operator). As shown in Chapter 3, many travel-trade firms may not need to adjust their approach to making projections as they are tending to be over-bonded.

Overall

The rationale for this option is that it starts to put limits on just how large the claims an individual collapse can give rise to. As a consequence the need to replenish the TPF or increase bonding rates is reduced, while still offering comparable levels of consumer protection as in Options B-D. While this option may be seen to penalise businesses outperforming expectations, it should incentivise better forecasting and more forward planning, such that trading is ceased only in exceptional circumstances.

Table 4.5: Summary of Option E against key evaluation criteria

Criteria	Assessment
No need for legislative change	✗
Impact on scheme effectiveness	✓✓
Impact on scheme efficiency	✓

4.6 Summary of proposed options

The table below summarises the five options in terms of the three main criteria set out at the start of this section, as well as in terms of the changes to bonding requirements, PLTO definition and one-off and on-going levies to replenish the TPF.

Table 4.6: Summary of proposed options for reform

Item	Option A	Option B	Option C	Option D	Option E
TA bonding	200%	4%	4%	8%	8%
TO bonding	100%	10%	10%	20%	20%
PLTO definition[42]	No change	No change	No change	Excludes payments passed onto supplier immediately and bills paid in arrears	Excludes payments passed onto supplier immediately and bills paid in arrears
One-off levy	No	2.5%, TO only	0.35%, TA and TO	0.35%, TA and TO	0.25%, TA and TO
On-going levy[43]	No	0.2%, TO only	0.03%, TA and TO	0.03%, TA and TO	0.02%, TA and TO
Other	-	-	-	-	Firms cannot exceed PLTO. Firms must identify at point of sale to consumer whether eligible to claim.
No legislative change required	✓	✓	✗	✗	✗
Impact on effectiveness	✓✓✓	✓✓	✓✓	✓✓	✓✓
Impact on efficiency	✗✗	✗	~	✓	✓

Our preferred option is **Option E**. This would require legislative change, but would help restore a sufficient level of consumer protection and reduce the potential scale of tail risks. The scheme would be more equitable by tailoring individual bonding to a business' riskiness (while not materially increasing administration costs) and by funding the collective TPF through an equal (small) levy across all travel-trade firms.

42 As mentioned earlier, the options that propose changes to the definition of PLTO might be refined by the Commission, either adding extra criteria or excluding one of the factors suggested.

43 As explained earlier, any ongoing levy would need to be kept under review by the Commission taking into account the size of the fund and the more recent history of collapses.

Annex

Past assessment of options for reform

Alternatives to the current regime have implications for who bears the costs of ensuring financial protection is in place for consumers travelling out of Ireland. In 2008, the Commission consulted on options such as:

- ending the bonding requirement and just relying on the TPF;
- requiring travel trade firms to have escrow accounts;
- assessing bonding requirements on a case-by-case basis;
- assessing bonding requirements with regard to the change in licensable turnover in the last year, rather than relying on firms to provide projections of licensable turnover; or
- redefining licensable turnover.

The Commission's recommendation was to allow for the possibility of switching to a collective insurance scheme, ending the requirement for all tour operators and travel agents to have separate bonds in place. This recommendation was made at a time when the Irish financial sector was de-risking and travel-trade firms were finding it increasingly difficult to secure bonds. The Commission wanted to explore whether it would be possible to secure a cost saving by switching to a collective scheme. Drawbacks with such a change were acknowledged, including the fact that it would represent risk pooling, so there might be less incentive for individual firms to reduce their risks. The recommendation was limited to seeking a change in the legislation so that such a collective scheme was permissible; had such a change been made, the Commission would then have worked with insurers to develop a detailed, fully-costed option.

The situation today is different. The problems with getting a bond are not as acute as they were during the height of the financial crisis. But in considering reforms to the current travel-trade regime, the basic trade-offs will remain between options that attempt to pool the costs across the industry and/or taxpayer, and those that attempt to make individual firms bear costs commensurate with the risk that it will be their consumers making claims for refunds or repatriation. The former options may be simpler to administer and therefore may impose a lower overall regulatory burden, but may have less desirable incentive properties. The latter options have the challenge of identifying what is material in determining the risks posed by different travel trade business models, making sure that the regime is manageable and does not impose excessive information requirements on firms or the Commission, and cannot easily be gamed (the current system, where bonds depend on projected licensable turnover, will only work as intended for as long as projections are reasonable estimates of future turnover).

Possible reforms of the current scheme

Based on our discussion with industry and our analysis of past collapses, as presented in Chapter 3, there are a number of possible reforms.

Options for reforming the bonding scheme

Reforms to the current bonding scheme that could be considered include:

- the percentage bonding requirements (with and without the TPF);
- the relative bonding requirements for travel agents and tour operators;
- the choice of metric on which bonding requirements are based;
- the assessment of bonding requirements on a case-by-case (i.e. risk-adjusted) basis; and
- the variation of bonding requirements through the year to reflect seasonality of cash flow/turnover.

Industry discussions on changes to the current bonding requirements were mixed, with some concerned that bonding costs are already too high, while others said that current percentages were too low such that there are times when they are under bonded from a cashflow perspective. In spite of this latter point, there is little appetite among industry for seasonal bonding, with some firms exhibiting very limited seasonal variation given the way the industry has evolved over time and others concerned about the unpredictability of any seasonality. As such, it seems likely that any seasonal bonding scheme could not be imposed on a one-size-fits-all basis and would essentially end up looking more like a case-by-case, risk-adjusted scheme.

Concerns were not raised about the relative bonding requirements of travel agents and tour operators, consistent with our analysis in Chapter 3 which found average claims, as a percentage of licensable turnover, to be higher for tour operators than travel agents (i.e. consistent with the current bonding requirements).

This analysis also showed that while the current percentage bonding requirements may be sufficient for most collapses, there are cases where it is not. This may be because the collapse happens at a time of year when the travel trade firm has greater exposure, and/or because the firm's turnover has deviated significantly from that projected. The latter point is linked to concerns about the limitations of licensable turnover as a proxy for expected claims in the event of collapse, insofar as it does not reflect the underlying risk of the business. As a result, some called for bonding requirements to be based on individual company assessments, such that bonding levels more accurately reflect the true costs of the business (stressing that certain factors, e.g. immediate payments to suppliers following the booking, meant that their business is inherently lower risk).

Overall, therefore, given the above industry feedback, our proposed options for reform set out a refined list of options on bonding which seek to address the following two key concerns:

- How, despite being appropriate for the average travel agent or tour operator, percentage bonding requirements would need to be adjusted to cover tail risks, especially given the inadequacy of today's TPF?
- How the metric on which bonding requirements are based may be adjusted such that the level of bonding more accurately reflects underlying risks?

Options for reforming the TPF

Changes to the TPF that can be considered are:

- the appropriate level of the TPF (with and without a bonding scheme in place);
- the levy required to return the TPF to this level;
- the length of time for which this levy should be in place; and
- the relative burden of any levy across tour operators and travel agents.

Our analysis in Chapter 3 has shown that in the case of certain collapses, the TPF has been fundamental to ensuring consumer protection and that in its absence the bonding alone may have only been capable of fully refunding 2 per cent of claimants (or, for all claimants, only 2 per cent of their original holiday cost). This demonstrates that with an unreformed system of bonding, the TPF has a crucial role to play and, therefore, the sustainability of its current level must be addressed as soon as possible.

There were generally negative views amongst industry regarding the reintroduction of a levy to replenish the TPF. Given the collective nature of the TPF, many firms are reluctant to pay additional levies to build up the TPF, as it effectively constituted a cross-subsidisation of riskier businesses. The introduction of a levy at the point of departure is frequently seen by industry as a more equitable solution for achieving effective consumer protection, although consideration of such a scheme is beyond the scope of this paper.

While there is reluctance amongst many that travel trade firms should pay into a collective pot for consumer protection, if such a levy were introduced there were no strong arguments made for why it should be paid by tour operators alone (as was the case when the levy was originally used in the 1980s). Many indeed emphasised the point that the traditional differences between travel agents and tour operators had become increasingly blurred, and thus the rationale for only levying tour operators was no longer justified.

Reforms that entail changes to the TPF require consideration of the following key issues:

- the optimal combination of bonding and TPF;
- an appropriate balance between individual and joint liability (and implications for burdens and incentives); and
- the optimal combination in the short-run (to replenish the TPF) and long-run (once TPF is replenished).

Taking our analysis and industry views, one of our proposed reforms seeks to answer the question of how the TPF could be replenished to a sufficient level in the absence of any change in the bonding requirements, using a levy across all licensed travel trade firms.

Other options for reform

In addition to reforms of the bonding scheme or TPF set out above, there are other possibilities for reform:

- A short-term government guarantee or loan to the TPF (until the TPF is restored).
- A requirement to have escrow (third-party) accounts.
- A revision of reporting, monitoring and enforcement (e.g. to reduce the possibility of fraud).
- A collective insurance scheme.

Our analysis in Chapter 3 has shown that the current scheme is ineffective and that, if another significant collapse were to arise, the current bonding and TPF arrangements may not be able to provide full consumer protection. Only in the presence of a short-term injection to the TPF could full consumer protection be ensured. However, it is our understanding that such a scenario is not favoured, but instead the focus should be on restoring the effectiveness of the scheme in as short a timeframe as practicably possible (e.g. by replenishing the TPF).

There was no call amongst industry for the establishment of escrow (third-party) accounts. Nor do we think that they would address all of the limitations of the scheme identified in Chapter 3.

Industry often spoke of the need to tackle fraudulent behaviour and risky 'cowboy' businesses. This is in part because more stable travel trade firms believe the reintroduction of any collective scheme would penalise their low risk business models, insofar as they are effectively cross-subsidising more risky business strategies adopted by other businesses. While this is not a reform which could in isolation restore the scheme's effectiveness in providing consumer protection, it is nevertheless a reform that should make other refinements to the scheme both more effective and more palatable to industry.

The TPF itself is a collective pot of money that is drawn upon when the individual company bond is insufficient to cover claims. However, given the unpredictability of large claims against the TPF, even once the TPF has been replenished to a suitable level through a levy, it may be that subsequent collapses render the TPF insufficient once more, invoking further levies and so forth. An alternative to this may be a collective annual insurance scheme, with each travel trade firm paying fees to contribute towards the insurance premiums. We have not developed this as a separate option in chapter 4: in the long-run, such an arrangement is likely to generate similar costs to the industry as collecting levies to top-up the TPF.