Europe Economics

Bonding of the Irish travel trade industry
Final Report

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1 Introduction

The Commission tasked Europe Economics 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?

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 firm posted when getting a licence. The size of the bond is 4 and 10 per cent of projected licensable turnover (PLTO) for travel agents and tour operators respectively. Should the bond be insufficient to fund all claims, the Travellers' Protection Fund (TPF) is used to fund the remainder. The TPF was originally funded by a levy on tour operators, but since 1987 there has been no levy on the basis that the Fund was always deemed to be sufficient to provide financial protection to customers.

1.1 Interim Report

In our Interim Report we found that the current travel trade scheme is not effective in providing full financial protection to customers of licensed and bonded travel agents and tour operators.[1] The levels of bonding plus the TPF would be insufficient to ensure such customers are fully protected in the event of a future, large collapse. The collapse of Lowcostholidays.ie in summer 2016 depleted most of the remaining money in the TPF.

We identified a number of possible changes to the scheme which might restore the effectiveness of the scheme in providing consumer protection in the event of travel trade firms collapsing, and provided a more detailed assessment of five reform options (see Table 1.1). The options for reform were motivated by the need to fully protect consumers in the event of atypical, large collapses – the existing scheme was already sufficient for dealing with most travel trade firm collapses. We assessed each option 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)

[1] Europe Economics (2017) "Bonding of the Irish Travel Trade Industry. Interim Report" Available online at [accessed on 16 November 2017] https://www.aviationreg.ie/_fileupload/Travel%20trade/TTConsumerProtectionMeasuresReport.pdf

The table below, reproduced from the Interim Report, summarises the five options in terms of the three main criteria. It also summarises the changes to bonding requirements, the definition of PLTO and one-off and on-going levies to replenish the TPF.

Table 1.1: Summary of options for reform proposed in Interim Report

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[2]	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[3]	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 was **Option E**, although we noted it would require legislative change. Its attractions were that it would help restore a sufficient level of consumer protection and reduce the potential scale of tail risks. It also seemed to be more equitable than some of the other options: it tailored individual bonding to a business' riskiness (while not materially increasing administration costs) and proposed funding the collective TPF through an equal (small) levy across all travel-trade firms rather than just tour operators.

In arriving at our findings, we assessed the evidence from:

- Analysing industry data, including data on industry trends and past collapses;
- interviews with a number of key stakeholders, including travel-trade firms, trade bodies and government;
- analysing the national schemes in place in five other countries in Europe.

2 We noted that the Commission might refine the options proposing changes to the definition of PLTO, either adding extra criteria or excluding one of the factors suggested.

3 We suggested that the Commission would need to continually review the level of any ongoing levy, ensuring that it remained appropriate given the size of the fund and the more recent history of collapses.

1.2 Subsequent developments

In August 2017 the Commission published our Interim Report along with Commission Paper CP8/2017.[4] In preparing this report, we have had regard to the responses to that consultation paper.

There have not been any other material developments since we published our Interim Report that have prompted us to revisit our thinking.

The remainder of this report addresses the points made by parties to CP8/2017, and sets out our final conclusions.

[4] Commission for Aviation Regulation (2017) "Consultation. Travel trade consumer protection measures" Available online at [accessed on 17 November 2017] https://www.aviationreg.ie/_fileupload/Travel%20trade/CP8%20Travel%20Trade%20Consumer%20Protection%20Measures.pdf

2 Responses to consultation

This chapter summarises the findings of the Commission for Aviation Regulation's consultation with industry on possible reforms to the travel trade licensing and bonding regime. There were a total of 42 responses to this consultation, predominantly from travel agents.

The consultation paper asked for stakeholder views in six key areas:

- Other material market developments relevant to assessing the effectiveness and efficiency of the scheme.
- The effectiveness of the current scheme in protecting consumers.
- The efficiency of the current scheme for the level of consumer protection it provides.
- The criteria for establishing what constitutes an effective scheme.
- Other reforms that should be considered in ensuring full consumer financial protection.
- Preference amongst proposed reforms set out in the consultation paper.

In this way the consultation was limited to reforms of the existing scheme, rather than possible changes to the scope of the scheme. However, the consultation attracted many responses about the suitability of the scope of the current scheme, which we summarise and respond to first, before addressing the feedback to the specific consultation questions.

2.1 Responses on scope of the current scheme

Consultation findings

The main themes to emerge from the consultation paper were dissatisfaction with the current regulations governing travel-trade licensing and bonding and a view that the consultation's scope was too restricted. Parties queried the rationale for inviting suggestions on reforms to the existing scheme when in their view the existing scheme was no longer fit for purpose.

The overwhelming majority of respondents to the consultation were travel agents, tour operators or trade bodies that represent them. Many queried why they alone had to be bonded and licensed, given the changes in the industry since the scheme was developed over 40 years ago. Many pointed out that nowadays the majority of travel purchased was not protected by the bonding scheme. There were suggestions that policy makers needed to think holistically about what they were trying to achieve with consumer protection for travel, and develop a scheme accordingly; focussing just on the minority of travellers who book through tour operators or travel agents made no sense. It was a mistake to persist with a financial protection scheme that relied on historic concepts of travel agent and tour operator given developments in the industry.

That so many travel customers choose not to buy from travel agents or tour operators was seen as evidence that they did not value the financial protection provided by the scheme. There were some calls for informing the public of the benefits of the scheme, so that they saw the value of booking via a bonded firm.

However a number of other respondents suggested that the appropriate action was instead to cease requiring travel agents and tour operators to be bonded and licensed. Instead, customers should contribute towards their own financial protection, which would have the attraction of being transparent with customers realising directly how much it costs to insure against the collapse of the party selling a travel product. Some parties suggested levying an insurance premium on all parties travelling so that they had coverage, which would widen the scope of which travellers are protected relative to the current scheme. Others instead thought customers should be free to choose whether they wanted to purchase such protection. In both cases, one rationale offered was that it would level the playing field between travel agents and tour operators and firms selling travel products not subject to bonding and licensing requirements.

Many respondents thought the scheme should be extended to include airlines and bedbanks, with a number referring to the recent collapse of Monarch to support their case. Parties wondered why the Commission was consulting on changes to a scheme that only dealt with customers of travel agents and tour operators when the collapse of a bed bank or airline could affect many more customers. It was also claimed that traditional travel agents posed less risk to customers than the newer business models that were increasing their market share, such as the bed banks.

A related comment was that the solution to topping up the TPF was a levy on all travellers leaving Ireland, rather than just confining it to tour operators, or tour operators and travel agents. The wider scope would mean that a smaller levy per passenger would be possible (suggestions for the level required varied between EUR 0.5 and EUR 2), while still generating the funds needed to ensure the TPF was adequate. There were some favourable references made to the UK Civil Aviation Authority's ATOL scheme, which it was claimed was based on realistic definitions and provided adequate consumer protection.

Another common criticism of the consultation paper concerned the timing, given the second Package Travel Directive (PTD2) would require changes to the current Irish travel trade licensing regime. Parties queried why the Commission would countenance potentially significant changes to the existing scheme in isolation, given new legislation was due in the near future that would have implications for the scheme. Instead, a long overdue assessment of the overall approach to protecting customers should be undertaken. Concerns were expressed that if reforms of the existing scheme were conducted in isolation, travel agents in Ireland may incur costs having to comply with the Irish regime and separately with requirements arising under PTD2.

Our response

We are generally sympathetic to these criticisms parties have made. The current travel trade protection scheme clearly does not provide protection to all travellers given that over 80% of travel is not booked via a travel agent or tour operator. However, it does provide protection to a subset of consumers who choose to book their travel using a travel agent or tour operator rather than booking individual components directly themselves.

We also agree that efforts should be made to minimise the disruption associated with temporary reforms to the existing scheme to make it effective, given further reforms may soon follow as Ireland introduces legislation to comply with PTD2.

But accepting these criticisms are valid does not address the Commission's immediate problem, which is that it has to administer the existing scheme and the finding in our Interim report remains: the current scheme can no longer be viewed as effective since the current bonding levels and funds in the TPF are inadequate to cater for all the valid claims that might arise following another large collapse by a licensed travel trade company. Even efforts to make the existing scheme effective (ignoring debates about its scope or the effects of PTD2) will benefit from some legislative changes that the Commission may or may not be able to secure. It is the Commission's intention to carry out, in addition, a review of the findings against the requirements of the Package Travel Directive.

2.2 Responses to consultation questions

Here we discuss the key consultation findings for each of the consultation questions, and set out our response.

2.2.1 Q1 – Other material market developments

Consultation respondents were asked the following:

"Are there material developments in the market that have been ignored that are relevant when thinking about the effectiveness and efficiency of the current travel trade protection scheme?"

Consultation findings

Consultation responses suggest no material market developments were omitted from consideration in assessing the effectiveness and efficiency of the current scheme. (As previously noted, some parties thought that the work should have had regard to PTD2.)

Several respondents reiterated how significantly the industry has changed since the scheme was introduced in 1982. In particular, respondents stressed how a large proportion (circa 80 per cent) of travel booked by Irish consumers today is not through a travel agent or tour operator and, therefore, not protected. One respondent attributes this to the influence of the Internet, Google and Smart Phones on the way consumers research and book travel packages. As a result, a number of respondents stress the increasing number of organisations (e.g. airlines) falling outside the legislation, which operate in comparable ways to travel agents and/or tour operators but are not required to comply with the travel trade licensing and bonding regime.

Another common theme raised by respondents is the lack of consumer awareness, and even concern, as to whether or not they are protected when booking a travel package. One respondent's perception of this was confirmed by a 'show of hands' survey they conducted to understand whether the audience knew what it meant to for a travel firm to be licensed and bonded.

Other issues raised are:

- One respondent confirmed the finding presented in the Interim Report that customers now typically pay later for their travel packages, while payments are forwarded to suppliers (especially airlines) much earlier. They also stated that payments by credit card had become more common.
- One respondent stressed that it is a low margin industry, with typical net returns of around 1-2 per cent.
- One respondent explained how the old model of airlines paying agents significant commissions is no longer how the industry operates.

Our response

Based on the above evidence, there are no material market developments omitted from the Interim Report that we think require us to reassess the effectiveness and efficiency of the current scheme.

2.2.2 Q2 – Effectiveness of the current scheme

Consultation respondents were asked the following:

Do you agree with the finding that the current scheme is not effective in protecting consumers?

Consultation findings

The majority of respondents agreed that the current scheme is not effective. That said, one respondent noted that the current scheme has performed well to date, with the exceptions of Failte Travel and Low Cost Holidays. However, another stakeholder noted that moving forward the scheme can only be "considered adequate for attritional claims", but not sufficient to cope with a catastrophic loss against the TPF.

Many respondents were of the view that the scheme is no longer effective because it no longer covers the vast majority of travel bookings made. This relates to the scope of the current scheme, which is beyond the remit of this particular study, but nevertheless has been discussed earlier in Section 2.1.

Our response

The responses are consistent with our findings in the Interim Report that the current scheme is not effective. Some intervention is necessary (obviously many parties favour an intervention that is wider in scope).

2.2.3 Q3 – Efficiency of the current scheme

Consultation respondents were asked the following:

Do you agree with the finding that the scope to reduce the costs of the current scheme while maintaining the current level of consumer protection is limited?

Consultation findings

Few consultation respondents made specific remarks in relation to this question, with most respondents instead focusing on the effectiveness of the current scheme and possible options for reform.

Often efficiency concerns were raised again in relation to broader concerns about the scope of the current scheme. One respondent said that the current scope of the scheme is anticompetitive, insofar as smaller companies are required to meet licensing and bonding requirements, while larger companies who are not travel agents or tour operators but sell individual travel products (especially airlines) were not required to do. Another respondent said that by expanding the scope of the current scheme, this would open up new possibilities that could have the potential to reduce costs. It was suggested, for example, that if the scope of the scheme was broadened then it would become more cost effective to provide traveller protection through a per passenger levy. Reference was made to cost savings businesses realised in the UK following the migration from ATOL bonding to ATOL Protection Contribution.

Very few specific comments were made in relation to the efficiency of the scheme given its current scope. One respondent claimed there was some potential for cost reduction while maintaining the current level of consumer protection, due to the fact that money collected by travel agents on behalf of tour operators currently results in a "duplication of bonding". In such cases the consumer's contract is directly with the tour operator. Hence, removing the bonding requirement on travel agents for this turnover would reduce the bonding costs to travel agents, while not jeopardising the level of protection afforded to consumers.

Our response

The fact that very few specific concerns were raised by industry about the efficiency of the current scheme, beyond complaints relating to its scope, is consistent with the Interim Report finding that there are no material efficiency concerns with the current scheme. The need for change (within the current scope of the scheme) is driven by the ineffectiveness rather than inefficiency of the current scheme, although any proposed reforms need to carefully consider the implications for efficiency.

The options for reforming the current scheme, discussed later in this report, include some that would re-define what constitutes licensable turnover. We recommend such a reform, and think that is the best way to deal with possible instances of duplication of bonding.

2.2.4 Q4 – Criteria for determining scheme effectiveness

Consultation respondents were asked the following:

Do you agree that to be effective, the scheme needs to be designed with sufficient contingency to be able to meet all claims in full in the event that there are two collapses in a single year that give rise to the same level of claims as the two largest collapses in the history of the scheme? If not, what criteria would you propose?

Consultation findings

Those parties that responded to this question did not agree with the proposed criteria. Some respondents highlighted the fact that average claims following collapses were much less than those associated with the collapse of Lowcostholidays and Failte Travel, and thought that the average rather than extreme events, should guide the thinking. Some thought that building in a contingency for extreme events was unfair and punished properly operated and compliant travel trade firms.

One contrary view was that although the experience in 2016 was unprecedented, the Commission, in addition to planning for claims of the same magnitude, should also factor in the potential for other additional losses.

Some comments suggested that the solution lay with improving the approach to financial fitness tests. If the criteria to get a licence were more stringent and the bonding was correct for all parties, a large TPF would not be needed. It was also suggested that the possibility of another large collapse like Lowcostholidays should be disregarded as lessons should have been learnt from that experience.

One suggestion was that the Commission should not seek to engage in worst-case planning, but instead should rely on bank borrowing or government support should the TPF be exhausted. In a similar vein, other parties suggested that the Commission should take our insurance or secure a line of bank credit rather than seeking to have funds in place in advance to cover worst-case scenarios.

One party argued that the arrangements for the TPF should be such that it would have the capacity to manage claims over a time period of 10 to 20 years, covering the normal economic cycle and geopolitical crises that may affect the industry. However, the party thought that when thinking about two major failures, the focus should be on understanding the individual firm's risk profile and ensuring it had adequate primary security in place, i.e. a suitable bond, and is closely monitored. The TPF should not act as a reserve fund to compensate companies managing risks poorly.

Our response

We think that the criteria we proposed for ensuring that the scheme remains effective are reasonable. We do not think the Commission will be able to rule out the possibility of future large collapses (although it clearly should take feasible actions to reduce the risks of collapses). Therefore, it would be remiss to plan on the basis that in the future all collapses will generate average levels of claims. But that does not mean that we think that such contingency planning removes the desirability of taking measures to avoid claims against the TPF arising, such as monitoring firms closely and seeking to ensure that bonding levels reflect the claims likely to arise should a given firm collapse.

As we discuss below, we think that there is merit in some of the alternatives to collecting a significant levy to top-up the TPF, such as an insurance policy.

2.2.5 Q5 – Other reforms to ensure full consumer protection

Consultation respondents were asked the following:

Are there other reforms that you think should have been considered? How would these reforms ensure that all consumers protected enjoy full financial protection?

Consultation findings

As discussed in section 1.1, most of the alternative reforms suggested went beyond the scope of our study and wanted fundamental changes to the travel trade licensing and bonding regime.

A number of responses argued for better policing of bonded companies, with a quite a few parties wondering how the Lowcostholidays collapse could have generated such large claims if the firm was being properly monitored. There was a hope that lessons would be learned such that a similar collapse does not happen in the future. The Commission was encouraged to identify companies most at risk of making a major hit on the TPF and impose regulations on them to pre-empt such an outcome. Characteristics that the Commission might look out for were companies registered overseas or corporately linked with airlines or bed banks. There were even suggestions that introducing a travel levy would allow the Commission to boost its staff numbers and ensure licences are well monitored. The Commission was also encouraged to use all legislative tools to pursue and penalise individuals and auditors who breach existing legislation, to deter others from being under bonded.

There was support for more tailored monitoring of the bonding needs for travel agents and tour operators, with a number of different models suggested. For example, one party suggested that the current bonding levels of 4% and 10% were an appropriate starting point but the Commission should raise the bonding levels for companies deemed as more risky according to set criteria. Another party referred to the approach of IATA, and encouraged the Commission to grade companies as high, medium or low risk and set bonding requirements accordingly. More generally, a number of parties encouraged the Commission to evaluate better the different business models and not apply a one size fits all approach to licensing and bonding. In doing so, the Commission was encouraged to avoid imposing additional reporting requirements on larger agencies that will not fail and instead focus on the actual risk and taking action there. In contrast, another respondent argued that all firms with turnover over EUR 10m should have to submit an audited statement or abbreviated audited management accounts to allow the Commission to take an informed view on its financial viability.

In setting the level of bonds, some parties suggested alternatives to projected licensable turnover. Given the difficulty in generating an accurate forecast, one party suggested using actual turnover (possibly a mark-up). Another party suggested focusing more on retained earnings, its bank position and cash flow, as this would be a better guide to how prudent a company was as it incorporated future planning (and moreover, turnover does not determine profitability).

One respondent suggested a tiered approach to setting bonding levels for travel agents, with bonding levels rising from 2% of projected licensable turnover for companies projecting less than EUR 2m, rising to 6% for turnover above EUR 6m. Responses also raised the possibility of redefining turnover when setting the bonding level, e.g. excluding turnover related to visas, passport applications, insurance and boarding-pass fees.

To provide coverage where the bond was inadequate, a number of parties advocated options that did not require immediate action to top-up the current TPF via a levy. Some suggested introducing a levy that could be used to purchase insurance and gradually top-up the TPF. Others suggested that the Commission should look into using the current funds in the TPF to purchase insurance or secure a line of bank credit to cover against the possibility of future collapses generating claims in excess of the company's bond. Another option put forward was to not take any immediate action to top-up the TPF, but instead introduce a levy only after the TPF has been exhausted, borrowing from the government or banks to make good a temporary shortfall.

Where parties discussed the possibility of re-introducing a levy, they tended to favour collecting it from all passengers rather than just from tour operators, or just from tour operators and travel agents. Reasons offered for this included fairness, minimising the burden on already stretched travel agents and tour operators, and as a way of increasing the visibility of the scheme by making everyone pay a nominal fee for bonding their travel.

There was some support for Ireland adopting the approach used in the UK, where a fee per passenger booked is applied as opposed to requiring the licensee to pay a considerable premium to an insurance company to fulfil bonding requirements. Such a scheme was considered effective, transparent and linked to actual travel, in contrast to the current approach in Ireland that depends on forecast licensable turnover.

Our response

We think that the option of purchasing insurance, rather than seeking to top up the TPF via a one-off levy, has merit. As a long-run measure, we would suggest funding the premium payments from a levy on the industry and use any funds in the TPF as a first tranche for paying out collapses (thereby allowing for a smaller insurance premium in the early years). We would suggest that the levy used to fund the premium should be raised from all firms that are covered by the scheme, as opposed to the current situation where the Commission could only levy tour operators. As a stop-gap measure, the possibility of purchasing insurance using funds in the TPF or relying on the government to act as an insurer of last resort if the TPF is exhausted should be explored.

The ability of the Commission to undertake risk assessments and monitor companies will never be perfect. While we think that the Commission should seek to learn lessons from past collapses (and also continually seek to learn from the approach used by other regulators and from regular communication with the industry), we do not think a commitment to do a better job of monitoring firms would suffice in making the current scheme effective. All of the travel-trade schemes we reviewed have experienced large collapses, and we think it would be naïve to think the Commission could develop a perfect monitoring system.

For similar reasons, we think that a commitment to pursue firms and, if appropriate, their auditors, that trade with an inadequate bond in place is laudable but in isolation will not ensure that travel-trade protection scheme is effective.

As indicated in our initial paper, we see merit in redefining projected licensable turnover for the purposes of setting bonds. That might even extend to allowing firms to base future projections on past turnover plus a mark-up, although this would not work for new entrants. We continue to favour approaches that determine bonding levels using objective criteria advertised to all parties. It has the advantage of being more transparent and, arguably, fairer to all firms seeking a licence, and by being simpler it should be administratively more efficient. But there needs to be flexibility over time to weak the criteria, to avoid the possibility that over time the bonding levels calculated bear no relationship to the underlying risks different business pose in terms of possible claims that may arise should they collapse.

2.2.6 Q6 – Preference amongst proposed options for reform

Consultation respondents were asked the following:

Which of the reforms do you think the Commission should pursue, if we conclude that the current scheme needs changing? Why?

Consultation findings

As previously noted, many respondents queried the scope of the review. Consequently, the general sentiment towards the options included in the consultation paper was unfavourable. Parties saw them as further distorting the already unlevel paying field facing travel agents and tour operators. It was also seen as unfair to penalise the sector because of Lowcostholidays.

The options to increase bonding levels or to re-introduce a levy on tour operators, options that are available to the Commission without any further legislation, were seen as non-starters, likely to cause firms to exit the industry. One travel agent noted that levying tour operators only to top up the TPF would suit their business, but would probably not be acceptable to tour operators.

Options that required introducing a levy met with opposition, absent a wider reform of the scheme, as such levies would further distort the market. Licence holders would be at a competitive disadvantage, and consumers would switch to unbonded sellers.

However, some parties viewed the option of no change in bonding levels, combined with a levy on both tour operators and travel agents (option C) as relatively more palatable than other options. One suggested tweaking the levy contributions so lower risk or smaller travel agents and tour operators paid less (possibly even nothing) while higher risk and larger companies paid a higher levy. Another party supportive of option C suggested tweaking the bonding requirements, so higher risk firms posted bonds greater than 4% or 10% of projected licensable turnover.

Many respondents opposed options that would require higher bonds. There were suggestions that some firms may struggle to secure larger bonds or find the costs associated with higher bonding levels made the business unsustainable. It was argued that such a measure would penalise smaller companies. There was also reference made to the fact that companies are now holding onto customers' money for shorter periods, which seemed at odds with increasing the bonding requirements.

A number of parties supported the idea of changing the definition of licensable turnover to reflect changes in how business is conducted. In addition to airline bookings paid at the time of the booking and corporate travel, there was also a suggestion that tour operator packages that are already bonded should be excluded from the definition of licensable turnover used to calculate travel agents' bonding levels.

While there was some support for re-defining licensable turnover, the logic of increasing the percentage of (redefined) licensable turnover used to determine bond levels was queried. There were a variety of arguments put forward:

- removing turnover that posed no risk from the definition of licensable turnover left the risk unchanged, and therefore the 4% and 10% remained appropriate;
- it would create winners and losers, with those firms whose licensable turnover would be little changed by the new definition having to post bigger bonds if the bonding percentages were changed;
- the proposed doubling of the bonding percentages was based on the erroneous assumption that about half of current licensable turnover would be exempt under the proposed new definition, whereas it might only result in a 30% reduction in projected licensable turnover;
- travel agents were already overbonded with average claims amounting to 3% of projected licensable turnover; and
- doubling the bonding requirement would send a negative message to insurance companies and banks, and affect these institutions willingness to provide bonds, which would adversely affect many travel agents who may not currently have the liquidity levels in place to post a cash bond.

Our Response

We agree that the options available to the Commission absent any change in the legislation are unattractive. Re-introducing a sizeable levy that is limited to tour operators would be difficult to justify, and may well prompt tour operators to exit the industry or rearrange their business model to avoid paying the levy. The one justification the Commission would have to levy just tour operators is that it may be a marginally better policy to the massive increases in bonding levels that would be necessary to ensure the scheme remained effective in dealing with all collapses, including large ones, absent any measure to address the depleted level of funds in the TPF.

We continue to think that Option E (redefining licensable turnover, prohibiting actual turnover from exceeding projected licensable turnover, and levying tour operators and travel agents) is the best of the five options we outlined. This would require legislative changes. Based on the feedback received, we would propose some refinements to this option.

First we think that purchasing insurance, rather than trying to top up the TPF, may be a better way to ensure that there are sufficient funds to deal with the possibility of another large collapse. That avoids asking industry to make a large, one-off contribution to re-build the TPF and instead would entail a levy (cost) on the industry that was more predictable and stable. While the legislation was being put in place to allow the Commission to impose a levy on travel agents and tour operators, the stop-gap measures some parties suggested, such as using the TPF to purchase insurance coverage or securing a government guarantee or a banking line of credit, would have merit. However, we recognise that some of these stop-gap measures themselves may require legislative actions.

We think a change in the definition of projected licensable turnover should be accompanied by a change in the percentages used to estimate the level of bonds, but would suggest conducting further empirical work to determine what the revised percentages should be. While conducting this work, thought might also be given to whether other changes to licensable turnover are warranted, such as excluding tour-operator packages from travel agent's licensable turnover. However, we would caution against making too many changes to how licensable turnover is defined immediately, and instead advocate a more incremental approach to refining the definition to make sure the effects are well understood (this advice assumes that in the future the Commission will have the discretion to make changes to how bonds are set without requiring further legislative changes).

We reject the argument that changing the definition of licensable turnover to exclude turnover that posed no risk requires no change in the bonding percentage. If EUR 4,000 is an appropriate bond for the "typical" travel agent with projected licensable turnover of EUR 100,000, then the appropriate bond remains EUR 4,000 if that travel agent's business model is unchanged. Hence, if there are proposals to change the definition of licensable turnover, and those changes would result in projected licensable turnover of EUR 50,000, then bonds should be set at 8% of projected licensable turnover to ensure an appropriate bond of EUR 4,000 remains in place. As a first approximation, the change in projected licensable turnover should not result in a change in the total level of bonds in place.

There will be distributional consequences, with some firms having to post larger bonds and other firms smaller bonds. We do not view that as a flaw, but rather part of the design to align better bonding costs with the relative risks different business models pose of giving rise to large claims. It is possible that this may prompt some firms with riskier business models to restructure their affairs to qualify for a lower bond. That would be a welcome development from the viewpoint of ensuring that the scheme remains effective. If significant numbers of firms re-arrange their business model to secure lower bonding requirements, then the total level of bonds may fall. This should not be a concern, provided the Commission is satisfied that firms are not engaging in regulatory gaming and arranging their affairs to qualify for a lower bonding requirement without actually reducing the likely level of claims that would arise should they collapse.

Prohibiting companies from trading if actual licensable turnover exceeds the projected licensable turnover on which their bond is based should help cap the costs of future claims from single collapses. It also arguably addresses calls from some in the industry for better monitoring, to ensure that the bonds in place align with the actual business of the firm.

3 Conclusions

Our conclusions on the specific questions we were asked to address are broadly in line with the conclusions we set out in our Interim Report. We have assessed the responses to CP8/2017, and agree with many of the criticisms parties raised. Yet those criticisms tend to focus on a different set of questions, with a broader scope than what we have been asked to assess.

3.1 Current travel trade scheme does not meet its objective

We continue to believe the current scheme needs reform. Even leaving aside concerns from the travel trade about the scheme's scope, the status quo is not an option if the scheme is to remain effective in covering the limited share of travel packages out of Ireland that are purchased from licensed and bonded travel agents and tour operators. There are no longer sufficient funds in the TPF for the Commission to be confident that all who have bought overseas travel covered by the current regime will enjoy financial protection should there be another large collapse.

Should there be a large collapse, the consequences will be felt by those yet to travel. Given the sequencing of events following a collapse, we think that the Commission will likely be able to repatriate those needing repatriation even after a large collapse. Instead, following a large collapse, the current scheme could not refund all valid claims in full. Because of this possibility, there may well also be delays in issuing refunds to all claimants as the Commission first has to identify the scale of the shortfall in the TPF.

3.2 Feasible options for a reformed scheme

The challenge in advising on which reform option to favour is that many of the better policy options are not entirely in the gift of the Commission. At a high level, we think better policy options will:

- Seek to align the costs of being bonded and licensed with the associated risks of claims from a given company's business model;
- Limit the extent to which firms are required to underwrite other firms' risks;
- Recognise that a backstop for low probability, high impact collapses is needed;
- Avoid placing the burden of funding the backstop arrangement on a small subset of firms that it covers;
- Favour options that are simple to administer, transparent and fair; and
- Strive to minimise the regulatory burden.

If the Commission is restricted to options that require no legislative action, we would reluctantly suggest that it introduce a levy on tour operators. This would mean only some licensed and bonded travel-trade firms contributed towards topping up the TPF, but the alternative policy option of significant increases in bonding levels across the board would impose an even worse regulatory burden.

If there is an appetite for legislative change, there are a number of actions we would advocate:

- Purchasing an insurance policy to cover "tail events" where the bond and the current funds in the TPF are insufficient to meet the costs of all repatriation and valid claims. The levy could then be set to fund this policy. Ideally, both tour operators and travel agents should pay the levy. Alternatively, if policy plans mean that that the existing scheme will soon be phased out, a government guarantee or using funds in the TPF to purchase insurance might be simpler administrative options to reintroducing temporarily a levy (after changing the definition of who can be levied).

- Considering changes to the definition of licensable turnover used to set bonding levels, with corresponding, appropriate changes to the percentage of PLTO used to calculate the required bond. We think that the candidates identified in our Interim Report remain appropriate (payments immediately forwarded by the seller and travel sold to business). We would recommend further work to understand how these changes affect the level of PLTO firms report. There should also be scope for further refinements to the definition of PLTO, to allow the Commission to continuously strive to keep bonding levels aligned with the level of risk posed by a given business model.
- Banning firms from trading above projected licensable turnover. This would help cap the size of backstop that is necessary. There should be flexibility, such that firms enjoying a good year of unexpectedly high demand are able to top-up their bond and continue trading. However, firms that do not top up their bond should not continue trading once turnover reaches the projected licensable turnover. The onus should be on firms and their auditors to make sure that they do not exclude from their estimates of licensable turnover packages that would enjoy financial protection following a collapse. To help with monitoring actual licensable turnover, there could be a requirement that at the time of sale the documentation clearly states whether the package is covered. (This might also serve to improve consumer awareness about the scheme.)

Where possible, any changes should not be made in isolation of wider policy developments. As a next stage the Commission needs to review any changes under consideration against the requirements of the PSD2. However, we recognise that the Commission faces constraints in adopting a holistic approach to reforms, given its current statutory remit is to oversee the existing scheme, a scheme for which changes are needed if it is to remain effective in offering the financial protection that it is intended to provide.