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Aircraft lessors have been left dismayed by a proposal that would condition green finance eligibility for new aircraft under the EU Taxonomy to lessors and operators scrapping more polluting aircraft within six months. The aircraft scrapping requirement is just one of a series of proposals by the Platform on Sustainable Finance (PSF), a working group aiding the inclusion of aviation into the EU Taxonomy.

Jan Melgaard, who leads the Aviation Sustainability Taskforce & Committee for Aircraft Leasing Ireland (ALI), acknowledges that while the EU has been doing a “great job” in developing the taxonomy, the proposed scrapping rule should have been brought up much earlier in discussions with stakeholders. “The scrapping rule is coming very late in the game, five minutes to midnight,” says Melgaard.



Other proposed requirements include a classification based on percentage margins below ICAO’s emission standards for new aircraft (similar to the one proposed by Steer earlier this year) and blending targets to encourage uptake of sustainable aviation fuel (SAF) – another decarbonisation priority for the Commission (see Fit for 55 coverage). Stakeholders including lessors are expected to submit feedback on these proposals (available in full here) by the end of this week.

Note for readers: *The proposed criterion does not represent the final view of the PSF or the European Commission, nor it precludes policy outcomes. The PSF’s purpose for this proposal is to gather feedback on how an aviation technical screening criteria can be incorporated to the EU Taxonomy.*

Scrapping does not fly with the industry

Melgaard believes the aviation technical screening criteria for the taxonomy would benefit from holding off on the scrapping rule for a period of time until it is “worked through” or until, in consultations with stakeholders, the European Commission can come up with a more “operational and constructive” approach. “As far as we are concerned, the EU taxonomy is well worked through, it would be very unfortunate to come with such a blunt measure as the ‘scrapping rule’ without having worked it through properly.”

Jim Bell, London Partner and Global Aviation Sector co-head at Watson Farley & Williams, also sees flaws in the way the scrapping rule has been conceived. “The problem is that the fleets of most airlines and aircraft lessors usually fit into one of three categories: new aircraft, mid-life aircraft, or older aircraft – and so, the airlines and aircraft lessors buying newer qualifying aircraft are often not the same as those that are decommissioning aircraft. It is therefore difficult to justify a direct decommissioning obligation for airlines and aircraft lessors that are buying or own aircraft that might otherwise qualify for sustainable financing,” Bell argues.

Bell also notes that “green investors want to invest in green products, and so anything that might cause a product to no longer be considered green is a challenge.” He argues that it may therefore be preferable for some investors for a financing to be determined as ‘sustainable’ for the purposes of the EU taxonomy by reference to the aircraft alone, including without a separate SAF usage obligation.

Proposals zero in on emissions, SAF use... and scrapping

The EU’s working group – the PSF – has outlined five options for passenger air transport on which they are currently seeking feedback from stakeholders.

The PSF’s Passenger Air Transport proposals (section 8.10) cover operators as well as the renting and leasing of air transport equipment. The proposed criterion aims to encourage aircraft investments that will make a “substantial contribution to climate change mitigation,” in particular:

1. [Air transportation] performed using zero exhaust CO₂ emission aircraft such as those powered by electricity or green hydrogen.

However, the PSF understands that complete zero-emission aviation technology in commercial aviation is “more than a decade away” from entry into service. Consequently, “transitional activities” (activities with lower greenhouse gas emissions than the industry average) are proposed for inclusion provided they comply with the “remaining” proposed technical screening criteria:

2. Until 2030, [air transportation] performed using aircraft meeting criteria as defined in NACE C30.3 (see appendix at the bottom of this report), acquired with the commitment that an aircraft not compliant with ICAO new type standards, with a size of at least 80% of max take-off weight of the new delivery, is decommissioned within 6 month of delivery of the new aircraft.
3. From 2030 onwards, performed using aircraft meeting criteria [2] and using a minimum of 10% of SAF, increased by 2 percentage points annually thereafter.
4. Performed using aircraft operated with a minimum of 5% SAF in 2022, with the percentage of SAF increasing by 2 percentage points annually thereafter.
5. Until [2024-2026], performed by the proportion of the fleet meeting NACE C30.3 criteria multiplied by the ratio of [aircraft retired / aircraft delivered] averaged over the last 10 years as evidenced by publicly available data (e.g. Cirium)

In a summarised form, Ishka understands that in addition to electric or green hydrogen-powered aircraft which are

“more than a decade away” from entering commercial service (Option 1), the initial proposal recommends the inclusion of aircraft as “transitional activities” under four qualifying options (Options 2 to 5):

- Option 2 (until 2030) would base eligibility on qualifying aircraft meeting margins vis-à-vis the ICAO emission standards and introduces a decommissioning requirement.
- Option 3 (from 2030) would base eligibility on qualifying aircraft meeting margins vis-à-vis the ICAO emission standard and a SAF requirement (10% blend rising by two percentage points annually thereafter)
- Option 4 bases eligibility on an increasing SAF requirement (5% SAF in 2022, rising by 2 percentage points annually).
- Option 5 remains unclear, but intention inferred is that the decommissioning requirement would apply by reference to a proportion of qualifying aircraft determined by dividing the number of aircraft decommissioned by those delivered over the past 10 years.

A SAF paradox

The proposed SAF requirements would initially surpass European blending mandates introduced earlier this year by Fit for 55 (see Insight: ‘Airlines react to EU’s new ambitious green deal measures’), which could encourage adoption of higher SAF blends. However, for that to be possible SAF production and distribution will need to be scaled to the point where mid-to-high single-digit (and eventually low double-digit) blends are available at most airports. At the same time, the exclusion of older aircraft types arguably creates a paradox: older aircraft with high SAF use can be more sustainable than new aircraft with lower SAF use.

According to a study unveiled this month by FPG Amentum, previous technology aircraft may level up and become as green as the newer technology by using additional SAF to offset the emissions resulting from the extra fuel consumption. For SAF blend rates of 0%, 1%, 5%, and 10% for the A320neo translate into matching blend rates of 14.4%, 15.3%, 18.8%, and 23.2% for the A320ceo. Assuming current SAF and Jet A-1 fuel prices, FPG estimates that the annual cost of bringing an A320ceo to the same level of emission reductions as an A320neo would be \$1 million.

The Ishka View

Ishka expects considerable backlash from the aviation finance community against some of these proposals, not least the scrapping requirement. Most stakeholders would agree that progression towards a net-zero 2050 should certainly involve a pivot towards the least-polluting transportation assets (be it electric cars, trains, and eventually zero-emission aircraft), but they would also argue aviation should not be penalised for its incapacity to switch to zero-emission assets sooner. That process could take decades, and in the meantime demand for air travel in much of the world is expected to increase. The current scrapping proposal leaves (theoretically) airlines and lessors to face a stark choice: either aim for green finance eligibility or choose growth and risk being labelled unsustainable.

However, it is important to consider that these are only initial proposals designed to gather feedback. Aviation is one of many sectors being worked on by PSF and the 32 members of the platform’s Technical Working Group (TWG) subgroup – which drafted the latest 993-page proposal. In that document, aviation only takes up 11 pages. In addition to air transportation (operators, lessors), the PSF’s latest proposal also include recommendations for the screening of

aviation OEMs and MROs to the extent to which they can be linked to eligible aircraft types. The coming months will be key to persuade the PSF into a practicable criterion with the right compromises ahead of its finalisation sometime in late 2021 or, most likely, the first quarter of 2022.

Appendix: NACE C30.3 criteria

In addition to the criteria outlined earlier in this report, the PSF is proposing that until end of 2027 taxonomy-compliant commercial aircraft (excluding aircraft categorised as “general aviation” and “business aviation”) meet the following “best in class” criteria:

1. Regional aircraft (Maximum Take-Off Mass or MTOM < 60t) certified to the ICAO CO₂ standard* with a margin of at least minus 11% to the New Type limit.
2. Narrowbody aircraft (60t < MTOM < 150t) certified to the ICAO CO₂ standard with a margin of at least minus 2% to the New Type limit.
3. Widebody aircraft (150t < MTOM) certified to the ICAO CO₂ standard with a margin of at least minus 1.5% to the New Type limit.
3. From 2028 to 2032, aircraft meeting the criteria [2] above and certified to run on 100% SAF
4. From 2033, aircraft meeting future criteria to be set at upcoming review of the taxonomy. The margins defined in [2a/2b/2c] will be subject to the regular review of the taxonomy taking into account available certified data and technological progress.

Ishka notes that the margins for narrowbody and widebody aircraft are lower than the ones proposed by Steer in their report to the Commission earlier this year (see Insight: ‘Will the new EU Taxonomy for green aviation address lessors’ concerns?’).

* The ICAO standard, contained in an annex to the 1944 Chicago Convention, is the world’s first global design certification standard governing CO₂ emissions for any industry sector and applies to new aircraft type designs from 2020 and to aircraft type designs already in-production as of 2023 (which would cover all new-technology in-production aircraft).

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