Airport competition in the EU: Main Characteristics, Evolution of the Case Law on Airport Charges and the need for Regulatory Oversight

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INTRODUCTION

- At the time of the Chicago Convention airports were viewed as only public utilities providing basic infrastructure.

- Over the past 50 years airports have undergone a major transformation:
  From mere infrastructure providers have become commercial entities.
  - Liberalization process
  - Emerge of new airline business models
  - Structural changes to the ownership status of many EU airports.

- Today airport management is an economic activity subject to competition rules.
KEY FACTORS OF AIRPORT COMPETITION IN THE EU

Main factors:

- The Liberalization of air services gradually led to:
  - The development of EU single aviation market
  - Conclusion of Open Skies agreements

- The development of competitive airline markets:
  - The emergence and rise of LCCs’
  - The creation of airline network concept / airline alliances
  - Consolidation of airline market / mergers between carriers EU and non–EU

- Wide spread of internet

- Advances in aircraft technology

- Development of road and rail network in the EU
THE ISSUE OF AIRPORT MARKET POWER & DOMINANCE

Dominance: “A position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on a relevant market by affording it the power to behave to an appreciable extent independently of its competitors its customers and ultimately of consumers” (EU Commission)

- Dominance is determined by Market Power which is “the power to influence market prices, output innovation, the variety of goods and services or other parameters of competition for a significant period of time.” (EU Commission)

- Factors for assessing market power and dominance:
  - market position
  - competitive constraints by competitors
  - competitive constraints by customers
  - barriers to entry
Airport Market definition: “the provision of airport operation services to passengers airlines including an airport’s land buildings and structures used for take-off and landing parking and servicing of passengers and airlines and the passengers terminals” (UK CAA).

Competitive constraints:

- Demand side substitutability:

  1. Ability of passengers to switch:

     Capability of the different categories of passengers to switch depends on:

     - Final destination of passengers: 63% of EU citizens live within two hours driving time of at least two Airports with annual traffic above one million passengers

     (Copenhagen Economics Study 2012).
THE ISSUE OF AIRPORT MARKET POWER & DOMINANCE

- Competitive constraints:
  - Demand side substitutability:
    1. Ability of passengers to switch
       - Proximity of the airport (catchment area): more than 50% on average of the destinations served by airports with the same catchment area
       - Other modes of transport and cost of switching: Leisure travelers are more price sensitive and less time sensitive than business travelers.

(Copenhagen Economics Study 2012).
Competitive constraints:

- **Demand side substitutability:**
  
  2. *Ability of airlines to switch by:*
  
  - Reducing capacity or frequency from one airport to another
  - Varying the size of aircraft
  - Switching airports and therefore by taking capacity from one airport and/or State and transferring to another

(Copenhagen Economics Study 2012)
THE ISSUE OF AIRPORT MARKET POWER & DOMINANCE

- Competitive constraints:
  - Demand side substitutability:
    
    2. Ability of airlines to switch - factors considered
    
    - Availability of airport infrastructure
    - Cost and slot capacity at alternative airports
    - Potential and actual competition from surface transport
    - Degree of competition from other airlines at alternative airports
    - Passengers ability to switch

    (Copenhagen Economics Study 2012)
THE ISSUE OF AIRPORT MARKET POWER & DOMINANCE

Competitive constraints:

- Demand side substitutability:

  2. Ability of airlines to switch
  
  - Increased flexibility for switching, especially for point to point carriers
  - Large number of routes are opened and closed annually (2500 routes opened in 2011 and 2000 were closed).
  - Traffic not easily replaced. Less than 20% of the lost capacity is regained in three years
  - Hub carriers less flexible in changing hub, yet can adjust a change in destination (spoke)
  - Majority of airports have a strong dependence on a single carrier.
Competitive constraints:

- **Supply side substitutability:**
  - factors taken into consideration:
  1. Readiness to provide the infrastructure required
  2. Time or regulatory barriers limiting an airport from switching operation (e.g. from seasonal to annual)
  3. Additional investment costs

In EU from 1996 to 2008 were added 81 airports, including the use of secondary airports, while the overall capacity is expected to increase by 41% by 2030.
THE ISSUE OF AIRPORT MARKET POWER & DOMINANCE

Competitive constraints:

- Barriers to entry:
  - Structural (for example those related to economies of scale and sunk costs).
  - Strategic (mostly related to excess capacity provided by airports, and pricing).
  - Legal (monopoly rights, subsidies, bilateral air services agreements, planning or environmental restrictions).

However:

- Most of regulatory barriers have been or are being removed as evidenced by the increase of new airports.
- LCCS are flexible enough to switch airports or to serve new ones.
- Passengers are also capable to switch between airports.
Conclusions as to airport competition:

In the EU:

- Airports are undertakings engaged to economic activities
- Airports face high fixed costs
- Airports are geographically fixed businesses
- Funding of infrastructure is indispensable part of airport's commercial use
- Airport substitutability exists for a significant portion of EU travelers

In view of the above characteristics actual market power is assessed based on:

- Airline business model and airline competition at the airport
- Extended competition among airports with overlapping catchment areas
- Competition with other modes of transport (road/high speed rail)
Conclusions as to airport competition:

As a result to the above:

- Airport market power cannot be assumed as in the past but it must be assessed on a case by case basis
- The ability of airlines and mainly that of LCC to switch and the dependence of an airport on a dominant carrier may result in generating countervailing buying power on the part of the airlines
Conclusions as to airport competition:

✓ The Level of airport competition in the EU can take different forms:
  □ competition between airports with overlapping catchment areas, within two hours driving time.
  □ competition for airport infrastructure, specifically, for airports with overlapping catchment areas or for airports competing for transfer passengers.
  □ competition between large airports, - hubs - including competition for network airlines and airline alliances.
  □ competition between airports of different size, including hubs and regional airports for LCCs’, serving point to point destinations.
  □ competition between airports for transfer passengers, irrespective of their location.
  □ competition between airports for leisure passengers irrespective of their location.
THE EVOLUTION OF CASE LAW ON AIRPORT CHARGES IN THE EU

PRICE DISCRIMINATION UNDER EU LAW:

- Price discrimination: the pricing structure where the same products or services with the same cost is sold to different customers to different prices (Stigler 1987)

- Price Discrimination ≠ Price Differentiation: In the latter case the price differentiation through rebates or volume discounts is justified, especially where customers are not completely homogeneous to the seller.

- Price discrimination is prohibited under 102 (c) TFEU under the conditions that:
  - The dominant undertaking has applied different prices to equivalent transactions
  - As a result other customers facing a competitive disadvantage
THE EVOLUTION OF CASE LAW ON AIRPORT CHARGES IN THE EU

- Common forms of price differentiation:
  - Quantity rebates provided that are based on economically justified factors (Case 322/81 Michelin v Commission 1983)
  - Loyalty rebates or fidelity rebates are prohibited (Case 85/76 Hoffmann-LA Roche v Commission, 1979).
  - Target rebates are assessed on a case by case basis to evaluate whether they raise entry barriers (Case T-228/97 Irish Sugar v Commission 1999).

- Therefore rebates and discounts are legitimate competition tools provided that:
  I. Are not exclusionary
  II. Must be linked with cost efficiencies
  III. The concept of abuse is objective and the threshold established by the Court does not require actual harm but the like-hood of potential harm
THE EVOLUTION OF CASE LAW ON AIRPORT CHARGES IN THE EU

EU CASE LAW- COMMISSION DECISIONS:

- First decision No 369 of 1995 for landing charges at Brussels Airport.

The Commission found that the system of discounts applied based on the number of movements on a month (volume discounts) “had the effect of applying dissimilar conditions to airlines for equivalent transactions linked to landing and take – off services thereby placing them at a competitive disadvantage.”

In reaching such decision the Commission was based on the following factors:

i. As relevant market was defined that of services linked to airport infrastructure.
ii. No genuine alternatives existed from Brussels airport for short and medium haul transport services.
iii. Brussels airport is an essential facility and a substantial part of the EU.
iv. Brussels airport holds a dominant position.
EU CASE LAW- COMMISSION DECISIONS:

Following the decision on Brussels airport charges, the Commission launched a large scale investigation during 90’s across the European Union.

- In 1999 Decision 199/1999 was issued for Portuguese airports
- In 1999 Decision 199/189 was issued for Finnish airports
- In 2000 Decision 521/2000 was issued for Spanish airports.

The Commission reaffirmed its reasoning in its decision for Brussels airport and reached on identical decisions for the discounts offered at either the Portuguese or the Spanish Airports, namely that such discounts which were mainly benefited the home base carriers of those airports had the effect of applying dissimilar conditions to equivalent transactions.
EU CASE LAW- COMMISSION DECISIONS:

Common findings to all the above cases:

▪ The definition of relevant market in the Brussels airport case was identically applied to all others.

▪ All airports in question were dominant undertakings within the meaning of Article 106 TFEU.

▪ Volume discounts in landing fees under which only one carrier benefits are discriminatory.

▪ Volume discounts in landing fees cannot justify economies of scale. The handling of the landing or the take-off of an aircraft requires the same service, irrespective of the owner or the number of aircraft belonging to a given airline.

▪ Volume discounts resulted to the abuse of dominant position of the undertakings entrusted with the operation of the airports, by applying dissimilar conditions to equivalent transactions.
EU CASE LAW- COMMISSION DECISIONS:

The evolution of case law on airport charges in the EU.

But: In decisions taken in considering the application of state aid rules different approach:

- In Decision 109/98 of 1999 on Manchester airport discounts on landing fees provided that are:
  - of limited duration
  - do not discriminate among users
  - set with objective criteria,

are considered as common commercial practice applied to attract new customers.

- In Decision 393/2004 of 2004 concerning an agreement concluded in between Charleroi airport and Ryanair the Commission reaffirmed the above approach by stating that in principle “it is not opposed to the granting of reductions to airlines to encourage them to launch new routes or increase flight frequency in order to stimulate passengers numbers under certain conditions.”
THE EVOLUTION OF CASE LAW ON AIRPORT CHARGES IN THE EU

EU CASE LAW- COMMISSION DECISIONS:

- In Decision C 12/2008 of 2011 concerning an agreement concluded in 2005 between Bratislava airport and Ryanair the Commission found that:
  - Revenues and cost structure differ from airport to airport and therefore the assessment must be based in relation to each airport conditions
  - The agreement was not exclusionary
  - Bratislava did not have a “flag” carrier
  - The agreement would render the airport more profitable

- Likewise in Decision C 25/2007 of 2013 concerning TMP airport in Finland and an agreement concluded in 2003 with Ryanair the Commission reached to identical conclusions.
THE EVOLUTION OF CASE LAW ON AIRPORT CHARGES IN THE EU

EU CASE LAW- DECISIONS ISSUED BY THE COURT OF JUSTICE OF EU

- Case C-163/1999 Portugal v Commission of the European Communities (2000). Discounts offered and enjoyed by only some trading parties giving them an economic advantage which is not justified leads to the application of dissimilar conditions to equivalent transactions.

- Case T-128/85 Aeroports de Paris v Commission (2002) Fixing of charges and fees with respect to the use of an airport is directly connected with the management of the airport infrastructure which is an economic activity.

Findings of the case law on airport charges

- Airport services to airlines and to passengers are economic activities

- Price differentiation based on different services and in the different needs of airlines must be provided in a no-exclusionary and non-discriminatory manner

- Volume discounts should be in principle accepted provided that are economically justified, cost efficient, capable of creating economies of scale not exclusionary and in case of public owned airports should meet the MEO test and being at least incrementally profitable for the airport concerned.

- The Decisional practice of the Commission on volume discounts on landing fees under 102 TFEU ≠ under 107 TFEU.
Findings of the case law on airport charges

- However the decisions issued under the period 1995-2000 where:

  1. Discounts were provided by a state owned airport to its flag carrier.

  2. No other airlines were objectively capable in meeting the requirements for the discounts.

  3. Airport competition was hardly existed in the EU

  4. Criteria relating to sharing of risk, guaranteed passenger numbers by the airline or the consequent welfare increase for consumers were not evaluated.
Findings of the case law on airport charges/ commercial agreements.

- In fact the validity of commercial agreements with airlines and the grant of volume discounts has never been really tested by the court under Article 102. Yet, it could be assumed that in line with the above findings developed by the Commission's practice and the Court’s jurisprudence any such agreement could be regarded as just and reasonable provided that:

i. The charges to be agreed must be economically justified, reflecting the costs of airport facilities and services actually rendered.

ii. The agreements must not be exclusionary and must not discriminate against the carriers of third countries.

iii. Price differentiation must result from differentiation in services rendered. Article 15 of the Chicago Convention should be adhered at all times.
Findings of the case law on airport charges:

iv. The agreement must be time limited and not of indefinite time.

v. In case of publicly owned airports where airport charges are seen as state resources any agreement must meet the requirements of the MEO test including an *ex ante* business plan evidencing the profitability of any such agreement.

vi. Volume discounts should be allowed provided that are open to all users and are based on objective criteria capable to be met by more users than the dominant carrier of the airport concerned.

vii. Commercial agreement should not be the only way of accessing airports installations especially in remote regions or in airports with significant market power.
CONCLUSIONS: THE NEED FOR REGULATORY OVERSIGHT REVISITED

- Airports differ in many ways (different business strategies & models geographical constraints)

- Passengers differ substantially as well (several categories of passengers)

- Airlines also differ depending on their business model (LCC’s, legacy carriers, charter operators)

- Major difference between airlines and airports: the latter are geographically fixed, two sided business seeking to attract both airlines and passengers.
CONCLUSIONS:
THE NEED FOR REGULATORY OVERSIGHT REVISITED

The competitive constraints faced by the airport and the increased airport competition should also be reflected in EU and to national regulatory practice and thus the following could be proposed:

1. Prior to any enactment of regulation either on the national or the EU level, the market power of each airport must be assessed by the ISA of each Member State by employing a uniform test across all EU based on guidelines and regulations issued by the Commission.

2. Most appropriate paradigm: The three tire test developed by the UK CAA.

3. In case of identifiable market power then the airport may be subject to regulatory provisions and annual monitoring.

4. The above should apply to all airports irrespective of their annual traffic with the exception of small regional airports serving regional connectivity and social cohesion.
5. Price differentiation based on different services must be provided on a non-exclusionary and non-discriminatory manner ensuring that the costs associated with different charges are not allocated to other users not benefiting from them.

6. Commercial agreements between airport and airlines should be fully accepted as legitimate competition tools.


8. Volume discounts should be also accepted provided that are justified cost efficient not exclusionary and capable of creating economies of scale.
CONCLUSIONS:
THE NEED FOR REGULATORY OVERSIGHT REVISITED

9. Central to the conclusion of commercial agreements and to any monitoring system is the issue of transparency and the exchange of information between the parties.

10. A critical issue is the existence of a binding dispute resolution system.

In conclusion, regulatory intervention is necessary to a degree proportionate to the identified market power of dominant or monopoly undertakings. Airport competition has been established in many parts of the EU and the institution and application of any regulatory or monitoring system along with the application of competition rules under a uniform manner in national and in EU level is capable to deter abusive conduct in the airport sector.
Kiss and goodbye
No Kisses above 3 min.!