

EC Competition Law – Its Effect on Air Transport Liberalisation

CATRIONA DALY*

Abstract: This paper explores the effect that EC Competition Law has had on the liberalisation of the European air transport sector and examines how it is contributing to further liberalisation. The competition rules are governed under the Treaty establishing the European Community; therefore this paper will refer to EC Competition Law. The terms EC and EU will be used interchangeably. The rules comprise of the prohibition on anti-competitive agreements in Article 81; the prohibition on abuse of a dominant position in Article 82; the rules in Articles 87-89 restricting state aids; the regulations providing for control of concentrations; and the special provisions on public and similar undertakings in Article 86. In order to appreciate the application of the competition rules we must first look at the liberalisation process. Section 1 looks at the background of liberalisation and how it was initiated in the EU. The remaining sections then proceed to examine how the EC's competition rules have been applied to the air transport sector. Section 2 examines how Articles 81 and 82 have been applied to the sector to ensure there is no restriction of competition. Section 3 looks at mergers and alliances and the impact of the Merger Control Regulation (1989). Section 4 examines the issue of state aids and the penultimate section explores the growing issue of access to airports and the liberalisation of airport services such as ground handling. The final section looks at what remains to be done in terms of liberalising the European air transport industry. Particular focus is on the extension of EC Competition Law to agreements between Member States and non Member States, the bilateral agreements between the EU and the US and the potential of Article 86 to liberalise the sector further.

Section 1: The Development of Liberalisation in EU Air Transport

1.1 Introduction

Competition policy has an important contribution to make to liberalisation. This applies to both the dismantling of unjustified state measures and to changing anticompetitive conduct on the part of companies. Competition policy must ensure that greater freedom due to liberalisation is not abused by firms in a dominant position or undermined through restrictive agreements and sharing of markets.¹

In the years that followed the Treaty of Rome, air transport was organised on the basis of the public regulation of conditions of competition, rather than the free market. As a consequence, air transport has been characterised by the existence of virtual national monopolies, market sharing and very high tariffs.² As a result of the Chicago Convention of 1944, which was held in order to decide on how to regulate international air transport, air transport was regulated by a series of bilateral agreements between Member States. This

* BA Law and Accounting, University of Limerick, Ireland

¹ Ehlermann, C.D., 'Contribution of EC Competition Policy to the Single Market' (1992) 29 CMLRev.at pp.257-282

² Blanco and Van Houtte, *EC Competition Law in the Transport Sector* (Oxford: Clarendon Press, 1996) at p.22

system left practically no scope for applying the competition rules.³ However, following the introduction of the Single European Act in 1986 it was no longer appropriate for air transport to be regulated in such a fashion. This Act was significant for two reasons. Firstly, it would permit free access to previously closed EU national markets for any EU airline. Secondly, competition rules would have to be applied to prevent limitations on competition being introduced.⁴

1.2 Background to Application of Competition Rules

The first obstacle to achieving the application of the rules lies within the Treaty of Rome itself. There is no basis for a Common Transport Policy within the Treaty, rather instead Title V (ex Title IV) which contains specific provisions relating to transport, is confined to establishing a procedure for the creation of a common transport policy by the Council. Also, air transport was one of the few sectors singled out for special treatment. It only receives one specific mention in the Treaty of Rome, namely Article 80(2), which excludes air (and sea) transport from the provisions of the Treaty dealing with transport policy and provides that air transport policy measures shall be taken as and when the Council decides.⁵

Regulation 17/62⁶, which was adopted in 1962, implemented rules for the enforcement of EC competition rules. However, the application of the Regulation was withdrawn from the transport sector some months later by Regulation 141/62.⁷ The Commission has stated that notwithstanding Regulation 141/62, Regulation 17/62 still applies to activities that are ancillary to air transport. Such ancillary activities include groundhandling services,⁸ computer reservation systems⁹ and computerised air cargo information systems.¹⁰ However, it was clear that the competition rules would not be able to be enforced effectively without some measures of liberality been introduced first.

1.3 Significance of *Nouvelles Frontières* Decision

Until the *French Seamen*¹¹ judgement, the Member States objected to the EU intervening in the maritime and air sectors. This judgement was crucial to the future, long-term application of competition rules to transport. However, the *Nouvelles Frontières*¹² case was the turning point in the Commission's attempts to introduce liberality into the air sector. In this case, the European Court of Justice (ECJ) definitively confirmed that the competition rules of the EC Treaty applied to the air transport sector. However, the Court held that implementing legislation was necessary in order to apply Articles 81 and 82. As this legislation had not yet been adopted by the Council, the Court ruled that therefore competition must be regulated by the "transitional provisions" of Articles 84 and 85.¹³

³ 'Extension of EU Air Transport Competition Rules to Air Transports to and from the EU', Speech by Humbert Drabbe to the 10th Annual Conference of the European Air Law Association, 6th November 1998. Available at www.europa.eu.int/comm/competition/speeches/text/sp1998_058.en.html

⁴ Blanco and Van Houtte, *op. cit.* fn. 2 at p.45

⁵ Balfour, J., 'Air Transport - A Community Success Story?' [1994] 31 CMLRev at p.1025

⁶ OJ 204/62; OJ Spec Ed 1962 87

⁷ [1962] OJ L124/2751

⁸ Olympic Airways, OJ 1985 L46/51

⁹ London European-Sabena, OJ 1988 L317/47

¹⁰ Van Bael, I. & Bellis, J.F., *Competition Law of the European Community*, (Oxfordshire: CCH Europe, 1994)

¹¹ Commission v France ("*French Seamen*") (Case 167/73) [1974] ECR 359

¹² *Ministere Public v Lucas Asjes ("*Nouvelles Frontières*")* (Joined Cases 209-213/84) [1986] ECR 1425

¹³ Adkins, B., *Air Transport and EC Competition Law* (London: Sweet & Maxwell, 1994) at pp.6-7

The *Nouvelles Frontières* case gave impulse to the Commission's efforts to liberalize European air transport and to establish detailed rules for the application of Articles 81 and 82 in the air transport sector.¹⁴ In December 1987, the first package of liberalisation measures was adopted by the Council of Ministers. From a competition point of view the essential element of the first package was the adoption of Regulation 3975/87¹⁵ that applied the competition rules of the EC Treaty to air transport between Member States. However, the Regulation does not apply to air transport between the EU and non Member States and so this remains subject to Articles 84 and 85.

The first package of measures was followed in 1990 by a Second Package and finally in 1992 by a Third Package.¹⁶ The liberalisation measures are an important part of the backdrop against which the competition rules are applied in the air transport sector, especially given Commission statements that the competition rules must be used to secure and protect the increased opportunities made possible by liberalisation.¹⁷ It must be emphasised too that the measures adopted by the EU to open up the market do not pre-empt the application of the competition rules in the EC Treaty.¹⁸

1.4 Block Exemptions

As opposed to the US, the EU recognised that some operations must be exempted from the rules due to the economic situation of the airline industry. As a result, an enabling regulation was also adopted by the Council¹⁹ giving the Commission the means to adopt block exemptions²⁰ in the air transport sector. Regulation 3976/87²¹ enables the European Commission to grant block exemptions not only for agreements that relate to air transport services but also for those that relate directly to ancillary services. Regulation 1284/91²² provides the Commission the authority to order a temporary relief against anti-competitive practices. The Commission, however, must have good reasons for believing that the practices in question are contrary to Article 81.

Following the implementation of the first package of liberalisation measures a series of block exemptions were granted by Regulations such as 2671/88-2673/88,²³ and 3618/92²⁴

¹⁴ Faull, J. & Nikpay, A., (eds), *The EC Law of Competition*, (Oxford: Oxford University Press, 1999) at p.876

¹⁵ [1987] OJ L374/1 (Amended by Regulation 2410/92 [1992] OJ L240/18). The amendment extends the Commission's powers to take measures for the application of Arts 81 and 82 to air transport within a Member State

¹⁶ See **First Package:** 1. Reg 3975/87 (Application of competition rules), 2. Reg 3976/87 (Concerted practices), 3. Dir 87/601 (Air fares), 4. Decision 87/602 (Capacity sharing and market access). **Second Package:** 1. Reg 2343/90 (Market access), 2. Reg 2342/90 (Air fares), 3. Reg 2344/90 (Concerted practices). **Third Package:** 1. Reg 25407/92 (Licensing of air carriers), 2. Reg 2408/92 (Market access), 3. Reg 2409/92 (Fares and Rates).

¹⁷ Van Bael, I., & Bellis, *op. cit.*, fn. 10 at p1022

¹⁸ Karlsson & Callaghan, 'Air Transport Liberalisation Comes Down to the Ground: Recent EC Developments in the Groundhandling Sector' (1999) 2 ECLR at p.94

¹⁹ Council Regulation (EEC) No 3976/87 of December 14, 1987, on the application of Article [81](3) of the Treaty to certain categories of agreements and concerted practices in the air transport sector, OJ 1987 L 374/9.

²⁰ Block exemptions are usually issued in the form of Commission Regulations, acting under powers delegated by the Council, in the form of an "enabling" Regulation. A block exemption is only applicable where certain conditions are satisfied.

²¹ [1987] OJ L374/9 (Amended by Regulation 2344/90 [1990] OJ L217/15 and Regulation 2411/92 [1992] OJ L240/19)

²² [1991] OJ L122/2. Council Reg 2299/89 (Code of conduct for computerised reservation systems) as amended by Council Reg 3089/93 [1993] OJ L278/1. Commission Reg 2672/88 [1988] OJ L239/1. Commission Reg 83/91 [1991] OJ L10/9. Council Reg 295/91 (Common Rules for denied-boarding compensation) [1991] OJ L36/5

²³ [1988] OJ L239/9-17

concerning joint planning, sharing of revenue, consultation on tariffs, computer reservation systems and groundhandling services. Furthermore, Regulation 1617/93²⁵ introduces more exceptions pursuant to Article 81(3) concerning special provisions for joint planning and coordination of schedules, special provisions for joint operations, for consultations on passenger and cargo tariffs, slot allocation and airport scheduling.²⁶ It seems that the introduction of exceptions goes on and on and undermines the substance of Article 81 despite the fact that certain conditions for the application of the exceptions are stated which might safeguard competition.²⁷

The aim of Regulation 3976/87²⁸ was to give the Commission the legal authority to issue block exemptions such that they would allow the airlines to adapt to an increasingly competitive environment. However, this Regulation was initially implemented over 15 years ago. I believe the airlines have now had sufficient time to adapt to the liberalised environment and therefore block exemptions should no longer be necessary. They are impeding the progress of achieving a fully liberalised market as they prevent the full application of Article 81 which is very significant in competition policy.

1.5 US Experience

By taking a gradual approach to liberalisation by the introduction of three separate packages the EU has tried to avoid the pitfalls of liberalisation in the US. There, liberalisation occurred almost overnight with the passing of the Airline Deregulation Act of 1978.²⁹ The limited success of liberalisation in the US has been blamed on the Reagan administration which failed to enforce anti-trust laws against the increasing number of concentrations. However, it must be noted that there are significant contrasts between EC and US Competition Law which is governed under the Sherman Act. For example, the definition of “restriction of competition” under Article 81(1) and “restraint of trade” under Section 7 of the Sherman Act – in the US a shift takes place from the ‘per se’ rules to the ‘rule of reason’ analysis, while the Commission interprets the prohibition of Article 81(1) very broadly. Also, the policy objectives under Section 2 of the Sherman Act, which concern abuse of dominant position, are narrower than those under Article 82.³⁰

The US experience also indicates that other responses to liberalisation include the establishment of “strategic alliances” with other airlines. Such practices are not always in the best interests of liberalisation as they restrict competition. It is perceived, therefore, as imperative that the competition rules are actively and effectively enforced in the sector to achieve liberalisation.³¹ I believe the EU’s phased approach was better suited to the liberalisation of the air transport sector. This allowed the airlines to adapt to the new competitive environment and avoided such a major exit of airlines from the market as

²⁴ [1992] OJ L367/16

²⁵ [1993] OJ L155/8 (Amended by Reg 1523/96 [1996] OJ L190/11 and by Reg 1083/1999)

²⁶ Reg 1083/99 has not prolonged joint planning and coordination of airline schedules and joint operations. Joint planning and scheduling within the limited meaning of the original definition in Reg 617/93 appear to be of lesser importance.

²⁷ Zekos, G., “The Implementation of EU Competition Policy and its Rules in Air and Maritime Transport” [1998] 7 ECLR at p.438

²⁸ [1987] OJ L374/9 (Amended by Regulation 2344/90 [1990] OJ L217/15 and Regulation 2411/92 [1992] OJ L240/19)

²⁹ 92 Stat.1705

³⁰ www.icclaw.com

³¹ Adkins, *op. cit.* fn.13 at pp.21-23

occurred in the US. This effectively reduced the number of competing airlines in the market leading to a reduction in overall competition.

1.6 Summary

The procedural framework within which competition law is enforced in the air transport sector varies depending both on the exact nature of the services in question and where such services are provided. There are three different procedural frameworks in which competition law is applied in the air transport sector:

- 1) Through the general implementing regulation, Regulation 17/62, as far as services ancillary to air transport are concerned;
- 2) Through the limited regime of Articles 84 and 85, as far as flights between the EU and non Member States are concerned; and
- 3) Through the air transport implementing regulations, Regulation 3975/87 and Regulation 3976/87 as far as flights between EU airports are concerned.³²

Section 2: Application of Articles 81 and 82 in the Air Transport Sector

2.1 Introduction

The regulation of competition within the EU is governed principally by the provisions of Articles 81 and 82 of the EC Treaty. Collectively they set out the general principles of competition law in the EU which aim to prevent the distortion of competition within the common market. Their relevance to air transport is significant given the vast number of multilateral and bilateral air transport agreements which exist, some of which may prescribe the level of fares, capacity or interlining³³ conditions and thereby produce anti-competitive effects.³⁴

2.2 Article 81

Article 81 prohibits all inter company agreements which have as their object or effect the restriction or distortion of competition within the EU and which may affect trade between Member States. Article 81 applies to both private and public undertakings in the air transport sector.³⁵ Of importance for the air transport sector is the fact that the article envisages exemption not only for individual agreements but also for categories of agreements known as block exemptions. It is contended that there have been no instances of the Commission enforcing Article 81 to a conclusion on its own initiative. However, the Commission has

³² Van Bael & Bellis, *op. cit.* fn. 10 at p1024

³³ Interlining is the acceptance by one airline of travel documents issued by another airline for carriage on the services of the first airline. An interline passenger is one using a through fare for a journey involving two or more separate airlines.

³⁴ Goh, Jeffrey, *European Air Transport Law and Competition*, (Sussex: John Wiley and Sons, 1997) at p.35

³⁵ Article 81(1) establishes a prohibition on all agreements, in any form, which prevent, restrict or distort competition in the common market and which produce an effect on trade between Member States. Where an agreement falls foul of the terms of Article 81(1), under Article 81(2) it is "automatically void". Where an agreement does fall foul of Article 81(1), it may nonetheless be exempt from the consequences of this by obtaining exemption under Article 81(3). An exemption will be granted where the agreement meets criteria set out in Article 81(3).

examined a number of applications for exemption of joint operating agreements between airlines.³⁶

2.2.1 Application of Article 81 - Case Examples

Lufthansa – SAS

In 1995, Lufthansa and SAS submitted to the Commission a co-operation agreement to create an integrated air transport system between the two airlines.³⁷ The Commission concluded that the conditions pointed to a substantial restriction of actual and potential competition between Lufthansa and SAS on the routes between Germany and Scandinavia. Inevitably this meant that trade between Member States would be affected. Consequently, the co-operation agreement was incompatible with Article 81(1).³⁸

SAS/Maersk Air³⁹

In this case, SAS and Maersk Air had notified a co-operation agreement to the Commission but it transpired that coinciding with the entry into force of this agreement, the airlines entered and withdrew from a number of routes. This had the effect of decreasing competition. These entries and withdrawals, which were not notified, formed part of a wider market-sharing agreement.⁴⁰ Agreements such as these are prohibited by Article 81(1). The market sharing agreed between SAS and Maersk Air is a 'hard core' restriction of competition that does not meet the conditions to benefit an individual exemption pursuant to Article 81(3).⁴¹ Secret cartels are among the most serious restrictions of competition. The detection, prosecution and punishment of secret cartels have been one of the central features of the competition policy pursued by the European Commission since it was set up.⁴²

Among the areas the Commission's enforcement activities in the air transport sector will continue to focus on is the fight against hard-core restrictions such as naked market-partitioning and price-fixing agreements. The Commission will also work to remove restrictive behaviour by air carriers, which could have the potential effect of foreclosing previously liberalised transport markets.⁴³ Article 81 will be of enormous benefit to the Commission in regulating these activities.

2.3 Article 82 - Abuse of Dominant Position

³⁶ *Supra* fn. 5 at p.1035

³⁷ The objectives of the agreement would be achieved by creating a joint venture for services between Germany and Scandinavia. In addition, Lufthansa and SAS would conduct joint network planning, a joint pricing policy and joint budgeting. There would also be reciprocal arrangements in respect of frequent flyer credits, code sharing, maintenance and groundhandling and data processing. A single marketing strategy would organise the marketing of services offered by both carriers.

³⁸ Goh, *op. cit.* fn. 34 at pp. 43-44

³⁹ Cases Comp/D2/37.444 and Comp/D2/37.386 (OJ L265)

⁴⁰ *31st Report on Competition Policy – 2001* (Luxembourg; Office for Official Publications of the European Communities, 2002) para 43 to 47

⁴¹ Martinez, R., 'Commission fines SAS and Maersk Air for Market-Sharing', Competition Policy Newsletter, October 2001 (Luxembourg; Office for Official Publications of the European Communities, 2001) at p.41

⁴² *Supra* fn.40 at para 31 and 32

⁴³ Stragier, J., 'EC Competition Policy in the Aviation Sector: State of Play and Outlook', Annual Conference of the Guild of European Business Travel Agents Lisbon, 22 March 2002. Available at http://europa.eu.int/comm/competition/speeches/text/sp2002_009_en.pdf

Article 82 concerns the abuse of a dominant position. It has been suggested that the difficulty in applying Article 82 to the provision of air transport services is to identify the relevant product and geographical markets on which dominance is to be assessed. In Ahmed Saeed,⁴⁴ the ECJ concentrated on the question of interchangeability and looked at the extent at which an operator of a given scheduled service faced competition either from operators of other scheduled services or from alternative methods of transport.⁴⁵

Article 82 is very important in the air transport industry. This is linked to the fact that “flag carriers” have inherited strong positions on their traditional home markets and often have considerable power to impede the development of competition, in particular from new entrants.

2.3.1 Application of Article 82 - Case Examples

British Midland v Aer Lingus⁴⁶

The airlines in question were participating in tariff consultations for the Dublin – London routes. Once an air carrier has participated in a consultation concerning tariffs for a specified route, that air carrier must grant interlining facilities to all air carriers operating on the route in question.⁴⁷ Under Article 82, the Commission found that Aer Lingus was abusing its dominant position by refusing interlining facilities to British Midland.

London European v Sabena⁴⁸

The Commission also applied Article 82 to a refusal by Sabena to allow access to its computer reservation system to London European. However, because this conduct concerned the operation of computer reservation systems rather than air transport as such, the proceedings were taken under Regulation 17/62 rather than Regulation 3675/87.

The cases highlighted concern the duty of an undertaking in a dominant position to allow its competitors access to “essential facilities” which it controls. This raises questions about the extent to which dominant companies should be obliged to assist their competitors.⁴⁹

Other cases examined by the Commission concerning possible breaches of Article 82 have included the following:⁵⁰

- Frequent flyer programmes (FFPs),
- Additional commissions over and above the normal commission to travel agents (sometimes called “override commissions”), and
- Excessive capacity or frequency (particularly when frequencies are increased with intention to exclude a new entrant).

⁴⁴ Ahmed Saeed Flugreisen and Silver Line Reise Buro v Zentrale zur Bekämpfung unlauteren Wettbewerbs (Case 66/86) [1989] ECR 803

⁴⁵ Friend, M., ‘Competition in the Air Transport Sector’ [1989] 14 ELRev at p.427

⁴⁶ (IV/33.544) OJ 1992 L 96

⁴⁷ Adkins, *op. cit.* fn.13 at pp.32-33

⁴⁸ Commission Decision 88/589/EEC of November 4, 1988, relating to a proceeding under Article 82 of the EEC Treaty (IV/32.318, London European – Sabena) OJ 1988 L 317

⁴⁹ *Supra* fn.36 at p.1051

⁵⁰ Faull & Nikpay, *op. cit.* fn.14 at p.910

These are examples of practices that airlines are introducing to protect themselves in the newly competitive environment. They often have the potential to be anti-competitive though and it is vital therefore that the competition rules are enforced against them. I wish to highlight in particular the Virgin/ British Airways (BA) case which concerned commissions paid to travel agents.

2.3.2 *Virgin/British Airways Case*⁵¹

Virgin's complaints against BA were the first of a series of complaints received by the Commission alleging abuses of a dominant position by airlines operating loyalty rebate schemes. These schemes effectively tie travel agents to a dominant airline. The Commission found that the commissions offered by BA to travel agents were equivalent to a 'loyalty discount'.⁵² These incentives had the effect of discouraging travel agents from selling air transport services to other airlines. Schemes of this type have been consistently condemned as an abuse of a dominant position in other industries in the past.⁵³ The Commission fined BA and ordered it to change its travel agency payments into a more competition neutral system. As a dominant firm, BA should provide supplementary concessions to travel agents only where these reflect extra services provided by the agent or efficiencies realised by BA.⁵⁴

2.4 Conclusion

The Comité des Sages⁵⁵ advocated a strong anti-trust framework if liberalisation was to lead to a healthy and competitive industry. The Comité recommended that competition authorities move quickly to enforce rules against predatory practices or other practices having similar effects.⁵⁶ These are common features of the air transport industry. Articles 81 and 82 have been used extensively in the past in opening up the air transport market to competition. I believe it is inevitable that they must play an even more important role in a liberalised market. Liberalisation usually leads to more intense competition between companies. Therefore, airlines might try to restrict competition by entering into price fixing or output limitation practices. This would undermine the benefits of the liberalisation packages. Articles 81 and 82 must be enforced to counter these practices.

Section 3: Concentrations

3.1 Introduction

On the 21st September 1990 the Council Regulation on the Control of Concentrations between Undertakings, often referred to as the Merger Control Regulation, entered into force.⁵⁷ A concentration is considered to take place for the purposes of the Regulation where two or more independent undertakings merge or where persons controlling at least one

⁵¹ [2000] OJ L30

⁵²This is a discount based not on cost savings but on loyalty.

⁵³ Case 85/76. Hoffman-La Roche & Co. A.G. v Commission: [1976] ECR 461, [1979] 3 CMLR 211

⁵⁴Wood, D., 'Competition and Networks in the Transport Industry' (2001). Available at http://www.iadb.org/sds/doc/IFM-David_Wood-paper.rtf.

⁵⁵ The Comité des Sages were a group of experts in the air transport sector appointed in 1993 by the European Commission for Transport to reflect and advise on the future of aviation in Europe.

⁵⁶ *Expanding Horizons*, A Report by the Comité des Sages for Air Transport to the European Commission, January 1994

⁵⁷ Reg 4064/89 [1990] OJ L257/14

undertaking acquire control of the whole or part of another.⁵⁸ Concentrations with an EU dimension are subject to notification to the Commission. The entry into force of the Regulation established a clear basis whereby the Commission could intervene in respect of concentrations.

The Regulation applies to the air transport sector with the same effect as it does in other industries. Therefore the concepts of restriction of competition, abuse of a dominant position and effect on trade between Member States are employed in the same manner as in other sectors. It applies to both intra and extra EU air transport. The substantive test to be applied by the Commission is whether the transaction would lead to the creation or strengthening of a dominant position within the relevant market.⁵⁹ I believe that the Merger Control Regulation is very significant for EU air transport as airline concentrations are among the most significant changes that have emerged in the air transport industry since liberalisation.⁶⁰

3.2 Distinction between Mergers and Alliances

Alliances are co-operative joint ventures, they do not involve a lasting change but rather instead an agreement between the parties to co-ordinate their competitive behaviour. These co-operative arrangements are subject to the procedural rules in Regulation 3975/87 and Regulation 17/62 and therefore are subject to Articles 81 and 82. The Commission has said that the distinction between concentrative and co-operative joint ventures is one of the most delicate matters it has to resolve under the Merger Control Regulation and also one of the most common.⁶¹ The criterion for distinguishing between them is found in Article 3 of the Regulation.⁶²

3.3 Application of Articles 81 and 82 to Air Transport Mergers

The Merger Control Regulation creates an exclusive regime for merger control. Regulations 17/62 and 3975/87 are not applied to concentrations as defined in Article 3. They are covered solely by the Merger Control Regulation. As a consequence of this, Article 81(1) ceases to be directly effective in respect of concentrations. However, this is not the case with Article 82 as this is directly effective and does not require the adoption of implementing legislation to be enforceable in a national court.⁶³

Prior to the adoption of the Merger Control Regulation there was a developing body of case law which applied both Articles 81 and 82 to concentrations.⁶⁴ The Commission actively intervened in air transport mergers even while the legal basis upon which it was entitled to

⁵⁸ Council Regulation (EEC) 4064/89, Article 3 (OJ L257 21.9.90)

⁵⁹ Stragier, Joos, 'Current Issues arising with Airline Alliances', Speech to the 11th Annual Conference of the European Air Law Association, Lisbon, 5th November 1999. Available at http://www.europa.eu.int/comm/competition/speeches/text/sp1999678_en.html

⁶⁰ Aer Rianta Report - Future Strategy Direction: A Report to the Minister for Enterprise (1999)

⁶¹ Adkins, *op. cit.* fn.13 at pp.104-105

⁶² Art 3 defines a merger as comprising of the following elements: (a) joint control between the parties; (b) the joint venture must perform on a lasting basis all the functions of an autonomous economic entity; and (c) there must be no co-ordination of competitive behaviour between the parties to the joint venture or with the joint venture.

⁶³ Adkins, *op. cit.* fn.13 at pp.137-139

⁶⁴ For example, in respect of Article 81(1), in the *Philip Morris* case it was established by the ECJ that insofar as the acquisition of both minority interests serves as a means for influencing the commercial conduct of the parties in question, with the result that competition is restricted or distorted, Article 81(1) would apply. Similarly for Article 82, the Court established in the case of *Continental Can* that it was an abuse of a dominant position to seek to strengthen that position by means of a concentration.

act was unclear. Thus, in 1987 it carried out an investigation into the then proposed merger between two privately owned airlines, British Airways and British Caledonian.⁶⁵ Again, in February 1990, the Commission sent a statement of objections to Air France, objecting to the takeover of UTA on the grounds that it may constitute an abuse of a dominant position.⁶⁶

3.3.1 Application of Merger Regulation – Case Examples

Unlike the US, the Commission has been particularly active in monitoring concentrations between airlines. Among the cases examined under the Merger Control Regulation are *Delta Airlines/ Pan Am*;⁶⁷ *Air France/ Sabena*;⁶⁸ *British Airways/ TAT*;⁶⁹ and *British Airways/ Dan Air*.⁷⁰

The Commission has not opposed any of these mergers. Where a merger has given rise to competition concerns, as in the case of *Air France/ Sabena* and *British Airways/ TAT*, the Commission has obtained detailed undertakings from the parties concerned and also, in the *Air France* decision, from the governments involved. These were aimed at facilitating new entry to the market.⁷¹ It has been considered that the Commission took a lenient approach in connection with *Air France* and *Sabena*. It is questionable whether the commitments obtained were very effective or went far enough to prevent the impediment of competition, particularly between two airlines operating from airports fairly close to each other, and particularly given *Air France's* position as the largest airline group in Europe.⁷²

3.4 Alliances

The airline industry is characterised by a number of alliance agreements. This can be explained by the regulatory barriers that currently make it difficult for airlines from different Member States to merge their activities in other ways.⁷³ Foreign ownership rules restrict foreign ownership of a European airline's voting shares to 49%.⁷⁴ In general, the Commission says that airline alliances can bring benefits for passengers by extending networks and improving efficiency. However, alliances can also significantly restrict competition on individual routes and remedies may need to be imposed to mitigate this.⁷⁵

3.4.1 Key Commission Decisions on Alliances

The first key decision related to the takeover by British Airways of all British Caledonian's operations at London-Gatwick at the end of 1987. In subsequent cases the Commission insisted on partner airlines giving up slots, either immediately or when asked to do so, and in some cases surrendering licences. However, the evidence to date suggests that in most of these cases little real competition has emerged to challenge the alliance partners. For

⁶⁵ [1988] 4 CMLR 258

⁶⁶ Adkins, *op. cit.* fn.13 at p.103

⁶⁷ [1992] 5 CMLR M56

⁶⁸ [1992] OJ C272; [1994] 5 CMLR M1

⁶⁹ [1993] 4 CMLR 10

⁷⁰ [1993] 5 CMLR M61

⁷¹ Adkins, *op. cit.* fn.13 at p.104

⁷² Balfour, J., *European Community Air Law*, (London: Butterworths, 1995)

⁷³30th Report on Competition Policy – 2000 (Luxembourg; Office for Official Publications of the European Communities 2001) para 91

⁷⁴ 'One World, Few Airlines', "The Economist", September 24th 1998

⁷⁵ *Supra* fn.40 at para 135

⁷⁶ *Supra* fn.43

example, on the routes operated by Lufthansa/SAS where remedies were imposed there are still no other airlines competing with these alliance partners.⁷⁶ Yet the European Commission has persisted in this approach notably in key decisions on two of the global alliances – British Airways American Airlines (BA-AA) and Lufthansa-SAS-United Airlines alliance.⁷⁷ The Lufthansa –SAS- United Airlines alliance which received Commission approval in October 2002 is the first of the EU/ US airline alliances examined by the EU competition authority to receive official approval.

3.5 Changes in Commission's Approach to Mergers and Alliances

The Commission has started to change its set of remedies for allowing mergers and alliances to proceed. It is adjusting its remedy approach towards making actual entry of new competitors more likely. A first step in this process is for the Commission to market test the proposed remedies in order to verify whether they are adequate and sufficient to attract effective new or increased competition. On this basis, the Commission was satisfied before granting an exemption to the Lufthansa/SAS/bmi British Midland co-operation agreement that there was an actual interest from third competitors to enter or expand their services on the route in question. In the Lufthansa/ Austrian Airlines alliance case the Commission goes a step further by proposing that the exemption decision should only be granted to the extent that market entry by a new competitor on certain key routes actually takes place. However, difficult problems arise when new actual entrants cannot be found.⁷⁸

3.6 Difference in Assessment of Intra and Extra EU Alliances

For services within the EU, Regulation 3975/87 determines the procedure for applying Articles 81 and 82. Regulation 3976/87 empowers the Commission to grant block exemptions in respect of co-operation agreements between airlines. However, both these Regulations only apply to air services within the EU.⁷⁹ For services between the EU and non Member States, the Commission must rely on the interim arrangements laid down in Article 85. This was confirmed by the ECJ in *Nouvelles Frontières*.

In analysing transatlantic air agreements, account must be taken of the regulatory barriers, in particular rights of access to the transatlantic and intra-EU routes of the parties to the agreements compared with the rights of third airlines, and of the existence of non-regulatory barriers, notably the scarcity of slots at certain airports or the pooling of frequent flyer programmes. It will accordingly have to be considered whether the agreements comply with Articles 81 and 82, and if appropriate under what conditions they may be authorised.⁸⁰

3.7 Conclusion

The Merger Control Regulation and Articles 81 and 82 have significant consequences for the air transport industry due to the increasing number of mergers and alliances. In order to clear co-operative arrangements between airlines, the Commission has accepted undertakings from the airlines to remedy any worries the Commission has. However, it is not readily apparent that those undertakings have actually facilitated new entry to the air

⁷⁷ Doganis, R., *The Airline Business in the 21st Century*, (London: Routledge Press, 2001) at p.96

⁷⁸ *Supra* fn.43

⁷⁹ 26th Report on Competition Policy – 1996 (Luxembourg; Office for Official Publications of the European Communities 1996), para 100

⁸⁰ *Ibid* para 99

transport market.⁸¹ The Commission is addressing this problem by market testing the remedies for their effectiveness in attracting new entrants.

Attention is now turning to mergers and alliances between EU and US airlines. The Merger Control Regulation enables the Commission to apply the competition rules to mergers between Member States and non Member States. As regards transatlantic alliances, Article 85 is inadequate to deal with the competition issues which these give rise to. The procedural framework for investigating international alliances must be simplified and made more effective.⁸² The benefits of liberalisation must not be rendered void due to the growing trend of international alliances with the potential to have distortive effects on competition.⁸³ If the Council is serious about prohibiting anti-competitive global alliances, it must confer the Commission with the appropriate powers of investigation. This is essential in order to fulfil the complete liberalisation of EU air transport.

Section 4: State Aids

4.1 Introduction

The rules on state aid contained in Articles 87-89 are very important in the context of air transport.⁸⁴ For a long time these rules were not applied in the air transport sector although the Commission had published guidelines on their application as early as 1984 and it had been clear since the *Nouvelles Frontières* decision in 1986 that the state aid rules applied to air transport.⁸⁵ However, EU air transport had been characterised by a high level of state intervention and bilateralism. Therefore, there was arguably little point in applying the state aid rules while the conditions of competition among airlines in other respects were still so unequal. As they began to change though, so did the Commission's attitude to enforcement.⁸⁶ Also, in the past serious political forces stood in the way of proper application of the rules.⁸⁷

The recent liberalisation of EU Skies has resulted in the disappearance of "flag carrier" status in relation to intra-EU services and state-owned carriers are now required to compete on equal terms with privately owned carriers. Given that a high number of airlines operating within the EU are either wholly or partially owned by the state, state aid is an issue of crucial importance: more so in the context of a liberalised market.⁸⁸

4.2 Background to Application of State Aid Rules

⁸¹ Faull & Nikpay, *op. cit.* fn.14 at p.921

⁸² *Supra* fn.59

⁸³ McShea, S., 'The "Dominant Position" Doctrine and the European Union's Response to the British Airways/ American Airlines Alliance', 21 Sept 2000, Available at http://www.bc.edu/bc_org/avp/law/lwsch/journals/bciclr/23_1/04_FMS.htm

⁸⁴ According to the definition set out in Article 87(1), state aid is incompatible with the common market if it is granted by a member state or through state resources, if it distorts or threatens to distort competition by conferring an advantage on certain undertakings or the production of certain goods and if it is liable to affect trade between Member States.

⁸⁵ *Supra* fn.5 at p.1039

⁸⁶ *Ibid*

⁸⁷ Balfour, J., *State Aid to Airlines- A Question of Law or Politics*, Yearbook of European Law 1995 (Oxford: Oxford University Press, 1996) at p.168

⁸⁸ Goh, *op. cit.* fn.34

In the early days the European Commission did not have a clear-cut policy on the issue of state aid. In their Report of January 1994,⁸⁹ the Comité des Sages urged the Commission to enforce strictly the state aids provisions in the Treaty of Rome, but accepted that: 'support for the transition of an air carrier to commercial viability may be in the Community's interest if the position of competition is safeguarded'. In essence, the Comité recommended the removal of state aid from airlines, with the exception of one final injection for restructuring purposes.⁹⁰ In November 1994 the Commission approved guidelines for the evaluation of proposals for state aid for airlines. These mirrored to a considerable extent the recommendation of the Comité des Sages.

The 1994 Guidelines for State Aid in the Aviation Sector⁹¹ gave the Commission more control in ensuring rigorous enforcement of the Treaty's ban on those aids which distort competition.⁹² The review of state aids needs to be more stringent in the post-liberalisation process. The first stage is to determine whether an aid has been advanced, and if so whether it is compatible with the Treaty.

4.3 Has a State Aid been Advanced?

Article 87 (1) defines state aid as being 'any aid granted by a Member State or through State resources in any form whatsoever'. State aid is given a very wide definition by the use of the words 'in any form whatsoever'.⁹³ According to the guidelines, the first thing which the Commission must appraise is whether the public funding (in the form of a capital injection, loan or State guarantee for an airline) constitutes state aid under Articles 87 and 88 or whether it can be compared to a normal commercial transaction by a private shareholder interested in investing in a company.⁹⁴ This is known as the 'market economy investor principle'.⁹⁵ The Commission's guidelines state that proper application of the market economy investor principle requires the analysis of a number of different factors depending on the nature of the alleged aid in question.⁹⁶

4.4 Distortion of Competition

Having established the existence of a state aid, the Commission must next determine whether the aid is compatible with the common market since the handing out of an aid *per se* is not an infringement of Article 87(1).⁹⁷ The test will be satisfied if the state aid would have the effect of altering the competitive position of rival undertakings which existed before the payment of the aid in question. Some commentators have said that this is an easy test in the

⁸⁹ *Expanding Horizons*, A Report by the Comité des Sages for Air Transport to the European Commission, January 1994

⁹⁰ Crosbie, N, 'Airline Deregulation & the North Atlantic Air Travel Market: Implications for the US-Ireland Route' (1996) UL Thesis Collection

⁹¹ Application of Articles 92 and 93 (now 87 and 88) of the EC Treaty and Article 61 of the EEA Agreement to state aid in the aviation sector (OJ C 350, 10.12.1994)

⁹² European Commission, *Moving Forward: The Achievements of the European Common Transport Policy* (Luxembourg: Office for Official Publications of the European Communities, 1998)

⁹³ Soames and Ryan, 'State Aid and Air Transport' [1995] 5 ECLRev at p293

⁹⁴ *The Functioning of the Air Transport Market*. Available at www.europa.eu.int/comm/transport/air/rules/state_aid_en.htm

⁹⁵ The test was laid down by the ECJ in the mid - 1980s and provides that any financial transaction made in circumstances which would not have been acceptable to a private investor operating under normal market economy conditions will constitute state aid.

⁹⁶ *Supra* fn.93 at p293

⁹⁷ Under Article 87(1) of the EC Treaty, a financial transaction, even if it has been deemed to constitute state aid, is only prohibited if it 'distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods'.

air transport sector, particularly given the intense degree of competition which characterises the EU market. For example, in the 1993 decision concerning the grant of state aid to Aer Lingus, the Commission said: 'The aid, given the strong and lively degree of competition existing on most of Aer Lingus' routes, could distort competition between EU carriers'.⁹⁸

4.5 Does the State Aid fall within the Exemptions?

If the aid is prohibited as incompatible, it then needs to be determined whether the aid falls within the exemptions. These exemptions are either mandatory in that the treaty provides for an automatic exemption – Article 87(2), or discretionary so that the exemption is dependant on a decision of the Commission – Article 87(3). In practice, it is the discretionary exemption of Article 87(3) which is the most frequently invoked in the case of state aid within the air transport industry and which is most obviously appropriate to restructuring aid granted as a prelude to privatisation.⁹⁹

4.6 Effect on Liberalisation

The crisis that hit the airline market in the early 1990's meant that it was necessary to grant state aid to some airlines. The Commission mapped out a strict approach to make sure that this aid genuinely met a need for restructuring, without distorting competition on the market in the process. The crisis also coincided with the introduction of the Third Package of liberalisation measures that confer on EU air carriers a general right of access to the market. Therefore, another objective was to enable airlines bearing inherited liabilities to make a fresh start without, however, damaging their competitors' interests.¹⁰⁰

The 1994 guidelines on the application of Articles 87 and 88 ensure that the process of liberalisation is not impinged by subjecting the grant of state aid to a number of stringent conditions. Among these conditions are:

- The aid must form part of a restructuring programme
- The aid may be granted only once (the "one time, last time" principle)
- The programme must include capacity restrictions
- The programme must not be targeted on expansion

Also, the government must not interfere in the management of the company, which must be run according to commercial principles. Restructuring aid as an exceptional measure to support restructuring of the airlines is also justified by the procedure laid down in Council Regulation 659/1999.

Since 1991, seven airlines have received public funding for restructuring which was considered state aid under Article 87: Sabena, Iberia, Aer Lingus, TAP, Air France, Olympic Airways and Alitalia.¹⁰¹ These restructuring programmes for airlines were necessary due to the liberalisation process but the Commission has responded to this need.

4.7 Case Example - *Alitalia*¹⁰²

⁹⁸ OJ 1994 L54/30, at 36

⁹⁹ *Supra* fn.93 at p.291

¹⁰⁰ *Supra* fn.94

¹⁰¹ *Ibid*

¹⁰² Decision 97/789/EC

In 1997, the Commission gave conditional authorisation for payment of aid to Alitalia. Its assessment was based *inter alia* on the viability of the restructuring plan and the commitments given by the Italian authorities, the complete absence of discrimination in favour of Alitalia and the absence of a dominant influence over prices. The Commission considered that the aid would be conducive to the development of air transport in Europe without adversely affecting trade between Member States to an extent contrary to the common interest. It acted with the twofold concern to preserve a company in the process of return to viability on the air transport market without jeopardising competition: consumers would benefit both from Alitalia's services and from those of competitors.¹⁰³

4.8 Implications of September 11th Attacks

Due to the "one time last time" policy, the European Commission was able to declare by the end of the 1990's that state aids were no longer warranted in the aviation sector.¹⁰⁴ However, the attacks of September 11th could have changed this. As operating aid is in principle prohibited, the Commission considered that the provisions of Article 87 (2)(b) fitted the problems facing the airlines. It is of the opinion that, given their unforeseeable nature, the number of victims and the impact on the world economy, the events of 11th September were exceptional occurrences within the meaning of Article 87(2)(b).¹⁰⁵ The measures, applied to all enterprises in the same manner, would not trigger distortions of competition in Europe, and the aid package would not be used as a pretext to solve other problems of the sector.¹⁰⁶ They only apply to extraordinary problems generated by the terrorist attacks.

4.9 Conclusion

Most of the airlines which needed restructuring have now completed the process. The Commission therefore considers that state aid is no longer necessary and there is no longer any reason for it except for truly exceptional and unforeseeable circumstances. It is imperative for the maintenance of a liberalised and competitive market that no more state aids are handed out. The actions of the European Commission post the events of September 11th show that the EU is not willing to return to the days of handouts for airlines. The Commission stressed that the events of September 11th must not undermine the Commission's policy on state aid to restructuring based in particular on the 'one time, last time' principle.¹⁰⁷

As regards the US, the authorities there have been highly critical in the past about the inequities of EU state aid. However, airlines in the US can also expect to benefit from

¹⁰³ *Competition Policy in Europe and the Citizen*, (Luxembourg: Office for Official Publications of the European Communities, 2000)

¹⁰⁴ Gimblett, R., *BLG Aviation News* (London: Issue 7, Winter 2001) Available at www.blg.co.uk

¹⁰⁵ The Commission considers that the provisions of Article 87(2)(b) of the Treaty may apply to two types of damage resulting from the events of 11 September 2001 - Measures to compensate for the costs to airlines of American airspace being closed for four days and assumption of the extra cost of insurance.

¹⁰⁶ It must also be noted that aid which was granted to airlines in this case must be distinguished from aid granted in the past. The reason for this is that the Commission itself did not hand out any money. Instead, the Commission will not oppose aid from member states in the categories allowed.

¹⁰⁷ Commission communication of 10 October 2001 on the repercussions of the terrorist attacks in the United States on the air transport industry - COM (2001) 574 final, para 29

Chapter 11¹⁰⁸ bankruptcy proceedings. As European state aid is decreasing, it appears to me that the number of US airlines operating under Chapter 11 actually appears to be increasing.

I think the policy for state aids which the Commission has adopted as a result of the liberalisation has been a success. It has been suggested that restructuring aid may be incompatible with the single market¹⁰⁹ but I believe it acts as a necessary support to the liberalisation process. Although state aids to airlines have decreased there is still scope for the grant of state aids in the air transport sector. An area which the Commission could become active in the future is state aids to airports and other facilities.¹¹⁰ Therefore the issue of state aids in the air transport sector has not disappeared just yet.

Section 5: Access to Airports & Services

5.1 Introduction

Although air transport has been gradually liberalised in the last decade, the European air transport industry remains hampered by a number of issues, among these is limited access to infrastructure such as airports.¹¹¹ Liberalisation in the air has to be matched by liberalisation on the ground.¹¹² Former Competition Commissioner Karel Van Miert identified access to airports as one of the most important issues that would arise for the Commission's attention in the future.¹¹³ It is submitted that the two main issues relating to transport infrastructure are firstly access, to ensure that operators can get access to the necessary infrastructure to operate their services, and secondly discrimination, to ensure that different operators are treated equally.¹¹⁴ In the first three years following the entry into force of the Third Package, the Commission's activities were mainly focused on ensuring free market access under Regulation 2408/92.¹¹⁵

5.2 Slot Allocation

In order for airlines to gain access to airports they must acquire slots.¹¹⁶ However, the growth of the market, due to liberalisation, has aggravated congestion at major airports and this has reduced the number of available slots. The Comité des Sages Report¹¹⁷ says that priority must be given to providing sufficient airport capacity. Congestion at some key airports has reduced the possibility for new entrants to take advantage of the opportunities offered by the Third Package.

¹⁰⁸ Chapter 11 is a protection for bankrupt airlines from creditors which allows them to continue operating.

¹⁰⁹ *Supra* fn.87 at p.166

¹¹⁰ 'EC Competition Law – Its Dramatic Influence on Public Sector Liberalisation - The Transport Sector' Lecture given by Vincent Power to the Irish Society for European Law, Dublin, 23 January 2003

¹¹¹ *Supra* fn.43

¹¹² *Supra* fn.92

¹¹³ Van Miert, Karel, 'Competition Policy in the Air Transport Industry', Speech to the Royal Aeronautical Society, 9 September 1998 www.europa.eu.int/comm/competition/speeches/text/sp1998_035_en.html

¹¹⁴ Faull, & Nikpay, *op. cit.* fn.14 at p.910

¹¹⁵ Pfahler et al, *Airports and Air Traffic Regulation, Privatisation and Competition* (Peter Lang GmbH Europaischer Verlag der Wissenschaften, Frankfurt am Main, 1999) at p.60

¹¹⁶ A slot is essentially a time which an airline can use the runway for landing or take off

¹¹⁷ *Supra* fn.55

Two fronts which the Commission has acted upon to ensure that new entrants have access to congested airports are:¹¹⁸

- On the regulatory front - Council Regulation 95/93¹¹⁹ has established the principle that at least 50% of available slots are to be for new entrants;
- In applying the competition rules - for example the Commission gave approval to the alliance between Lufthansa and SAS on condition that the airlines sold a substantial number of slots so as to facilitate the entry of new competitors on certain routes between Germany and Scandinavia.¹²⁰

Council Regulation 95/93 bases slot allocation on the system known as “grandfather rights”.¹²¹ This system was established by the IATA and was used by EU airports before the introduction of Regulation 95/93. The system makes it extremely difficult for new entrant airlines to obtain access at airports. However, along with the 50% rule the Regulation contains a “use it or lose it” rule which means that airlines would have to surrender slots if they did not use them for 80% of the year. Some commentators consider that the effects of the Regulation may be limited.¹²² It is also questionable whether the system based on historical rights can ensure the most efficient use of scarce resources. The crisis in the aviation industry following the events of September 11th also revealed the inflexibility of the current regulation.¹²³ The Commission’s investigations into several airline alliances and merger cases have highlighted too the shortcomings of the current slot regime. Concerns about proposed airline mergers and alliances arise because competitors cannot easily enter the market since they cannot get slots at congested airports.¹²⁴

On 20 June 2001, the Commission adopted a proposal to revise the Regulation based on a study of its impact. The changes should primarily help to make the slot system more flexible in terms of both allocation and use and strengthen the co-ordinator’s role and the monitoring of compliance.¹²⁵

5.3 Application of Competition Rules to Slot Allocation

The application of competition rules to the allocation of slots has been hindered by the block exemption permitting grandfather rights which has been applied to slot allocation and airport scheduling. This exemption must be acted upon in accordance with the Regulation. However, the fact that the Commission has issued a block exemption clearly shows that these practices fall within Article 81(1). Also slot allocation procedures may involve the participation of airlines which would give rise to the application of Article 81 (1). It has been

¹¹⁸ Speech by Humbert Drabbe, ‘EC Competition Policy in Relation to Airports’, 13th April 1999. Available at www.europa.eu.int/comm/competition/speeches/text/sp1999_012_en.html

¹¹⁹ OJ 1993 L14/1

¹²⁰ 28th Report on Competition Policy – 1998 (Luxembourg: Office for Official Publications of the European Communities, 1999)

¹²¹ Grandfather rights mean that “a slot that has been operated by an air carrier as cleared by the co-ordinator shall entitle that carrier to claim the same slot in the next equivalent scheduling period” – Art 8(1)(a) of Reg 95/93.

¹²² Balfour, *op. cit.* fn.72 at p.99

¹²³ Due to the crisis the European Parliament and the Council adopted a Regulation amending Article 10 of the Regulation on the allocation of slots. As a result of the Regulation airport co-ordinators would be required to allocate slots to air carriers for the summer and winter seasons 2001/2002 which were affected by the crisis even if air carriers had not used them in accordance with the Community rules. This was to address their capacity to the significant drop in demand during the period in question

¹²⁴ *Supra* fn.43

¹²⁵ *Supra* fn.92

questioned whether the block exemption permitting grandfather rights satisfies the requirements for block exemptions set out in Article 81(3).¹²⁶ Article 82 would usually have no significance for slot allocation procedures since under the Regulation slot allocation is now handled by an independent co-ordinator. The scope for the application of the rules is enormous though as the system of grandfather rights is inherently at odds with competition policy.

5.4 Non - Discriminatory Access

The Commission's main concerns in airport cases have been to ensure non-discriminatory access, in particular at the level of airport charges, and to enable carriers to benefit from airport services, such as handling of luggage, catering or registration of passengers, which are of good quality at a reasonable price.¹²⁷

The types of discrimination which can arise are as follows:

1. Fees charged to airlines

The *Zaventem*¹²⁸ case illustrates landing fee discrimination and the Commission position. In this case British Midland (BM) argued that a system of discounts on landing fees, which increase in line with an airline's volume of traffic, favoured carriers with a high volume of traffic and thereby placed small carriers competing with them at a disadvantage. Moreover, according to BM, there was no objective justification in granting such discounts since the services, which an arriving or departing aircraft requires, are the same, however many times they are supplied. The Commission found that the Airways Authority held a dominant position in its capacity as airport authority on the market in aircraft landing and take-off services. The Commission also found that the system of discounts on landing fees had the effect of applying dissimilar conditions to airlines for equivalent transactions. This constituted an abuse of a dominant position within the meaning of Article 82(c). Since this system had been established by a Member State by way of an administrative act, it constituted an infringement of Article 86 read in conjunction with Article 82.¹²⁹

In 2000, the Court of First Instance gave an opinion on the issue of airport charges stating that the Commission was right to demand, on the basis of EU law, that charges should be non-discriminatory, which does not necessarily mean that they must be all the same. This allows for the possibility of having different levels of charges as long as the differences can be justified on the basis of objective, non-discriminatory criteria.¹³⁰ Also in view of this development the Commission is considering whether it should at some point in time again put forward an updated proposal to take account of the above findings of the Court.¹³¹

2. Landing fee system

In the decisions against landing fee systems in Finland and Portugal there was discrimination between domestic flights and intra-EU flights.¹³²

¹²⁶ Balfour, *op. cit.* fn.72

¹²⁷ Faull & Nikpay, *op. cit.* fn.14 at p.910

¹²⁸ [1995] OJ L216

¹²⁹ Faull & Nikpay, *op. cit.* fn.14 at pp.910-911

¹³⁰ Aeroports de Paris/ Alpha Flight Services T 128/98, 12 December 2000

¹³¹ *Supra* at fn.94

¹³² [1999] OJ L 69

5.5 Groundhandling Services

Traditionally groundhandling¹³³ at many EU airports has been restricted to the airport operator or the national flag carrier. However, as a result of the third liberalisation package Council Directive 96/67¹³⁴ was adopted. This directive gradually opened up the services to competition and led to full liberalisation in December 2002. The Commission has received many complaints concerning the supply by monopolies of ground handling services of poor quality at an excessive price. The Commission's approach has been to take steps to ensure that the monopoly is broken and that second operators are allowed in on a non-discriminatory basis. The Commission has applied Article 82 to cases involving the provision of ground handling services.

These cases are amongst the most difficult the Commission has to deal with. Not only is there often substantial local political interest in the outcome, they raise significant questions as to the technical feasibility of allowing competing operators to provide services in conditions where safety is paramount and space is limited.

5.6 Application of Competition Rules to Groundhandling: Case Examples

The Commission initiated proceedings under Articles 82 and 86 concerning the exclusive right granted to Olympic Airways to provide services to third parties. As a result of the proceedings, the Greek Government undertook to liberalize airport services a year earlier than envisaged under the Council Directive and to introduce quality standards and quality control, tariffs more closely linked to cost, separate accounting for ground-handling activities and improved infrastructures.¹³⁵

5.6.1 Frankfurt Airport Case¹³⁶

Following complaints from several airlines, the Commission found that under Article 82 the operator of Frankfurt airport had abused its dominant position as operator by prohibiting airlines from providing self-handling services and by denying access to any independent providers of ground handling services.¹³⁷

¹³³ Groundhandling services comprise all the activities performed when an aircraft stops over in respect of the aircraft itself, the passengers and the cargo. In general, ground-handling services may be provided for airlines by the airport operator, by another airline or by an independent specialized ground-handling company (third-party handling). Air carriers may also provide their own handling services either individually (self-handling) or in a pool (joint handling).

¹³⁴ Council Directive 96/67 of 15 October 1996 on access to the ground-handling market at Community airports provides that, in the case of airports whose annual traffic is not less than three million passenger movements and of certain categories of services, Member States are required to take the necessary measures to ensure free access by suppliers of ground-handling services to the market for the provision of ground-handling services to third parties as from January 1, 1999. However, they may limit the number of authorized suppliers to no fewer than two. Similarly, Member States have to take the necessary measures to ensure the freedom to self-handle as from January 1, 1998; however, they may reserve the right to self-handle (to no fewer than two airport users), self-handling being narrowly defined.

¹³⁵ *Supra* fn.79 para 129

¹³⁶ Flughafen Frankfurt/ Main AG [1998] OJ L72/30; [1998] 4 CMLR 779

¹³⁷ 'Competition Overview' [1994] CMLRev at p.1009

5.6.2 *Alpha Flight Services/ Aeroports de Paris (ADP) Case*¹³⁸

In this case the Commission found that the operator of the two Paris airports had abused its position as operator by imposing discriminatory commercial fees on suppliers or airlines providing ground-handling or self-handling services such as catering, cleaning and freight handling. ADP charged different level of fees to the two third party suppliers, AFS, the plaintiff, and OAT, a subsidiary of Air France. The Commission also clarified that the Groundhandling Directive does not affect the application of the competition rules of the Treaty.¹³⁹

Case law demonstrates that measures to prevent new entries, discriminatory pricing and inefficiencies can amount to an abuse in violation of Article 82. There is no doubt that Article 82 is likely to bolster the effectiveness of the Groundhandling Directive. However, it is not only Article 82 that may play an important role in the liberalisation process. Article 81 also provides the Commission with the ability to limit foreclosure effects on third parties where agreements would afford groundhandling operators the opportunity to eliminate competition. For example, the Commission has intervened against the Frankfurt Airport operator's attempt to preserve its old monopoly by concluding long-term contracts with airlines. The Commission's intervention shows that exclusive agreements with customers infringe Art 81(1) and would also be difficult to justify under Article 81(3).¹⁴⁰

Where groundhandling services are operated by the airport operator or the national flag carrier and an infringement of Articles 81 and 82 occurs, the Member State in question will be in breach of its obligations under Article 86¹⁴¹ by reason of the conferral of a special or exclusive right on the undertaking to perform handling services. However, often service providers found guilty of abusing a dominant position argue that they are fulfilling a public service role and hence are exempted pursuant to Article 86(2).¹⁴²

5.7 Conclusion

Although the principles of neutrality, transparency and non-discrimination are followed by the Regulation 95/93, it could be said that the mechanism of allocating slots represents a barrier to entry and as such is at variance with the basis of EU competition policy.¹⁴³ I agree with this contention. It is surprising that the Commission allowed the practice of grandfather rights to continue. The process of finding an alternative should have been conducted before the implementation of the Directive. A major concern is that the sale of slots could lead to anticompetitive effects, particularly to the reinforcement of dominant positions.¹⁴⁴ This is one area in which the Commission's attempts to liberalise air transport have failed.

¹³⁸ *Alpha Flight Services/ Aeroports de Paris* [1990] OJ L230/10; [1998] 5 CMLR 611

¹³⁹ Forrester *et al*, 'Competition Law', Yearbook of European Law 1998, (Oxford; Oxford University Press, 2000) at p.535

¹⁴⁰ See Karlsson & Callaghan, 'Air Transport Liberalisation Comes Down to the Ground: Recent EC Developments in the Groundhandling Sector' [1999] 2 ECLR at pp.86-100

¹⁴¹ Article 86 makes it clear that public undertakings and undertakings which are granted special or exclusive rights are generally subject to the rules in the EC Treaty, subject to limited scope for exemption and the Member States have an obligation to ensure that such rules are respected.

¹⁴² Balfour, *op. cit.* fn.72 at p.203

¹⁴³ *Supra* fn.27

¹⁴⁴ Blum & Logue, *State Monopolies Under EC Law*, (Sussex: John Wiley & Sons Ltd, 1998) at p.348

It is submitted that as regards groundhandling the general competition rules in the EC Treaty may provide for a further degree of liberalisation than the 1996 Directive.¹⁴⁵ I agree with this proposition. The general competition rules may be invoked to ensure access at those airports which fall outside the scope of the Groundhandling Directive, provided they are of a sufficient size within the EU to attract interest.¹⁴⁶ Also, I think the Commission could invoke Article 86 more often in groundhandling cases where groundhandling services are operated by the airport operator or the national flag carrier.

However, the focus of the Commission's concerns in liberalising air transport as regards airports has shifted to ensuring there is no discrimination in landing fees charged by airports. It is expected that a number of new cases will arise in the near future.

Section 6: How can EC Competition Policy contribute to further Liberalisation?

6.1 Introduction

Despite all the progress achieved so far in moving from a regulatory regime to a more open competitive environment for air transport, much remains to be done. Air transport within the EU has almost been fully achieved as far as the legislation concerns. However, as regards flights between the EU and non Member States the picture is very different. Two areas where more needs to be done by EC Competition Law to achieve liberalisation are the extension of EC Competition Law to flights between the EU and non Member States and the negotiation of bilateral agreements with non Member States.

6.2 Extension of EC Competition Law to Air Transport to and from the EU

In the *Ahmed Saeed* case¹⁴⁷ the ECJ held that the competition rules applied in principle to both domestic and external air transport and not merely international air transport between Member States. The Commission has adopted two proposals for Council Regulations which would give full effect to the competition rules between Member States and non Member States.¹⁴⁸ One of the directives contains an extension of the implementing rules which currently only apply to transport between EU airports. The other contains the legal basis for the adoption of block exemption regulations.¹⁴⁹ However, the proposals regarding air transport between Member States and non Member States have still not been adopted by the Council. In the absence of enabling legislation applicable to flights between the EU and non Member States, Articles 84¹⁵⁰ and 85¹⁵¹ of the EC Treaty apply.

The application of these articles may give rise to legal conflicts though, in particular where Member State Authorities and the Commission open procedures at the same time. Also, the

¹⁴⁵ Soames, T., 'Ground Handling Liberalization' (1997) Vol 3 Journal of Air Transport Management at p.94

¹⁴⁶ Many airports in the Community, in light of their size and volume of international traffic, should fall under Article 82, even though they fall outside the Groundhandling Directive

¹⁴⁷ *Ahmed Saeed Flugreisen and Silver Line Reise Buro v Zentrale zur Bekämpfung unlauteren Wettbewerbs* (Case 66/86) [1989] ECR 803

¹⁴⁸ Art and Van Linderkerke, *Developments in EC Competition Law in 1997: An Overview* [1998] 35 CMLRev 1167

¹⁴⁹ COM (97) 218 final

¹⁵⁰ Art 84 establishes the power of authorities in member states to apply Articles 81 and 82 to areas concerning which implementing legislation has not been passed by the Council pursuant to Article 83.

¹⁵¹ Art 85 grants limited authority to the Commission to investigate suspected infringements of Article 81 and 82. Art 85 does not, however, give the Commission itself the power to bring such infringements to an end. On the contrary, the Commission may only publish a decision and authorise member states to take the necessary measures.

Treaty does not appear to establish a hierarchy between these two articles. It is therefore not clear if action by a Member State under Article 84 precludes action by the Commission under Article 85 or vice versa. The Commission takes the position that parallel proceedings are possible since both articles contain clear obligations to act without establishing such a hierarchy.¹⁵²

6.3 Negotiation of Bilateral Agreements with Non Member States

The Commission has always considered it unacceptable that Member States have persisted in concluding bilateral agreements with non Member States since the internal market was completed. These bilateral deals hinder the total liberalisation of European aviation as they do not involve the application of EC Competition Laws. Also, some of the bilateral deals which the US has struck with some Member States give antitrust immunity to designated EU flag carriers which have entered into alliances with their chosen partners.¹⁵³ The Commission obtained negotiating briefs from the Council enabling it to conclude agreements on the gradual liberalization of air transport services with certain non-member countries, e.g., Switzerland and the US. However the negotiating brief with the US only covers certain issues and was not effective enough to deal with competition issues.¹⁵⁴

The White Paper on European Transport Policy¹⁵⁵ for 2010 “Time to Decide” identified the development of a coherent external policy for aviation as an urgent priority given the effects of a fragmented approach on the development of our airline industry.¹⁵⁶ Much of the debate surrounding an external relations policy in air transport has centred on the issue of competence.¹⁵⁷

6.4 Ruling on Bilateral Agreements

On 5th November 2002 the ECJ ruled that eight member states had breached EU law by signing “open skies” agreements with the US.¹⁵⁸ The court ruled that clauses restricting the ownership and control of national airlines were incompatible with EU law.¹⁵⁹ The current bilateral deals are illegal as they discriminate against other member states by restricting the takeoff and landing slots to airlines from the host country.¹⁶⁰

¹⁵² Drabbe, H., ‘Extension of EU Air Transport Competition Rules to Air Transport to and from the EU’, Speech to the 10th Annual Conference of European Air Law Association, 6th November 1998. Available at www.europa.eu.int/comm/competition/speeches/text/sp1998_058_en.html

¹⁵³ ‘Liberalising Aviation – Unfinished Business’, *The Economist*, 24th May 2001

¹⁵⁴ 27th Report on Competition Policy – 1997 (Luxembourg; Office for Official Publications of the European Communities 1997), at para 89

¹⁵⁵ COM (2001) 0370

¹⁵⁶ Communication from the Commission on the consequences of the Court judgements of 5 November 2002 for European air transport policy COM (2002) 649 final

¹⁵⁷ This eliminates the Commission’s claim to exclusive jurisdiction under Article 113 EC. The main difficulty with the Commission’s proposals stem from its decision to adopt Article 113 of the EC Treaty as the legal base for its proposed legislation, instead of Article 84(2).

¹⁵⁸ Cases C-466/98, C-467/98, C-468/98, C-469/98, C-471/98, C-472/98, C-475/98 and C-476/98 against the United Kingdom, Denmark, Sweden, Finland, Belgium, Luxembourg, Austria, Germany

¹⁵⁹ A bilateral agreement would require that an air carrier to be designated under the agreement must “be substantially owned and effectively controlled by nationals” of the Contracting State. This would be a clear infraction of Community law since it would be contrary to the right of establishment as recognised under the Treaty, the freedom of market access under Council Regulation 2408/92 and the common criteria for the licensing of Community air carriers under Council Regulation 2407/92.

¹⁶⁰ Lannin & Miles, *Reuters*, Available at www.reuters.com/news

However, it is to be noted that the ECJ has not ruled that the Commission has exclusive competence to negotiate bilateral agreements on behalf of Member States, or that the existing bilateral agreements are of themselves illegal in their entirety.¹⁶¹ The Court also noted that many aspects of the agreements were properly handled by national governments, not by the Commission.¹⁶² Analysts claim that the national governments may prefer instead to rework their bilateral deals with the US in a way that stops discrimination against other EU carriers.¹⁶³

The Commission has submitted several proposals, most recently in 1997, to the Council to provide it with the power to apply Articles 81 and 82 to routes between the EU and non Member States.¹⁶⁴ The Commission argues that there is an urgent need to re-launch consideration of these proposals in the light of the Court's judgement on the 5th November 2002. It adds that only by overcoming the limitations of the existing investigation and enforcement regime could a fully effective co-ordinated air transport policy be achieved.¹⁶⁵ However, it is unlikely that the Council will give these powers to the Commission as the individual Member States wish to guard their national territory.

6.5 Article 86

Article 86 is of importance in the field of air transport, both because of the prevalence of State-owned airlines and also because airlines are frequently given special or exclusive rights, not only to operate routes, but also in respect of other operations and activities at airports.¹⁶⁶ So far, the Commission's application of Article 86 in the air transport sector has been relatively modest. It is submitted that it is surprising that Article 86 has not been invoked more often in the air transport sector. Such use as has been made of it has been in relatively minor cases. Nevertheless, the Commission's ability to threaten use of its powers under Article 86 to issue directives provides it with a strong lever with which to persuade member states and airlines to "voluntarily" take action to pre-empt action by the Commission.¹⁶⁷

6.6 Conclusion

Although, the *Ahmed Saeed* case arose in 1989, the transitional provisions still apply to air transport between the EU and non Member States. Articles 84 and 85 are inadequate to enforce competition rules, as national courts do not have the authority to apply Article 81.¹⁶⁸ However Article 82 can apply as it contains no exemption provision comparable to Article

¹⁶¹ Airline Regulatory ECJ Rules on Open Skies Bilaterals, BLG News, Issue 11, Winter 2002. Available at www.blg.co.uk

¹⁶² Landler, M., *Europe's Highest Court Voids Air Treaties*, available at www.nytimes.com

¹⁶³ Castle & Harrison, *Open Skies: European Court of Justice declares bilateral air traffic deals and ownership rules illegal*, Available at www.independent.co.uk

¹⁶⁴ 'Full Implementation of Competition Rules Proposed for Air Transport Sector'. Available at www.iclaw.com/devs/uk/ec/ukee_024.htm

¹⁶⁵ Communication from the Commission on the consequences of the Court judgements of 5 November 2002 for European air transport policy COM (2002) 649 final

¹⁶⁶ Article 86 requires Member States to withdraw any national measures contrary to the EC Treaty rules with respect to undertakings and companies to which a Member State has granted "special" or exclusive rights. It can be invoked against a Member State only in conjunction with the infringement of one or several other provisions of the EC Treaty.

¹⁶⁷ *Supra* fn.5

¹⁶⁸ This reflects the fact that it would be contrary to the general principles of legal certainty for Articles 81(1) and (2) to be applied by member state courts unless it was possible to determine whether the exemption of Article 81(3) was applicable.

81(3).¹⁶⁹ The Commission can take action against restrictive practices on extra-EU routes only under Article 85 of the Treaty, which allows it to introduce monitoring provisions in the absence of any specific implementing regulation. The Member States are furthermore entitled to initiate parallel proceedings under Article 84.¹⁷⁰ It is contended that this is a very inefficient practice. It also does not provide sufficient legal security. It is vital that the Commission has at its disposal adequate legal instruments for guaranteeing the application of its competition rules both within the EU and in relations with non-member countries. Also, the extension of EC Competition Law will mean that the Commission will have the same powers that the US Antitrust authorities have. These authorities already apply their competition law to European airlines.¹⁷¹

So far the Council has refused to give the Commission the mandate it requires to do this. This is unacceptable in the light of the internal common market. The Commission must also be vested with the relevant powers of enforcement and authority to negotiate air service agreements with non-EU countries. In order to get the process started the Council could give the Commission powers to deal with some competition issues and gradually this could lead to full powers, a phased approach just like the implementation of the three liberalisation packages. The airlines must be able to know exactly what practices are allowed on such routes.

Section 7: Overall Conclusion

A decade has now passed since the adoption of the third package of aviation liberalisation measures which applied the EC Competition rules to the air transport sector. The question must be asked at this stage has the application of the competition rules been a success. In 1999, the Commission presented an analysis of the functioning of the internal market.¹⁷² Competition has increased, with many major routes being flown by three or more airlines. Also, consumers have benefited from lower fares. However, the number of new entrants has been modest compared to the US where around 15 per cent of the domestic air travel market is offered by low cost, low fare new entrants (U.S. Department of Transportation, 1996).¹⁷³ It is argued that on balance the result of EU liberalisation has been disappointing. However, this is hardly surprising though given the timing of the final stage of liberalisation in the middle of an economic recession, the concern of the larger airlines with more global events, and the time needed to change some of the more deep-seated structural barriers, such as airport slot availability, input market monopolies and state aids.¹⁷⁴

Putting aside the poor effect on the market due to the economic recession, I believe the air transport legislation which has been enacted by the EU has been very comprehensive and has covered most areas, except the application of the competition rules to air transport between the EU and non Member States. Through these regulations the Commission has

¹⁶⁹ Ahmed Saeed Flugreisen and Silver Line Reise Buro v Zentrale zur Bekämpfung unlauteren Wettbewerbs (Case 66/86) [1989] ECR 803

¹⁷⁰ *Supra* fn.154 at para 87

¹⁷¹ Speech by Karel Van Miert at the North Atlantic Assembly Meeting, 16th February 1998, *The Transatlantic and Global Implications of European Competition Policy*. Available at www.europa.eu.int/comm/competition/speeches/text/sp_054_en.html

¹⁷² Commission Communication entitled "The European Airlines Industry: From Single Market to Worldwide Challenges" COM (1999) 182

¹⁷³ Morrell, P., 'Air Transport Liberalization in Europe: The Progress So Far', *Journal of Air Transportation Worldwide* Vol.3, No.1 - 1998 at p.50

¹⁷⁴ *Ibid* at p.42

actively enforced the competition rules of the Treaty. Competition enforcement has also played a major role in bringing forward the necessary degree of liberalisation to ensure competitive markets.¹⁷⁵ Without the Member States enacting the legislation, liberalisation would not have been a success. Some commentators contend that the various EC Council Regulations that have been introduced in order to implement the general competition rules in the transport sector should be combined into a single regulation.¹⁷⁶ However, I do not support this. The sectors of transport are very different and each has its own individual needs and these are properly addressed in legislation specific to that sector. Air transport is a clear example of this, for example consideration must be taken of extra safety and security concerns.

I believe the Council and the Commission should concentrate now on applying the competition rules to routes between the EU and non Member State countries. This has implications for a number of areas, most importantly mergers and alliances. It is claimed that the international alliance system is an unsatisfactory surrogate for the cross-border mergers that seem to be an eventual necessity.¹⁷⁷ Liberalisation needs to be further continued to allow the alliances that exist at the moment to become mergers. Some might comment that consolidation is undesirable and will lead to the preclusion of new entrants. It is argued that a high degree of concentration could foreclose routes and airport slots, thereby re-erecting legally removed barriers.¹⁷⁸ However, I believe that once the competition rules and the different instruments of competition law are properly applied and enforced the result will be beneficial.

There is a real chance of consolidation occurring now due to the ECJ's ruling of the 5th November 2002 which held that nationality clauses in bilateral agreements were illegal under EU Law. The elimination of nationality clauses would take away a major impediment to restructuring and consolidation in the EU airline industry. If the Council of Ministers fails to give the Commission the power to apply the competition rules to routes between the EU and non Member countries, consolidation would be beneficial. This is because under the Merger Control Regulation the Commission can enforce the competition rules against routes between the EU and non Member States. Until open skies are universal and limits on foreign ownership are relaxed, airlines will continue to live in the twilight world of shifting alliances rather than the clear day of global consolidation.¹⁷⁹

¹⁷⁵ *Supra* fn.43

¹⁷⁶ *Supra* fn.27 at p.441. Vincent Power also supported this proposition in his lecture to the Irish Society for European Law, 23 January 2003. He suggested that we could use the new Regulation 1/2003 instead of the individual regulations which are currently in force.

¹⁷⁷ Airline Business, December 2000, Editorial J.A. Donoghue

¹⁷⁸ *Supra* fn.43

¹⁷⁹ 'Flying in Circles', *The Economist*, July 15th 1999