IATA submission in response to European Commission consultation on EU Guidelines on State aid to airports and airlines

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This submission presents the response of the International Air Transport Association (IATA). IATA’s mission is to represent, lead and serve the airline industry and brings together over 240 member airlines comprising 84% of scheduled global air traffic.

IATA welcomes the opportunity to provide comments on the Commission’s proposed new guidelines on State aid for airports and airlines. IATA also welcomes the Commission’s view that “State aid control in the airport and the air transport sectors should promote sound use of public resources for growth-oriented policies, while limiting competition distortions that would undermine a level playing field in the internal market, in particular by avoiding duplication of unprofitable airports and creation of over capacities”.

Although the guidelines represent a positive step towards the achievement of this goal by providing specific rules under which state aid could occur, we have identified crucial areas of concern that must be addressed before the final guidelines are published at the end of this year. Otherwise the current severe impediment to competition between the airlines at the various airports would not only continue, at the expense of European consumers, but any past illegal behavior which has occurred could be considered legitimized. In summary, our main concerns relate to the following points:

General aspects:
- The need to have clearer guidance on the MEO test, and the potential need for the Commission to be notified when this test has been carried out.
- The need to clarify how these guidelines will be applied in cases of airport networks and airport systems.
- The need to amend the definition of the catchment area (distance & time indicative values)
- The need to ensure that these guidelines do not put civil aviation at a disadvantage against other modes of transport.
- A clearer guidance on how States should be dealing with non-economic activities.
- The need to include freight airports in the scope.

Investment aid:
- The need to allow investment aid, including at major European airports, to provide support for airport infrastructure when private investment is unable or inadequate to facilitate the development of efficient and cost-effective infrastructure and/or when there are extenuating circumstances.
- The need to take airport capacity into account when classifying airports and determining the amount of aid to be allowed
- The need for clarification of paragraph 96 to determine whether aid should be paid back if actual profitability proves to be better than the forecast in the ex-ante analysis

Operational aid to airports:
- The need to reduce the operating aid transitional period to 3 years
- The need to disallow airports above 500 thousand passengers from operational aid (even within the transitional period)

Aid to airlines:
- The need to ensure that airlines are not discriminated independently whether or not they are benefiting from the aid.
- An airline receiving start-up aid should return such aid if it ceases operating this new route before the 24 month period
- Start-up aid should be limited in time
- Start-up aid should be only allowed at airports with lower than 1 million passengers

Applicability of the new guidelines:
- The new guidelines should not be applicable to already granted operating aid and pending cases. These should be assessed under the current guidelines of 2005.

These concerns are further detailed below:

A) General Aspects

- Market Economy Operator test: further guidelines are needed on how the Market Operator Test should be carried out (with specific examples applicable to the airport environment). This would ensure that the test is carried out adequately and consistency across all States applying it. Our fear in particular is that if the new guidelines are to be applied to existing cases of operating aids to airports (passed through to airlines), the MEO test (as defined in sections 3.5.1 and 3.5.2 of the draft) will either be impossible to pass (no possible comparison with market prices), or be quite easily satisfied (ex-ante profitability analysis: incremental cost is not the right criteria when a whole airport infrastructure has been built for just one airline in some extreme cases); as a consequence, those airlines having benefitted from these aids will not be considered as having received aid, which in our view would be unfair for their competitors. This is also the reason why we plead in point 4 below for the non-applicability of the new guidelines to pending cases.

As a further measure for ensuring that the MEO tests are consistently applied, the Commission should, for a period of time, request States to notify the Commission on all the cases in which this test has been applied at least at airports that were not profitable (for the moment, States are only required to notify the Commission when aid has been granted, not when the MEO test was applied to determine whether there is state aid or not).

- Network charges: the Commission does not make any mention as to how the guidelines will apply to an undertaking that has a network of airports (particularly, situations in which charges at each individual airport do not bear any relation to the costs of these airports).

The Commission should assess whether state aid exists at each individual airport in the network. If this approach is not followed, significant distortions of competition could arise especially because users at other airports of the network would cross-subsidize these airports. For this same reason (cross-subsidization), IATA is against the principle of network charging.
- **Catchment areas:** the recommended travel time should be in line with the one determined in EC Regulation 1008/2008, Art. 19 para 2 b) and should therefore be increased to 90 minutes. Accordingly, the distance factor should be amended to 150 kilometers.

- **Aid at other modes of transport:** we welcome the Commission’s decision to review the existing guidelines on State aid to airports and airlines. We also welcome the fact that the Commission is pursuing a level playing field by securing a market with undistorted competition. However, this level playing field should be extended to other modes of transport. Should state aid exist for other modes of transport (for instance railways), particularly between cities in which airports do not qualify for state aid, then the Commission should take the necessary steps in order to ensure that civil aviation is not in a unfair disadvantage against these other modes of transport.

- **Non-economic activities:** although it is indicated that only economic activities are covered in these guidelines, extra care is necessary on how States decide to support non-economic activities. At least, such an approach should be the same across all locations at the same state (i.e. a State should not support a reduction of a terminal navigation charge at one airport, while all other airports in the State pay full charge. Support should be consistent).

- **Scope of application of the guidelines:** airports that specialized in freight transport are beyond the scope of the guidelines (which would be applied on a case-by-case basis). Because some cargo airports may receive large amounts of State aid and then be converted in passenger airports, and because some airports may have a primary cargo function but also handle a few passenger schedule flights, IATA suggests that freight airport be subject to the guidelines.

- **Compatibility of aid under Article 107 3 (c):** in its assessment under Article 107(3)(c) of potential negative side effects it is important to take into account system wide impacts from any subsidies:
  
  - **Considerations due to economies of scale:** size thresholds of eligibility (the ones currently proposed in the consultation are arbitrary) for subsidies may discriminate against certain types of operating models despite being more efficient at providing connectivity, particularly in the case of airports. This may create dis-incentives to further enhance economies of scale where such opportunities exist, which may impact air transport through promotion of less efficient connectivity. This may also have adverse impacts on sectors that are not direct users of air transport. For instance, potentially agglomeration benefits in the vicinity of other airports (especially major ones) may be foregone within the EU.

  - **Consideration due to economies of density:** in addition to distortive impacts on direct alternatives/competition, subsidies can have unintended consequences and complex impacts when considering network characteristics of the air transport industry. To illustrate this case a simplified hypothetical example is
presented from the airline sector. If locations A and B are currently connected only through a hub airport (no direct connection) in location C. Subsidizing an air connection between A and B to the point of making that connection commercially viable can result in the connection between A and C becoming commercially non-viable, which could potentially have more adverse impacts on air connectivity for location A then the addition of a direct flight to location B.

- **Assessment of competition:** the draft guidelines (paragraph 40) suggest that competition between airports and airport managers can be assessed in light of airlines’ criteria of choice, in particular by comparing factors such as type of airport services provided and the clients concerned, population or economic activity; with the charge level being a key factor.

Airport competition is complex to assess and is driven by many factors that may include location, services offered, airline considerations, passenger preferences and other factors. While it may be that in some cases the presence of subsidies can distort competition, especially in the long term, there are several factors that make competition among airports, especially major airports, inefficient. Factors that explain inefficient competition among airports, especially major airports, are location specific catchment areas, switching costs of airport users, capacity constraints, and other factors that make it difficult to have substitutable alternatives. However, even in cases where there is limited distortion in direct competition within the airport sector, the subsidy can result in distortion of consumer choice in the transport sector and the economy as whole. Also, even in cases where subsidies are not distortive for airport competition they may result in inefficient functioning and development of air transport.

**B) State Aid to airports**

1) **Investment aid to airports**

In addition to improving airport operating efficiency, IATA’s well-known view is that one way to address scarce capacity and growing demand in Europe, in particular at major European hubs, is to ensure the timely building of efficient infrastructure. This view has most recently been put forward on the occasion of the revision of the slot allocation regulation.

Allowing Member States to provide support for airport infrastructure when private investment is unable to facilitate the development of efficient and cost effective infrastructure and/or when there are extenuating circumstances (including financial crisis, natural disaster, war, etc.), should be part of the EU long term transport strategy.

Investments in air transport infrastructure are often characterized by peaks, which may create transitional differences in costs and services which in turn may prohibit the development of efficient infrastructure. Public sector participation can address market failures that may arise as result of these characteristics. Extenuating circumstances may also create the need for public intervention. The use of subsidies should ensure
the development of efficient airport infrastructure and an efficient air transport network provided it is aligned with ICAO policies, creates minimal market distortion and is in strict adherence to state aid conditions.

- Airport thresholds: It is not clear which source has been used for creating the 5 categories of airports. Further details are necessary in order to support the Commission's view. Application and/or eligibility of subsidies needs to be outcome driven where the most effective approach is pursued to "contribute to a well-defined objective of common interest in the absence of market delivery of that objective" and is in strict adherence to state aid conditions.

- Criteria for banding airports: the Commission is currently proposing the usage of number of passengers for classifying the amount of aid that airports could receive. If the aid is given in order to expand the capacity of airports, then consideration should be given to the future capacity at the airport, and not to the existing number of passengers. If the aim of the Commission is to avoid the creation of unnecessary and inefficient overcapacity at airports, then bandings which also have a relation to capacity will provide the incentives for adequate airport planning.

- MEO test: the FAQ to the guidelines indicate the MEO test could be applicable when analyzing public funding on infrastructure. Public funding in the form of "grants" would not pass the MEO test, as by definition, investment related to grant money is not expected to earn a return.

- Ex ante test: does paragraph 96 only cover cases of repayable advance or all cases of investment aid? If it does not apply for all cases, aid should be given back to States where the actual figures proved to be better (in terms of profitability) than that forecast in the ex-ante analysis.

2) Operating aid to airports

- Applicability of Operating aid: if the existing guidelines do not support the existence of operating aid, it is unclear as to why the Commission is now proposing a 10 year period to airports for its removal. Such actions provide a precedent and a perverse incentive for not following EC guidelines.

- Duration period for the removal of operating aid: a 10-year period for the removal of operating aid is too long (considering that the current guidelines already disallow it). As the Commission itself indicates, operational aid creates a significant distortion to competition. As such, the transitional period allowed for such removal should be, at a maximum, for 3 years.

- Incentives and differential charges: public funds earmarked for supporting airport operations should not be used in such a manner as to distort competition between airlines operating to/from the same platforms: differential charges and incentives must
always be provided in an equal manner to the airlines operating to/from an airport and must comply with the criteria of non-discrimination.

- Devolution of operating aid: as operating aid will be defined on the basis of an ex-ante analysis (and assigned via lump sum), aid should be paid back if the cost coverage actually needed is lower than that forecast ex-ante basis.

- Airport size: again, as operating aid is being identified as one of the largest distortions to competition, operating aid should only be allowed (during the transition period) towards airports with less than 500 thousand passengers..

C) State Aid to airlines

- Length: the current guidelines do not clearly specify any time limit to start-up aid. As this is aid solely to “start up” an operation, it should logically be limited in time. As the guidelines indicate that the route should be profitable for the airline within 24 months, then the aid should also be limited to this timeframe (or 3 years, maximum)

- Airport size: start up aid to airlines should be limited to airports with passengers below 1 million.

- Airline eligibility: the aid should be made available to all airlines.

- Incentives: in order to avoid any perverse incentives, an airline receiving start-up aid should return such aid if it ceases operating this new route before the 24 month period.

- Paying for aid: when analyzing aid provided to an airline, the Commission must make sure that airlines not receiving the aid are not actually paying for it.

D) Applicability of the guidelines

Application of the guidelines: the new guidelines should not be applied to existing cases of operating aid. Such cases should be assessed under the current guidelines. The 2005 guidelines on operating aid to airlines were clear and sufficient to close the pending cases. Therefore we suggest that paragraph 125 be redrafted in the sense of confirming that the notice published on 22 may 2002 is applicable.

A retroactive application of the new Guidelines would violate European rules of law and contradict the judicature of the European Court of Justice (C-74/00 P, C-75/00 P and T-92/11), since the mandatory legal requirements for a retroactive application are not met.
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