September 2013

Event Notes

Citizens, Aviation & Competition

Context

Transport & Environment hosted a seminar on Monday 16 September to discuss the new draft guidelines on State aid to airports and airlines. The Agenda included aviation campaigners, experienced aviation State aid lawyers and the department of the European Commission responsible for the guidelines. The seminar was run under the Chatham House rule. Thus no statements will be attributed to individual participants but this note will broadly set out the issues discussed

Why T&E hosted the seminar

Transport & Environment have discovered that the amount of aid given to airports and airlines every year across the EU is roughly €3 billion. With the Emissions Trading system for aviation being cut down dramatically, subsides given to the industry become more of a focal point for the environmental issues created by the industry. The European Commission published new guidelines on when and how State aid can be given to the aviation industry on 3 July and they are open to public consultation until September 25.

The regulation of State aid for airports & airlines was originally the prerogative of DG Move, the transport department of the Commission. It was moved to DG Competition, responsible for competition in the internal market at the beginning of the last Commission term.

There is unfortunately no published Impact Assessment that can be discussed to understand the economic underpinning of these guidelines better.

Current Situation

There are approximately 60 cases pending against airports and airlines. 25 are formal investigations, opened as early as 2007. These cases are essentially ‘on-hold’ until the new guidelines are finalised.

The current guidelines date from 1994 and 2005. In 1994 the low-cost model was unknown and the 2005 guidelines were introduced to reflect the 2004 Ryanair/Charleroi decision. The current revision of the guidelines is to coincide with the general State Aid Modernisation Package which has the tag-line ‘less and better targeted aid’. It was suggested that taking resource efficiency into account with this revision of the aviation guidelines would bring them further in line with the State aid rules for other sectors. In general it was stated that there is a level playing field for aviation in terms of legislative density.

What is State aid?

State aid rules essentially prohibit Member States from subsidising industries in any way that would distort the internal market within the EU. The general rule is stated in Article 107(1) of the Treaty on the Functioning of the European Union (TFEU): “any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market."

However, the EU Commission can authorise such aid. For this the potential aid measure must be notified to the Commission and they will then investigate to decide whether to allow the aid or not.

Another way that the aid can be given is if it is given on the same terms that a rational private investor would have accepted. Essentially, this means that if the aid is given on market terms, it is not state aid at all, but rather the Member State concerned is simply acting as any other market operator would do. For aviation this means that airports should be able to prove that they will be able to make a commercially acceptable return on investment within a reasonable time.

However, it was noted that the private investor test is very artificial as if aid is really granted at the same rates that a private investor would accept, then there should be an available private investor, rather than run the investment risk with public money. If it is really going to be profitable then why is there no investor?

There is also a carve out for Services of a General Economic Interest (SGEI) where a Public Service Obligation (PSO) can be imposed upon airlines or airports to maintain vital transport links. These links are essentially for isolated or outer-most regions of the EU where no other form of transport is available.

It is difficult to draw a clean line on when and where a service is necessary for an area to ensure that the economy prospers. It is easy to say that an airport is important in almost every area. However it was also noted that there must be coordination of airport locations, at least at national level as otherwise it can lead to the situation where every local region develops their own airport, duplicating infrastructure which often leads to subsidisation by the local authority.

Notification

Under Article 108(3)(3) of the TFEU, Member States are obligated to notify the Commission of any plans to grant State aid. They are then required to put the proposed measure on hold until the Commission has come to its final decision on whether to allow the aid or not. Indeed one of the reasons the Commission wishes to be able to streamline the rules with the current update is to be able to take quick decisions when they are notified of potential State aid.

Under the notification procedure, public authorities must provide all necessary information to the Commission to make its decision including: ex ante business plan, profitability analysis, counterfactual analysis/incentive effect and evidence that the aid is proportionate.

Under the new draft guidelines Member States would not need to notify the Commission of every airport but only the most distortive.

There is an obligation to repay illegal State aid with interest where it is granted without notification and or approval of the Commission. But there can also be consequences under national law and any relevant contracts may become invalid. Essentially the obligation to repay forces Member States to take aid back against their own intensions.

What do the new guidelines provide?

The new guidelines are only guidelines. This means that while the Commission will assess any aid given in light of the guidelines, ultimately if a case goes to court, the Court of Justice of the EU will apply primary (the Treaties) and secondary (Regulations and Directives) legislation first and disregard the guidelines if they decide they do not accord with the Treaties or secondary legislation. However, because the guidelines exist, airports feel obliged to comply and without their guidance a lot of commercial uncertainty would exist.

Under the old guidelines, the decision of whether to allow aid was often on the basis of a case-by-case assessment. Sometimes grants of aid to airports with 100% aid intensity were approved (i.e. where the airport did not provide any money to cover its costs). The new guidelines divide up potential aid into 3 types with different rules for each: Investment, Operating and Start-up.

Investment Aid

This type of aid applies to capital or infrastructure costs. Under the new guidelines, the amount of aid allowed varies as a percentage of the overall project cost, based on the number of passengers the airport serves. The smaller the airport, the higher the percentage of aid it can receive. To receive aid under this heading, the airport must demonstrate that the investment would ensure capacity at the airport will be able to meet medium term needs. Under the new guidelines, no aid should be given where there is another airport within the catchment area of the airport looking for aid. However it was pointed out that it seems that the rule should not be that the catchment area does not contain another airport but rather that the catchment areas of two airports should not intersect.

Operating aid

Operating aid is essentially aid to cover the day-to-day operating costs of an airport. This is potentially the most controversial area of aid. This is where the aviation sector seems to be getting the most differential treatment from other sectors e.g. operating aid is usually held to be a very distortive form of aid only allowable in extreme cases. However, the Commission proposes to allow this aid for a maximum period of 10 years after the new guidelines come into effect and allow such aid with retroactive effect (e.g. excuse past grants of illegal aid). During the 10 years where aid is allowed, it must be reduced by at least 10% a year on average. But the 10 year period is a maximum so that where an airport is already meeting 60% of its cost coverage, it will only have 4 years to phase out operating aid (i.e. it needs to phase out the aid by 10% a year and it is currently receiving 40% aid).

The view was that enforcing the old guidelines would lead to the closure of a number of regional airports. However, an alternative view was expressed that as smaller airports haven had a much higher growth rate across the EU, withdrawing State aid to these smaller airports would simply level the playing field and close the disparity in airport fees (with the smaller airports having the lowest fees currently), allowing larger airports to compete on a level playing field.

The idea behind operating aid is that it provides a consumer benefit in improving mobility. However that idea was contrasted against the idea that a consumer benefit can be taken as a given but it must be proven that it feeds into the wider economy.

The Commission will decide whether operating aid is allowed on the basis of a business plan provided by the airport. The business plan is not public and cannot be challenged by the public.

Start-Up Aid

This was rarely used due to complexity of the rules on receiving this type of aid so an attempt has been made to simply the conditions. The new proposal is to allow this type of aid for at most 2 years and only to 50% of costs. The eligible costs are those related to starting up a route, e.g. marketing.

Wider Aviation Issues

Restructuring aid to airlines was discussed briefly but it was noted that these grants of aid come under different rules and so are not relevant to the new draft guidelines. But noting this form of aid is necessary to get a good overall picture of the aid that goes to the aviation sector as a whole.

There is no VAT or fuel tax on aviation. This could be an extra €39 billion a year for Member State governments and could be seen as an indirect subsidy to the aviation industry. In addition, a number of people at the seminar questioned whether aviation pays for the environmental and health costs it causes.

The question was asked that if State aid does distort the market then is it beneficial to distort the market? The longer State aid continues, the harder it will be for it to be withdrawn. Subsidies are generally suboptimal and can lead to smaller growth in other areas. There is not necessarily net economic growth from the provision of a subsidy. The question has to be asked of every airport receiving a subsidy as to whether it is really essential for the local economy. Also, what would be the cost to the local economy if it shut down? The New Economics Foundation (NEF) are currently carrying out such a study (to be released in November) to find out the cost to the London economy of the closure of City Airport, and the potential benefits that could be created from using the current airport space for a different commercial project.

There are wider subsidy issues with a number of airports. The example was given of Heathrow, where much money was spent on improving the motorway when a new terminal was built but that was not classified as a subsidy to aviation. Similarly, planning permission can be worth millions in certain areas but is not classified as a subsidy.

Timeline

The Commission started the process of revising the guidelines in 2011. There is no formal consultation with the Member States or Parliament. Everyone is invited to fill out the public consultation. It is no definite date for the release of the final updated guidelines.

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