

# EUROPEAN COMPETITION LAWYERS FORUM (ECLF)

## COMMENTS ON THE DRAFT COMMUNICATION FROM THE COMMISSION

### EU GUIDELINES ON STATE AID TO AIRPORTS AND AIRLINES

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#### **INTRODUCTION**

This paper is submitted on behalf of the European Competition Lawyers Forum (the “ECLF”) in response to the European Commission’s public consultation on the Draft Communication setting out the EU Guidelines on State aid to airports and airlines (the “Draft Guidelines”). The ECLF is a group of practitioners in competition law from around 80 law firms across the European Union.

This paper has been compiled by the ECLF State Aid Working Group (the “Working Group”) (Peter Alexiadis, Paris Anestis, Bertold Bar-Bouyssiére, Jose Luis Buendia, Jacques Derenne, Edurne Navarro Varona, Nina Niejahr, Ulrich Soltész, Isabel Taylor) and does not purport to reflect the views of all ECLF members. While the paper has been circulated within the Working Group for comment, its content does not necessarily reflect the views of the individual members of the Working Group or their law firms.

#### **GENERAL COMMENTS**

Overall the Draft Guidelines represent a welcome initiative, as it provides an opportunity to review the 2005 Aviation Guidelines and to take into account the significant developments that transformed the sector over the past 8 years. The numerous cases in which the Commission had to assess, under the European Courts review, the State aid to the sector, has also considerably affected the applicable legal framework.

As a result of these evolutions, the Commission proposes to introduce a new approach to the assessment of compatibility of aid to airport and airlines, with the aim of better addressing the specificities of the sector.

The Commission proposes a balanced approach deemed to be neutral *vis-à-vis* the various business models of airports and airlines.

The Draft Guidelines concentrate on State aid to airport and airlines in relation to passenger air transport. Airports and airlines specialised in the freight transport are excluded from the scope of the guidelines (point 20). The Draft Guidelines do not apply to the provisions of ground handling services where they are offered by airports or airlines themselves, although these services are relevant to the Commission’s assessment<sup>1</sup>.

The Commission emphasises the need to ensure consistency of these rules with the legal framework introduced in the context of the State Aid Modernisation (“SAM”). The overall coherence with the State aid instruments is crucial, although the current draft would probably deserve some refinements in that respect.

#### **SPECIFIC COMMENTS**

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<sup>1</sup> SA.33337 – Possible aid to LOT Polish Airline.

## 1. NOTION OF UNDERTAKING AND ECONOMIC ACTIVITY

The Draft Guidelines essentially take account of the learning of the *Leipzig-Halle* case law and confirm the inclusion of construction of airport infrastructure in the scope of airports' economic activities. This case law departs considerably from the approach of the 1994 Airport Guidelines whereby "*the construction or enlargement of infrastructures projects (such as airports, motorways, bridges, etc.) [were deemed to represent] a general measure of economic policy which cannot be controlled by the Commission under the Treaty rules on State aid*".

The Commission proposes to set a switching date between this "new approach" and the way financing measures to airport infrastructure were assessed in the past. The Draft Guidelines states that "*before the 'Aéroport de Paris' judgement [12 December 2000], public authorities could legitimately consider that the financing of airport infrastructures did not constitute State aid*". The relevance of this distinction in time is however questionable in light of the state of legal uncertainty which prevailed before the entry into force of the 2005 Airport Guidelines as regards the economic nature of the construction of airport infrastructure. The isolated nature of the 'Aéroport de Paris' judgement, which addressed a legal issue bearing no relation with the financing of airport infrastructure and which was not confirmed by the Court before the Leipzig-Halle case in 2011, prevented that judgement from being considered as directly binding for the Member States on the financing of airport infrastructures, especially since the Commission indicated precisely the opposite in the 1994 Airport Guidelines, in force at the time, and reversed its position for the first time only in 2005 when it adopted the 2005 Airport Guidelines. The Draft Guidelines should therefore favour the application of the "new approach" with respect to airport infrastructure as from 2005 at the earliest, and not 2000.

The relevance of this distinction in time is also questionable in light of the 10 year limitation period set out in article 15 of the Procedural Regulation with regard to the Commission's scrutiny on unlawful aid. Points 25 and 26 of the Draft Guidelines do not bring any real guidance and therefore should be deleted. Moreover the statement under point 26 is ambiguous and leaves room for legal uncertainty: "*Conversely, before the 'Aéroports de Paris' judgment, public authorities could legitimately consider that the financing of airport infrastructure did not constitute State aid, and accordingly such measures did not need to be notified to the Commission*" (emphasis added).

On the contrary, regarding the definition of existing aid pursuant to Article 1 (b)(v) of the Procedural Regulation, inclusion of a definite point in time would have enabled to define with more legal certainty the period "*before any competition developed in the airport sector*".

Indeed, the liberalisation of European air transport was achieved in four stages:

- i) In 1987 with the first package of liberalisation measures, fare restrictions were reduced; carriers were also given additional flexibility for cooperation within the limits of existing air service agreements;
- ii) In 1990 with the second package of liberalisation measures, all European airlines to carry passengers to and from their home countries to other EU Member States (3rd and 4th freedoms); freedom flights, i.e. intra-European flights with stop-over in a third country and the right to pick-up and drop-off passengers during the stopover, were allowed to a greater extent; fare and capacity restrictions were further abolished;

- iii) In 1993 the third package of measures, including the common licensing of carriers and freedom of access to the market, was introduced. All carriers holding a community license were allowed to serve any international route within the European Union; finally, carriers were given almost full freedom to set fares;
- iv) In 1997, as part of the third liberalisation package, all carriers holding a community license were given the right of cabotage, i.e. the right to operate domestic routes within the whole of the EU.

Against that background, the Draft Guidelines should define a precise date (1987, 1990, 1993 or 1997) beyond which an aid measure should be defined "new aid". Moreover, any consideration on existing aid is not justified under section 3.1, as this section deals with the notion of undertaking and economic activity. There is a fundamental difference between the assessment of a measure as "no aid" and the assessment of an aid as "existing aid". The section should better highlight this difference to avoid any confusions.

Moreover, the scope of the *Leipzig-Halle* judgment should be qualified, contrary to the current wording of the Draft Guidelines. It cannot be inferred from this judgment that all transport infrastructure will automatically fall under the remit of State aid rules. A distinction between the construction and the operation is not always relevant in that respect. Besides the situations foreseen under points 31 and 32 of the draft guidelines, there is a need to examine whether the new infrastructure (or an extension of it) serves, by its nature or purpose, the exercise of an economic activity, rather than the exercise of State authority. Arguably, the dividing line may be thin in certain cases (ex. regulatory fire-prevention facilities for example), as such activity can be linked, by its nature and purpose, to the exercise of an economic activity (the commercial use of a transport infrastructure). Due to this link the activity will also be considered as economic and therefore will be caught by the State aid rules.

In paragraph 32, the Draft Guidelines identify airport's activities such as air traffic control, police, customs and activities necessary to safeguard civil aviation against acts of unlawful interference, as non-economic activities falling outside the scope of the rules on State aid. A clarification of the scope of non-economic activities at airport, for instance as to whether it includes activities such as fire protection or wildlife hazard (which are considered as non-economic activities in some Member States), would be welcome.

In paragraph 33, the Draft Guidelines make a confusion between Services of General Interest ("SGI") and ("SGEI"), which deprives the notion of SGI from its *raison d'être*. The Draft Guidelines states that "*any possible overcompensation by public authorities of costs incurred in relation to non-economic activities may constitute State aid*". The concept of overcompensation merely relates to the notion of SGEI and not to activities consisting of the exercise of its official powers as a public authority. As indicated in point 32, activities that fall under the State responsibility in the exercise of its official powers as public authority (such as air traffic control, police, customs and security) are not subject to State aid rules and therefore the Commission should not have the possibility to assess the existence of an overcompensation in such a case (nevertheless, the Commission could presumably control the absence of cross-subsidies between non-economic and economic activities, which requires overcompensation of non-economic activities in the first place).

2. **THERE IS A RISK OF ENTERING INTO A COST/REVENUES JUSTIFICATION AND EFFICIENCY ASSESSMENT FOR ACTIVITIES WHICH CONSTITUTE THE EXERCISE OF A STATE AUTHORITY.PUBLIC FUNDING OF AIRPORT AND THE APPLICATION OF THE MARKET ECONOMY OPERATOR PRINCIPLE**

Point 37 of the Draft Guidelines concentrates on the use of public resources. In Section 3.1 of the Draft Guidelines, the Commission indicates that airport managers also carry out economic activity and generate commercial revenues from these activities. In general, the Draft Guidelines should better differentiate between these two sources of revenues (public and commercial revenues).

A clarification of the notion of the MEOP in the context of airport managers is appropriate as it is the consequence of the fact that airports, even when publicly owned are often managed on a commercial basis and the EU Treaties are neutral as between public and private ownership (Article 345 TFEU). However, it is unclear whether the notion of MEOP should be understood as being similar to the MEIP, which is the test that has been elaborated by the case law. The notion of MEOP is an innovation of the Draft Guidelines and its scope should be better clarified.

Point 46 states that the Commission will assess “*whether such funding constitutes aid by considering whether in similar circumstances a private operator, having regard to the foreseeability of obtaining a return and leaving aside all social, regional-policy and sectoral considerations*” (emphasis added). The test proposed in the Draft Guidelines is at odds with the case law which refers to “*a higher return or a lower risk compared with the next-best alternative use of capital*”<sup>2</sup>.

In addition it is important that the Draft Guidelines put emphasis on the recent *Edf* case confirming the effect-based approach of the MEIP test (or MEOP as the case may be)<sup>3</sup>. The case would provide essential guidance to the airport operators which may use measures specific to public authorities in the exercise this function.

The Draft Guidelines refer to airport revenues as defined in its Annex 1. The definition of "airport revenues" provided in this Annex is not easy to handle, as it mainly contains exclusions (and therefore this definition does not provide sufficient guidance). On the definition of revenues, it is questionable to exclude revenues derived from non-aeronautical activities from the scope of revenues. The reason for such an exclusion is unclear as it is hardly understandable why they constitute commercial revenues of a different nature.

3. **DEFINITION OF A SERVICE OF GENERAL ECONOMIC INTEREST IN THE AIRPORT AND AIR TRANSPORT SECTORS**

In point 65, the Draft Guidelines restrict the possibility for the overall management of an airport to be considered an SGEI to the case where “*the area potentially served by the airport would be, without the airport, isolated from the rest of the EU to an extent that would prejudice its social and economic development*”. This interpretation, which further restricts the possibility to consider airport management as an SGEI in comparison with the previous 2005 guidelines, infringes upon the States’ margin of discretion to define an SGEI, and fails to take into account the importance of small airports in the local economy of several Member States, as explained in more details below. The Draft Guidelines

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<sup>2</sup> Commission decision of 20 October 2004 on aid from Germany for Westdeutsche Landesbank – Girozentrale (WestLB), now WestLB AG, OJ (2006) L307/22, para. 215. See also Joined cases T-228/99 and T-233/99 Westdeutsche Landesbank Girozentrale and Land Nordrhein-Westfalen v Commission [2003] ECR II-435, points 314 to 315.

<sup>3</sup> Case C-124/10 P, Commission v. Edf [2012] ECR n.y.r.

should leave open the possibility to consider the overall management of small regional airports (if necessary subject to a threshold) as an SGEI, which would apply not only to isolated airports but to all airports not exceeding that threshold.

#### 4. COMPATIBILITY OF AID UNDER ARTICLE 107(3)(C) OF THE TFEU

Section 5 of the Draft Guidelines represents one of the main parts (and maybe the most crucial part) of the Draft Guidelines. However, overall, the Section is poorly drafted and deserves a series of improvements, as the current drafting can be misleading:

The section presents a series of inaccuracies which would need to be corrected:

- (a) In point 70, the reference to point 61 with respect to measures granted to airlines which incrementally decrease the profitability is misleading as point 61 does not address this aspect (but the issue of economic activities carried out by airport managers or airlines as SGEI instead); this notion of measures which incrementally decrease the profitability of airlines is otherwise not defined in the Draft Guidelines;
- (b) In point 72, the Commission refers to 7 cumulative conditions to be fulfilled for a measure to be compatible with the internal market, whereas in reality it lists only 6 points; the missing point seems to be "access to the airport" referred to as point (g) in Section 5.1;
- (c) Point 73 indicates that "*if all necessary conditions are met, the Commission normally balances the positive effects of the aid measure in reaching an objective of common interest*" (emphasis added); the word "normally" creates some confusion as to whether the 7 criteria are sufficient for an aid to be declared compatible, as it seems to indicate that the Commission will nevertheless keep a margin of appreciation even though the 7 criteria are met; this approach is at odds with the principle of legal certainty;
- (d) Point 74 states that "*the Commission considers that the expected positive effects of aid outweigh its potential negative effects if all conditions as outlined in section 5.1 and 5.2 are met cumulatively*"; this wording is confusing as it seems to indicate that the criteria of Section 5.1 must be cumulated with the ones of Section 5.2; the point could be redrafted as follows: "*(...) if all conditions as outlined in each of the sections 5.1 and 5.2 are met*";
- (e) In the Section on the compatibility assessment of "aid to airports" (Section 5.1), the Commission elaborates on the 7 condition mentioned above:
  - (i) Under the first compatibility criteria, point 78 gives rise to some confusion; the Draft Guidelines indicate that "*in order to assess whether State aid is effective in achieving an objective of common interest, it is necessary to have a first diagnosis of the problem to be addressed*"; the meaning of this sentence is unclear and does not bring guidance on what the Commission intends to do; the point further states that "*State aid should be targeted towards situations where such aid can bring about a material improvement that the market itself cannot*"; this condition is in reality too restrictive as it in fact requires the measure to: (1) not only address a market failure (which would be the only relevant criteria to require under State aid rules), but also (2) bring a material improvement; only the first item is necessary to justify the measure; it is unclear why the measure should also "bring a material improvement" and what this notion covers; it is unclear what

should constitute a “material improvement” and whether this is to be linked to a balancing test between the potential distortions and benefits of the measure;

- (ii) In point 79, the Draft Guidelines refer to "smaller airports" indicating that these entities are generally facing more difficulties to access financing; as a general remark, the Draft Guidelines should define the different categories of airports according to their scale (small, medium, large) and how they reconcile to the categories identified in paragraph 80 (see point (iii) below);
- (iii) In point 80, the Draft Guidelines identify a series of airport categories and define their financial capabilities (ex. *"airports with up to 200 000 passengers per annum might not be able to cover to a large extent their capital costs and their operating costs"*); as the sector can be dramatically affected by external factors (natural disasters, geopolitical conflicts, etc.), the average should be calculated on a period which is broader than a year (for example *"airports with an average of 200 000 passengers per annum over a period of 3 years"*) to better factor the risk of fluctuations; the same remark applies to the *"forecasted demand of airlines, passengers and freight forwarders in the catchment area of the airport"* referred to in point 81; the Commission indicates that the new infrastructure will have to meet the demand as forecasted in the mid-term; this criteria should better factor the possibility of accidental fluctuations;
- (iv) In point 81, the Draft Guidelines stipulate that *"the duplication of unprofitable airports or the creation of additional unused capacity does not contribute to an objective of common interest" and that "if an investment project is primarily aimed at increasing capacity of an airport,... any initial investment, which does not have satisfactory medium-term prospects for use... of existing infrastructure in the catchment area, cannot be considered to serve an objective of common interest"*. The corollary of this approach is that after the transitional period, *"all airports must have reached full coverage of their operating costs"* (point 107). This approach assumes that small airports unable to cover their operating costs (i.e. airports with a traffic of less than 3 million passengers according to the Commission's typology in point 80) should remain the exception and that closing such airports would help other airports to reach their breakeven point. This approach appears questionable in so far as (i) it is based on (undemonstrated) assumptions on the existence of overcapacities in Europe and on the harm caused by such overcapacities; (ii) it assumes that traffic growth is the only desirable objective for small airports; and (iii) it ultimately favours a concentration of traffic on large regional airports - the efficiency and environmental-friendliness of which is not demonstrated. More importantly, the proposed approach fails to take into account the positive impact of small regional airports on the local economy, which go far beyond the direct profitability of the airport itself, and can be demonstrated by economic studies. The Draft Guidelines should therefore leave open the possibility to allow operating aid to small airports after the transition period based on the demonstration that the benefits of such aid on the local economy outweigh its costs.
- (v) In point 82, the Draft Guidelines indicate that the airport capacity will be used as a benchmark in the Commission's assessment of the contribution

of the aid measure to a well-defined objective of common interest; If an existing airport is not operating at or near full capacity, *"the Commission will have doubts as to the medium-term prospects for use of airport infrastructure at an airport located in the catchment area of an existing airport"*. This need to assess the likely effect of the investment on the use of the already existing infrastructure is coherent with the other Commission guidelines regarding the application of State aid rules to other industries<sup>4</sup> and this approach must be welcomed;

- (vi) Regarding the proportionality criteria, in point 90 the Commission proposes to introduce a test which defines the proportionate amount of aid, as *"the extra costs (net of extra revenues) which result from undertaking the aided project/activity instead of the alternative project/activity that the beneficiary would have undertaken in the counterfactual scenario"*; the test is acceptable as such, but it is to be noted that the test proposed for assessing the proportionality of the measure also covers the test suggested for determining its incentive effect (see point 87); both criteria should be therefore merged;
- (vii) With regard to the assessment of the negative effects, some precisions should be added in paragraph 95 respect the different categories of airports foreseen in point 92: "passenger traffic exceeding 3 million" should read "passenger traffic exceeding 3 million and below 5 million";
- (viii) In points 100, d) and 111, 2) the Commission uses the notion of catchment area for establishing a presumption of distortion of competition; the Commission sees a possible distortion when an aid is granted to *"an airport located in the same catchment area within 100 kilometres distance or 60 minutes travelling time by car, bus, train or high-speed train from an existing airport"*; putting all types of transports on the same level and using both *"100 kilometres and 60 minutes"* may lead to some difficulties in applying the principle; a unique unity should be used (time or distance) and a clear distinction should be made between the types of transport (at least between road transport and rail transport, where high-speed train should be clearly separated).

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<sup>4</sup> EU Guidelines for the application of state aid rules in relation to the rapid deployment of broadband networks, OJ C25, 26.01.2013, p.1.