



COMPETITION AND REGULATION UPDATE

COMMERCIAL NEGOTIATIONS FOR AIRPORT SERVICES IN THE UK SPARK A RECONSIDERATION OF AIRPORT MARKET POWER: HOW DOES AUSTRALIA COMPARE?

INTRODUCTION

In our August article on [recent developments in airport regulation](#), we considered the United Kingdom (UK) Civil Aviation Authority's (CAA) path to economic licencing of airports. To recap, the path is such that if an airport operator passes the market power test, it will be required to hold an economic licence to charge for its services. Recent commercial agreements with airlines made by Manchester Airport Group plc (MAG), owner of Stansted airport, have resulted in the CAA inviting submissions on how the relevant agreements may affect the market power assessment of Stansted airport currently being undertaken by the CAA. Certain types of commercial agreements with airlines may indicate that Stansted may not have the ability or incentive to exercise any market power sufficient to require regulation of the airport.

Similarly in Australia, the Productivity Commission's 2012 Report on "Economic Regulation of Airport Services" (Report) considered whether commercial negotiations between airlines and Australian airports suggested a need for more heavy-handed regulation. The Productivity Commission (Commission) found that commercial negotiations were preferred by most parties, but due to the "claim and counterclaim nature of the evidence", it could not make a definitive decision that greater regulation was required. The outcome of the CAA's consultation regarding Stansted airport may provide insight for Australian airports on the significance of commercial agreements for market power assessments and for the question of whether further regulation of Australian capital city airports is required.

STANSTED AIRPORT'S RECENT AGREEMENTS

Recently, MAG announced that it had made a long-term agreement with Ryanair to increase Ryanair's passenger numbers at Stansted from just over 13 million a year to nearly 21 million a year by 2023. Earlier this year, MAG also announced its long-term agreement with easyJet to more than double easyJet's traffic at Stansted.

In its "minded to" report on the market power assessment, the CAA acknowledged that its analysis of whether Stansted had sufficient market power to require further regulation could change over the longer term, for example if Stansted's change in ownership could establish different behaviours and relationships with airlines. MAG's recent agreements with airlines may be indicative of such behavioural changes. Stakeholders have been invited to submit representations on how these agreements may impact the market power assessment of Stansted airport, delaying the final proposals on the future regulation for Stansted from 1 April 2014.

THE PRODUCTIVITY COMMISSION'S REPORT

At the time of the Commission's Report, commercial negotiations had replaced price regulation of Australian airports for less than a decade, providing limited opportunities for parties to create new commercial agreements as normally Aeronautical Service Agreements are for five years. The Report considered airlines' assertions that commercial negotiations with some airports were one-sided and dysfunctional. The Commission said that due to the "claim and counterclaim nature of the evidence" it could not come to a definitive finding

on whether or not greater regulatory intervention was required. However, it did find that there was scope to improve commercial negotiations. The following table demonstrates some of the diverging views regarding the approach of airports to commercial negotiations:

Airline claims	Airport counterclaims and responses as summarised in the Report
Adopting a “take it or leave it” approach and dictating rather than negotiating.	<ul style="list-style-type: none"> ■ Airports cannot make new investments without the approval of airlines. ■ Airlines can and often do refuse to pay increased charges. ■ Airlines’ conflicting needs can cause disagreements about the provisions and pricing of common use services and facilities.
Having protracted negotiations and being unwilling to provide information.	<p>The Commission noted that:</p> <ul style="list-style-type: none"> ■ Airports provide substantial information under the building block framework. ■ Protracted negotiation can mean delayed investment for airports.
Unfairly transferring risk to airlines e.g. not responding to airlines’ increased risk during the Global Financial Crisis (GFC).	<ul style="list-style-type: none"> ■ Airports did renegotiate some terms of their commercial agreements during the GFC.
Not being amenable to resolving disputes.	<ul style="list-style-type: none"> ■ Virtually all commercial agreements have dispute resolution processes. ■ The parties’ differences can be so intractable that agreement cannot be reached. ■ Airlines sometimes pay for services whilst thinking the airport’s conduct is outside the Pricing Principles.

The Commission found that the dissatisfaction of airlines is not indicative of systemic failure as some airports were characterised as more reasonable than others. Despite the above claims, most parties agreed that commercial outcomes were preferable to heavy-handed regulation.

LESSONS FOR AUSTRALIA

The Report showed that for Australia with a system focused on commercial negotiations that had some level of constructive engagement, it would be “retrograde” to re-introduce heavy-handed regulation that could displace commercial negotiations and encourage gaming. That is, commercial agreements accepted by airlines indicated that Australian airports did not have the ability or incentive to exercise any market power to justify heavier handed regulation.

The CAA is now assessing the impact of MAG’s recent agreements with two airlines on the market power test and therefore whether or not Stansted should be subject to further economic regulation. The CAA’s reasoning will provide insights for Australian airports on when, despite the making of commercial agreements, airport conduct will warrant increased regulation.

Look out for our upcoming articles on the CAA’s decision regarding the future regulation of Heathrow and Gatwick airports and the outcome of the CAA’s assessment of the impact of Stansted’s recent commercial agreements.

MORE INFORMATION

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