

**Title:** Mild Turbulence and Crash Landings for Illegally State-Aided European Airlines

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### **Key points**

- In 2014, the European Commission introduced new Guidelines on State Aid to Airports and Airlines, which properly balance intra-regional travel and issues of unfair competition.
- In determining whether an act constitutes unlawful state aid, a distinction must be drawn between economic and non-economic activities. Though the former activities are properly regarded as constituting state aid, the latter may constitute such aid where the public authority overcompensates the costs incurred by the recipient.
- To determine whether an economic advantage has been achieved, the Market Economy Operator Principle is applied. This considers whether in similar circumstances, a private operator, having regard to the foreseeability of obtaining a return, would have granted the same funding.
- The imposition of greater publication requirements on Member States will facilitate greater transparency in decision-making.

### **Abstract**

As it relates to the European Union airline and airport sector, the desired goal of the European Commission is healthy competitiveness through the introduction of a level playing field. The clarity of the recent guidelines on state aid to airlines and airports will assist Member States and other public bodies in determining whether any public assistance falls afoul of the law; thereby distorting fair competition. Apart from imposing greater restrictions on investment aid and relaxing restrictions on operating aid, the 2014 guidelines, building on previous guidelines and case law, introduce the Market Economy Operator principle and clarifies the distinction between economic and non-economic activity. In addition to discussing these key concepts, the article, through a discussion of recent cases, shows the application of the Market Economy Operator Principle and is evidence of the Commission's determination to strike down and demand the return of any unlawful state aid.

#### **I. Setting the Context: Boosting intra-regional travel**

The importance of sustainable transport infrastructure is evident in its inclusion in the Europe Union 2020 Strategy. This issue of sustainability is even more poignant given the range of issues affecting the transportation sector, which include, general economic conditions

(recessionary concerns), competition from low-cost carriers, possible congestion at transportation hubs, fuel security, decarbonisation agendas and changing consumer needs (in particular, the availability of technologies which increase global connectivity and diminish the usefulness of travel). Though the European Union air transport sector linked over 840,000,000 passengers in 2013 to their destinations (Eurostat, 2014), the increasing air traffic (8% increase on 2011) has not been met with a corresponding increase in profits. Quite to the contrary, many EU airlines, including many flag-carriers, are being significantly impacted by an increase in competition, both from low-cost airlines and other more affordable forms of transportation, such as rail.

To turn this tide, many of these airlines have approached Member States for subsidies to boost their increasingly-slim profit margins. Much of this aid has been allegedly given under the threat of the removal of the carrier from that airport with the contingent implications on the profitability of the airport. It is well established under Article 107 on the Treaty on the Functioning of the European Union (TFEU or ‘The Treaty’) that any state aid, given through a Member State or its resources, which distorts or threatens to distort competition is prohibited. Prior to 2014, regulation for the air transport sector was provided by the combined effect of section 107(3)(c) of the TFEU, the Community guidelines for restructuring and restructuring firms in difficulty and the 1994 Aviation guidelines as supplemented by the 2005 Aviation guidelines. These provisions sought to shield the transport sector from the negative effects of unfair competition which would ultimately undermine the desirable level playing field. The increasing regulation and decreasing profitability has brought to focus a trade-off between boosting regional travel and issues of unfair competition, in particular where some of this aid has not been approved by the European Commission (as required). In this turbulent economic and regulatory state, in February 2014, the European Commission published new guidelines on State Aid to Airports and Airlines. These have been regarded by the European Commission as “a key ingredient for a successful and competitive European aviation industry”. These guidelines, which replace the 1994 and 2005 Aviation guidelines, anticipate and address the challenges which will face the airline sector within the two coming decades. This article will briefly consider the substance of the new guidelines and assess recent Commission decisions on state aid to airlines.

## **II. The Commission’s New Guidelines on State Aid to Airports and Airlines (February 2014)**

There are ten key elements of the new guidelines which will facilitate the movement of the air sector to a “successful” and “competitive” state of affairs. These simplified points are critical for airports, airlines and all relevant stakeholders. First, relying on ‘*Leipzig-Halle airport*’ judgment ([2011] ECR II-1311 at [93] and [94]), the Commission noted that, contrary to the approach taken in the 1994 Aviation guidelines, the activity of airlines which consists of providing transport services to passengers or undertaking constitutes economic activity. Thus, any such aid falls within the ambit of State aid control. Second, an important distinction must be made between activities of an airport which are of an economic and non-economic nature. Though only the former can be properly considered for issues of state aid, the latter must be strictly limited to compensating the costs to which they give rise and may not be used to finance other activities. Some examples include air traffic control, police customs, firefighting, activities necessary to safeguard civil aviation against acts of unlawful interference or the investment of any infrastructure and equipment necessary to perform these

activities. Though it may not be strictly regarded as state aid, any overcompensation by public authorities of costs incurred in such activities may constitute State aid.

Third, whether a measure can be properly regarded as imputable to the state as a public undertaking depends on a range of circumstances including the context in which it was given. The European Court in *France v Commission* [2002] ECR I-4397, termed the ‘*Stardust Marine*’ judgment, noted other relevant factors at [55] and [56]. These include its integration into the structures of the public administration, the nature of its activities and the exercise of the latter on the market in normal conditions of competition with private operators, the legal status of the undertaking (in the sense of its being subject to public law or ordinary company law), the intensity of the supervision exercised by the public authorities over the management of the undertaking, or any other indicator showing, in the particular case, an involvement by the public authorities in the adoption of a measure or the unlikelihood of their not being involved, having regard also to the compass of the measure, its content or the conditions which it contains.

Fourth, the resources of a public airport constitute public resources and thus any such airport may grant aid to an airline using the airport if the measure is imputable to the State (as determined under [3] above) and other conditions of Article 107(1) of TFEU are met. Fifth, at the heart of the Treaty is the issue of unfair competition. Whether this exists must be determined by a range of factors such as the airlines’ criteria of choice, in particular, the type of airport services provided, the clients concerned, population or economic activity (whether this relates to the area in which the service is established or the Member State as a whole is uncertain), alternative modes of transportation (such as access by land), charge level and overall conditions for use of airport infrastructure and services.

Sixth, whether an economic advantage has been achieved is determined by the Market Economy Operator Principle, MEOP (also referred to as the Market Economy Operator Test or the ‘test’). The test is 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, would have granted the same funding. Relying on *Italy v Commission* (‘*Alfa Romeo*’ judgment) [1991] ECR I-1 603 and *Westdeutsche Landesbank Girozentrale v Commission* [2003] ECR II-435, regard may also be had to, a comparison of the prospects of profitability in the longer term over the lifetime of the investment. The relevant information is limited to available information and foreseeable developments at the time when the public funding is granted and should not rely on analysis based on a later situation. In determining the satisfaction of the MEO test, the absence of a business plan may be an indication that the test is not met. This is indicative and not decisive as this void could be substituted by the provision of prior analysis or internal documents from the public authorities or airport concerned. No regional or policy consideration should be regarded in determining the satisfaction of the MEO test, though it may be relevant in assessing the compatibility of aid. If the MEO test is not satisfied, the Commission will determine whether the aid is compatible within the EU’s Single Market.

Eighth, where an airport has public resources at its disposal, aid to an airline may be excluded where the relationship between the airport and airline satisfies the MEO test. This is normally the case if the price charged for airport services corresponds to the market price (identification of a benchmark using comparator airports) or it can be demonstrated through an ex ante analysis that the airport/airline arrangement will lead to a positive incremental contribution for the airport. Ninth, there is some scope under the guidelines for the provision of start-up aid to airlines. To satisfy this, the state aid must contribute to a well-defined

objective of common interest (such as increase mobility and connectivity or facilitation or regional development of remote regions), there must be a need for state intervention, state aid is the appropriate policy instrument, there must be an incentive effect, the aid must be proportionate and there must be an avoidance of undue negative effects on competition and trade. [There is also leeway for investment and operating aid to airports but this article is primarily focussed on state aid to airlines.]

The tenth note-worthy point is the emphasis on transparency – thus, justice, fairness and reduction of unfair competition must be both done and seen to be done. To ensure transparency, the Commission requires that Member States should publish the full text of each approved aid scheme, the identity of the granting authority and the identity of the individual beneficiaries, the form and amount of aid to each beneficiary, the date of granting, the type of undertaking, the region and principal economic sector. This information should be freely accessible and retained for a minimum of ten years.

### **III. Recent decisions**

Below are some of the recent decisions of the European Commission with a special focus on allegations of illegal state aid to airlines. The court's seamless application of the market economy operator principle is noteworthy.

#### ***France: Angoulême – Cognac International Airport, Pau Pyrénées Airport and Nîmes-Alès-Camargue-Cévennes Airport***

In July 2014, the European Commission ordered Ryanair, a low-cost Irish carrier, to repay almost €10m in illegal state aid which it obtained from three French regional airports. This primarily related to rebates and marketing-related services. Ryanair was required to pay €800,000 to the first airport (as listed above), €2.4m to the second airport and €6.4m to the final airport.

As it relates to Angoulême - Cognac International Airport, the decision of the Commission was quite balanced: on the one hand, the Commission accepted that the financing provided was limited to compensating it for the provision of services of general economic interest. This facilitated the safe and viable air transport infrastructure in that region. Equally important was the fact that the nearest regional airport was 100km away. On the other hand, the court investigated the contractual rebates and marketing arrangements in 2008 between Ryanair and Airport Marketing Services (AMS) [a subsidiary of the airport]. Given that this arrangement would not satisfy the MEO test, they constituted state aid. On the issue of the satisfaction of this test, the court accepted that they could not be reasonably expected to improve the financial situation of the airport and no private actor, in a similar position, would have granted similar conditions. This was mere operating aid and could not be regarded as furthering the interests of the internal market. A similar conclusion was reached in relation to Pau Pyrénées Airport and the Nîmes-Alès-Camargue-Cévennes Airport.

#### ***Germany: Zweibrücken Airport***

In the midst of the insolvency proceedings of this German airport, the European Commission, on October 1, 2014, ordered Ryanair, which had stopped flying to this airport, since 2009, to repay €500,000 in illegal state aid. Ryanair has allegedly transported just over 50,000 passengers to this airport. A higher demand for the return of illegal state aid (€1.2m) was imposed on Germanwings (a subsidiary of Deutsche Lufthansa) for marketing and airport

services it had received. TUIFLY was also required to return €200,000 of illegal state aid. The Commission reached this conclusion having been satisfied that the market economy operator principle would not have facilitated the conclusion of these agreements given that these airlines were expected to generate more revenues than additional costs. Thus, no private operator would have concluded such loss-making agreements.

#### ***Italy: Alghero-Fertilia Airport***

The critical importance of considering the potential for undue economic advantage over their competitors is best understood by the contrasting outcomes of this October 1, 2014 decision. Both of the outcomes related to the operator of the Alghero airport, So.Ge.A.AL. On the one hand, the Commission concluded that agreements conducted with the airport operator and Ryanair/AMS, Aliytalia, Volare, bmibaby, Air Italy and Air Vallée could have been reasonably expected to improve the financial situation of the airport at the time they were entered and thus could not be regarded as giving any undue advantage. In contrast, the agreements concluded with Germanwings and Meridiana, constituted operating aid which could not be declared incompatible with EU rules.

#### ***Belgium: Charleroi Airport***

On October 1, 2014, the Commission also concluded that a number of measures granted by Belgium to Brussels South Charleroi Airport (BCSA), the operator of this airport, constituted State Aid. These measures included the concession fee which was lower than a normal market operator would impose. However, Ryanair, which has been credited, in part, with an increase of over 6.5 million passengers in 2013, was cleared of any receipt of illegal state aid. Having assessed its agreements with BCSA, the Commission held that these measures could not be properly termed state aid for two reasons: first, the measures could not be imputed to the State and, second, when granting the measures, the BCSA and Walloon Region behaved like a market economy operator.

### **IV. Going Forward**

It has oft been said that a word to the wise is enough. Even more important, is a clear word to the wise. The clarity and simplicity of the new guidelines should serve well when advising airlines or airports on the scope of any state assistance. As it relates to airlines, the regulations are balanced in facilitating start-up airlines and the development of existing airlines. Further, the detailed mandatory reporting will ensure that past decisions are transparent and open to scrutiny, thus ensuring that the healthy competition desirable in the transport sector, and the European Union as a whole, is achieved. The recent decisions of the European Commission are evidence that any state aid is open to scrutiny. Contrary to beliefs that some airlines may be targeted, the decisions focus on any state aid, not the airline, which facilitates duplication as this is simply a waste of taxpayers' money. This all inures to a conclusion that state aid guidelines in the air industry are flying in the right direction: later decisions of the court will continually add flesh to some of the uncertain provisions in the guidelines.