



ECA (European Competition Authorities) was founded in Amsterdam in April 2001 as a forum for discussion of the competition authorities in the European Economic Area (EEA) (the Member States of the European Community, the European Commission, the EFTA States Norway, Iceland, Liechtenstein and the EFTA Surveillance Authority).

ECA improves the co-operation between the competition authorities and contributes to the efficient enforcement of the respective national as well as European competition laws. Co-operation is developed, inter alia, through the organisation of meetings, the establishment of working groups and the exchange of information and expertise.

ECA set up an Air Traffic Working Group during the plenary meeting in Athens in April 2002 in order to improve co-operation between them with regard to their dealings with the airline industry and to seek to enhance competition in this sector. ECA considers that competition between airlines is influenced by some specific features of the airline industry, in particular its network character.

The paper on mergers and alliances in civil aviation is the result of discussions within the ECA Air Traffic Working Group based on the enforcement experience of the ECA members.



## **Report of the ECA Air Traffic Working Group**

### **Mergers and alliances in civil aviation**

- an overview of the current enforcement practices of the ECA concerning market definition, competition assessment and remedies**

**The competition enforcement practices described in the present document do not legally bind the members of ECA in any way and thus cannot form the basis for any legal action. The paper is the result of discussions within the ECA Air Traffic Working Group and does not have the status of an official notice or guideline published by one of the national authorities, the European Commission or the EFTA Surveillance Authority. Moreover, it should be stressed that each individual merger or alliance will be decided on a case by case basis.**

## 1. Introduction

1. The European Competition Authorities (ECA)<sup>1</sup> set up an Air Traffic Working Group during the session in Athens on 15 and 16 April 2002 in order to improve cooperation between them in relation to their dealings with the airline industry and to seek to enhance the present degree of competition in this sector. The ECA consider that competition between airlines is influenced by some specific features of the airline industry, in particular its network character.
2. The ECA Air Traffic Working Group has been considering ways in which the enforcement of competition law in the field of air transport could be improved through closer cooperation between the competition authorities. Following the 'open skies' judgment of the European Court of Justice on 5 November 2002<sup>2</sup> and in view of the ongoing consolidation process in the European airline industry and new market developments, high priority has been given to a more uniform and consistent application of the competition laws of the national states and the European Community with regard to mergers and alliances. This is particularly important with regard to (scheduled) air passenger services. Three key issues have been identified: market definition, competition assessment and remedies.
3. The purpose of the present document is to provide an overview of the current competition enforcement practices of the ECA with respect to alliances and mergers in the passenger air transport sector<sup>3</sup>. In covering the three key issues, identified above, the text takes into account the existing case law of the EC and of ECA members. Since the authorities' enforcement experience in the field of passenger air traffic is still limited, it must be emphasised that the present document does not address all questions that may arise in the assessment of an airline merger or alliance. Against this background, the ECA Air Traffic Working

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<sup>1</sup> The European Competition Authorities consist of the competition authorities in the European Economic Area (EEA) (the 25 Member States of the European Community, the European Commission, the EFTA States Norway, Iceland, Liechtenstein and the EFTA Surveillance Authority).

<sup>2</sup> Cases C-466/98, C-467/98, C-468/98, C-469/98, C-471/98, C-472/98, C-475/98 and C-476/98 against the United Kingdom, Denmark, Sweden, Finland, Belgium, Luxembourg, Austria and Germany. The judgment establishes that Member States acted illegally when they entered into agreements with the United States on several issues where Community laws are in place. The judgment specifically identified slots, intra-Community fares and computerised reservation systems as being matters of Community competence. The Court also found that Member States acted illegally in agreeing bilateral agreements that discriminate between Community air carriers on the basis of the nationality of their owners.

<sup>3</sup> I.e. Cargo services are not considered.

Group will modify or amend the present document from time to time as the authorities' enforcement experience develops further. In this respect the results of the industry dialogue on air transport competition policy launched by the European Commission on 14 April 2003 will be of particular interest.<sup>4</sup> The ECA Air Traffic Working Group expects that it will lead to further clarification in the assessment of mergers and alliances in the field of air transport.

## 2. Definition of terms

### 2.1. Mergers

4. For the purposes of this document, mergers are all operations which imply structural changes caught either by the EC Merger Control Regulation<sup>5</sup> or Article 57 of the EEA-Agreement, or by one or more merger control regimes of the national states.

### 2.2. Alliances

5. For the purposes of this document, alliances are cooperation agreements by which airlines integrate their networks and services and operate as if they were a single entity (but without the implied irreversibility of a concentration) while retaining their corporate identities (as in particular strategic alliances) and which are caught either by Article 81 (1) EC and/or Article 53 (1) of the EEA-Agreement or by the corresponding provisions in the competition laws of one or more of the national states. Cooperation agreements of this kind may comprise several or all of the following fields of cooperation: code sharing; revenue and cost sharing; joint pricing; coordination of capacities; route and schedule planning; coordination of marketing, advertising, sales and distribution networks; coordination of travel agents and other commissions; branding/co-branding; integration and development of information systems; information technologies

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<sup>4</sup> See at [http://europa.eu.int/comm/competition/general\\_info/airline/en.pdf](http://europa.eu.int/comm/competition/general_info/airline/en.pdf).

<sup>5</sup> Council Regulation (EEC) No 139/04 on the control of concentrations between undertakings, OJ L 24 of 20.01.2004, p. 1 (hereinafter: "EC Merger Regulation") ([http://europa.eu.int/eur-lex/pri/en/oj/dat/2004/l\\_024/l\\_02420040129en00010022.pdf](http://europa.eu.int/eur-lex/pri/en/oj/dat/2004/l_024/l_02420040129en00010022.pdf)).

and distribution channels; coordination of frequent flyer programmes; sharing of facilities and services at airports.<sup>6</sup>

### 3. Definition of relevant geographic and product market

#### 3.1. Introduction

6. A key element in identifying whether a merger or alliance will give rise to competition concerns is the definition of the relevant market.<sup>7</sup>
7. Generally, passengers purchase scheduled air transport services between a point of origin and a point of destination (O&D) as the basic product. As in other sectors the market definition has both a product or service dimension and a geographic dimension. However, as an air transport service has an inherent geographic dimension in itself, when defining the relevant market it is less useful to draw the line between the service dimension and the geographic dimension of air transport services.

#### 3.2. Existence of specific consumer groups

8. When taking a demand-based approach to market definition it may be necessary to make a distinction between different groups of passengers, given that different services may be substitutable for different kinds of customers.<sup>8</sup> It is particularly worth considering a distinction between time-sensitive and non time-sensitive passengers as well as between point-to-point passengers and connecting

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<sup>6</sup> See for example the description of the alliances between KLM and Northwest in the notice of the European Commission (OJ 2002 C 181/6) ([http://europa.eu.int/eur-lex/pri/en/oj/dat/2002/c\\_181/c\\_18120020730en00060008.pdf](http://europa.eu.int/eur-lex/pri/en/oj/dat/2002/c_181/c_18120020730en00060008.pdf)) and between Lufthansa/SAS/United Airlines in the notice of the European Commission (OJ 2002 C 181/2) ([http://europa.eu.int/eur-lex/pri/en/oj/dat/2002/c\\_181/c\\_18120020730en00020005.pdf](http://europa.eu.int/eur-lex/pri/en/oj/dat/2002/c_181/c_18120020730en00020005.pdf)). See also European Commission, case 37.730 - Lufthansa/Austrian Airlines (hereinafter: "Lufthansa/AuA"), OJ 2002 L 242/25, para. 53 ([http://europa.eu.int/eur-lex/pri/en/oj/dat/2002/l\\_242/l\\_24220020910en00250043.pdf](http://europa.eu.int/eur-lex/pri/en/oj/dat/2002/l_242/l_24220020910en00250043.pdf)). With regard to the evolution of different types of airline co-operations the outcomes of the European Commission's industry dialogue on air transport competition policy will be of particular interest.

<sup>7</sup> For a general discussion of market definition issues see European Commission, Notice on the definition of the relevant market for the purposes of Community Competition law, OJ C 372 of 09.12.1997 (hereinafter: "EC Notice on the definition of the relevant market") ([http://europa.eu.int/comm/competition/antitrust/relevma\\_en.html](http://europa.eu.int/comm/competition/antitrust/relevma_en.html)); OFT's market definition guidelines, OFT 403, 1999 (<http://www.of.gov.uk/NR/rdonlyres/972AF80C-2D74-4A63-84B3-27552727B89A/0/oft403.pdf>).

<sup>8</sup> See, for example, EC Notice on the definition of the relevant market, para. 43.

passengers.<sup>9</sup> The distinction between different types of customers reflects the established practice of the national competition authorities<sup>10</sup> as well as that of the European Commission.<sup>11</sup>

9. The distinction between time-sensitive (generally business travellers) and non time-sensitive travellers (generally leisure travellers) can be of great importance in the competition assessment.<sup>12</sup> Generally, time-sensitive travellers expect faster connections and a higher level of punctuality than non time-sensitive travellers. The former are not flexible in terms of departure and arrival time, and they expect to be able to change their reservations at short notice. Non time-sensitive travellers are interested in obtaining the lowest fares, and are willing to accept longer travel time and less flexibility. As data on whether passengers are time-sensitive or not is unavailable, appropriate proxies (e.g. passengers holding restricted/unrestricted tickets) have to be used (this issue is discussed in paras. 36 ff.).
10. The existence and the number<sup>13</sup> of connecting passengers has been an important factor in assessing competition on a specific O&D route in several cases, although it has not been the main focus of the analysis. In contrast to the situation of O&D (point-to-point) passengers, for connecting passengers a flight between two airports forms only part of their travel and the airport where the connection is made is neither their point of origin nor their point of destination. Connecting passengers and O&D passengers may thus belong to different

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<sup>9</sup> Though other distinctions between certain groups of passengers may be appropriate depending on the individual case (e.g. the preference for schedule flexibility of travellers).

<sup>10</sup> See e.g. UK Competition Commission (CC), case Air Canada/Canadian Airlines Cm 4838 (hereinafter: "Air Canada/Canadian") ([http://www.competition-commission.org.uk/rep\\_pub/reports/2000/443air.htm#ful](http://www.competition-commission.org.uk/rep_pub/reports/2000/443air.htm#ful)), where the distinction between time-sensitive and price sensitive passengers was described as reasonable.

<sup>11</sup> See e.g. European Commission, case M.1305 – Eurostar, para. 14 (hereinafter: "Eurostar") ([www.europa.eu.int/comm/competition/mergers/cases/decisions/m1305\\_en.pdf](http://www.europa.eu.int/comm/competition/mergers/cases/decisions/m1305_en.pdf)); case M.2041 - United Airlines/US Airways, para. 18 (hereinafter: "United Airlines/US Airways") ([http://www.europa.eu.int/comm/competition/mergers/cases/decisions/m2041\\_en.pdf](http://www.europa.eu.int/comm/competition/mergers/cases/decisions/m2041_en.pdf)), where the question of whether there is a distinct market for time sensitive passengers was left open; case JV.19 - KLM/Alitalia, para.21 (hereinafter: "KLM/Alitalia") ([www.europa.eu.int/comm/competition/mergers/cases/decisions/jv19\\_en.pdf](http://www.europa.eu.int/comm/competition/mergers/cases/decisions/jv19_en.pdf)), where this distinction, however, has not proved decisive for the Commission's assessment of the operation.

<sup>12</sup> See e.g. European Commission, United Airlines/US Airways (see footnote 11 above), para. 18; KLM/Alitalia (see footnote 11 above), para. 21.

<sup>13</sup> It should be noted that in some cases the airlines concerned were not in the position to give quantitative information about the type of passengers conveyed.

relevant markets. They also have a wider choice of flight alternatives than O&D passengers.<sup>14</sup>

11. In its decisions the European Commission has differentiated between point-to-point passengers and connecting passengers in relation to the relevant O&D routes<sup>15,16</sup>. Connecting passengers and O&D-passengers were considered to belong to different relevant markets. In *Air Canada/Canadian Airlines*<sup>17</sup> and in *British Airways/City Flyer Express*<sup>18</sup> the UK Competition Commission (formerly known as the Monopolies and Mergers Commission) also analysed connecting passengers as separate markets. In contrast to this, in *Lufthansa/Eurowings*<sup>19</sup> the Bundeskartellamt considered point-to-point passengers and connecting passengers as belonging to the same relevant market. In any event, the effects of connecting traffic should be taken into account in the overall competition assessment of affected O&D routes.

### 3.3. *Substitutability in geographical respect*

#### 3.3.1. *O&D approach to market definition*

12. The O&D approach to market definition is at least a suitable starting point for the competition analysis in air transport cases. According to this approach every combination of a point of origin and a point of destination is to be considered a separate market from the consumer's point of view. The O&D approach is thus a demand-based approach to market definition. It has the advantage of being capable of taking into account many relevant competition aspects in the airline sector. The O&D approach is applied by the European Commission<sup>20</sup> as well as by national competition authorities.<sup>21</sup>

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<sup>14</sup> See e.g. European Commission, *Lufthansa/AuA* (see footnote 6 above), para. 65.

<sup>15</sup> For a discussion of the O&D approach to market definition see below, paras. 12 ff.

<sup>16</sup> See e.g. European Commission, *United Airlines/US Airways* (see footnote 11 above); *Lufthansa/AuA* (see footnote 6 above), paras. 64-72.

<sup>17</sup> See footnote 10 above.

<sup>18</sup> See CC, *British Airways Plc and City Flyer Express Limited*, Cm 4346 (20.07.1999). (hereinafter: "BA/City Flyer") ([http://www.competition-commission.org.uk/rep\\_pub/reports/1999/430ba.htm#full](http://www.competition-commission.org.uk/rep_pub/reports/1999/430ba.htm#full)).

<sup>19</sup> See Bundeskartellamt, case B 9 – 147/00 - *Lufthansa/Eurowings*, decision of 19.09.2001 (hereinafter: "Lufthansa/Eurowings") ([http://www.bundeskartellamt.de/wDeutsch/download/pdf/Fusion/Fusion01/B9\\_147\\_00.pdf](http://www.bundeskartellamt.de/wDeutsch/download/pdf/Fusion/Fusion01/B9_147_00.pdf)).

<sup>20</sup> See e.g. European Commission, *Lufthansa/AuA* (see footnote 6 above), para. 46.

<sup>21</sup> See e.g. OFT, case CP/1535-01 – *British Midland/United Airlines* (hereinafter: "BMI/United Airlines"), a non-confidential version is available at

### 3.3.2. Adjacent airports with overlapping catchment areas

13. Direct transport services from two or more adjacent airports may belong to the same relevant O&D market. Those passengers living in the catchment areas of two or more airports (i.e. 'overlapping catchment areas') may consider those airports as possible substitutes when choosing which airport they fly from and which airport they fly to. This depends on a number of factors, including the number of potential passengers living in the overlapping catchment areas concerned, the frequency of the services, the duration of the journey,<sup>22</sup> the prices of tickets and the type of passengers travelling (in particular whether they are time-sensitive or non time-sensitive passengers). Airport substitution increases competition between flights on a particular route (only) if the choice between different airports also implies a wider choice between different individual airlines.<sup>23</sup>
14. The substitutability of airports has been an important issue in a number of cases. In the British Midland/Lufthansa/SAS case the European Commission considered 'secondary' airports to be not as attractive to business travellers as 'primary' airports.<sup>24</sup> In the United Airlines/US Airways case it was found that flights from Munich and Frankfurt airports to US cities were not competitively constrained either by flights from regional airports or from certain European hub airports (i.e. Amsterdam, Brussels or Zurich) on almost all city pairs concerned.<sup>25</sup> In BA/Iberia/GB Airways<sup>26</sup> the European Commission recently found that for

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[www.offt.gov.uk/Business/Legal+Powers/United+Airlines+and+British+Midland+Alliance+Expansion+Agreement.htm](http://www.offt.gov.uk/Business/Legal+Powers/United+Airlines+and+British+Midland+Alliance+Expansion+Agreement.htm).

<sup>22</sup> In Lufthansa/AuA (see footnote 6 above) the European Commission found that "There is a correlation between the extra time a traveller is willing to spend by travelling to an airport which is farther away and the overall travelling time. For flights within Europe it can be assumed that the radius of an individual airport's catchment area is small, given the short travelling time. Overlapping catchment areas are therefore of little relevance for flights within Europe." (para. 55)

<sup>23</sup> See e.g. European Commission, United Airlines/US Airways (see footnote 11 above), para. 20; European Commission, Lufthansa/AuA (see footnote 6 above), para. 54; OFT, case BMI/United Airlines (see footnote 21 above) and case BA/British Regional (hereinafter: "BA/British Regional") (<http://www.offt.gov.uk/business/mergers+fta/advice/clearances+and+referrals/ba.htm>).

<sup>24</sup> See European Commission, Case COMP/37.812 - British Midland/Lufthansa/SAS (hereinafter: "British Midland/Lufthansa/SAS") (notice published in OJ C 83 of 14.3.2001) ([http://europa.eu.int/eur-lex/pri/en/oj/dat/2001/c\\_083/c\\_08320010314en00060010.pdf](http://europa.eu.int/eur-lex/pri/en/oj/dat/2001/c_083/c_08320010314en00060010.pdf)). See also press release IP/01/831.

<sup>25</sup> See European Commission, United Airlines/US Airways (see footnote 11 above), paras. 23 ff.

<sup>26</sup> See European Commissions' notice in case COMP/38.479 – British Airways/Iberia/GB Airways, 14.1.2004, paras. 21-24 (hereinafter: BA/Iberia/GB Airways) (<http://europa.eu.int/comm/competition/antitrust/cases/decisions/38479/en.pdf>).

services from the UK to Spain the London airports (Heathrow, Gatwick, Luton and Stansted) were all sufficiently substitutable for non time-sensitive passengers, although the conclusions for time-sensitive passengers were less clear cut. In relation to two pairs of Spanish airports, Sevilla/Jerez and Valencia/Alicante, the European Commission found that there was substitutability between the respective adjacent airports for non time-sensitive passengers but not for time-sensitive customers.

15. The UK's competition authorities addressed the question of airport substitutability with particular respect to the main London airports (i.e. Heathrow and Gatwick) and the 'secondary' airports (i.e. Luton and Stansted) in the BMI/United Airlines, BA/British Regional, BA/City Flyer and Air Canada/Canadian Airlines cases. In BA/City Flyer it was noted that catchment areas for short haul routes tended to be narrower than those for long haul routes and that airports were less dependent on their main catchment areas for leisure travellers compared to business travellers. In general Luton and Stansted have been viewed as secondary airports that are not substitutable, at least for time-sensitive passengers.<sup>27</sup> It has also been recognised that Heathrow and Gatwick are not perfectly substitutable. For example, in BMI/United Airlines it was noted the average fare from Heathrow was significantly higher than that from Gatwick (on the basis of the average fare data from the DOT's survey of 2000), which reflected the fact that a greater number of high fare-paying (primarily business) passengers could be attracted on flights to Heathrow. However, as an analysis of the relevant O&D markets was not dependant on reaching a conclusion as to whether the London airports should be included in the same market, the question was left open. In the Alitalia/Volare code sharing case the Italian Competition Authority considered the issue of substitutability of airports (i.e. Milano-Malpensa/Milano-Linate) focusing on the distinction between time-sensitive and non time-sensitive passengers.<sup>28</sup> In its decision the Authority concluded - based on the results of a market test it had carried out using passenger interviews at

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<sup>27</sup> See BA/City Flyer (see footnote 18 above), para 2.69. It was noted in this decision that competition from Stansted and Luton operated at the margin of the market, although such competition could be expected to increase in the future.

<sup>28</sup> See Autorità garante della Concorrenza, decision in the case Alitalia/Volare Group, July 2003 (hereinafter: "Alitalia/Volare") (see at [www.agcm.it](http://www.agcm.it)).

the two airports - that the two airports, at least for business travellers, were not substitutable.

### *3.4. Substitutability with indirect flights and alternative modes of transport*

#### *3.4.1. Indirect flights*

16. Direct flights (i.e. non-stop services) and indirect flights (i.e. one-stop services) may be considered as substitutable transport options by customers. Because indirect flights imply one (or more) stops and take longer than non-stop flights they are usually more inconvenient and, *ceteris paribus*, less attractive to customers.<sup>29</sup> The main factors – providing indirect flights are available – that determine whether indirect flights represent a competitive alternative to direct flights are the type of passengers (in particular whether they are time-sensitive or non time-sensitive), the duration of the flight and the connecting time, flight schedules and prices. In general, indirect services are more likely to be substitutable for direct services on long-haul flights than on medium- or short-haul (e.g. domestic) flights.<sup>30</sup> Furthermore, for competition policy purposes only indirect flights offered by independent competitors of the parties can be considered as a competitive alternative for passengers. Against this background, the extent to which indirect flights are substitutable with direct flights in an individual case can be assessed only on a route by route basis.
17. With respect to long haul routes the European Commission concluded in *United Airlines/US Airways* that indirect routes may constitute a competitive alternative to non-stop services if they meet the following conditions: they must be marketed as connecting flights on the city pair concerned (and thus appear on the computer reservation system (CRS)) and they may only result in a limited extension to the duration of the journey.<sup>31</sup> In *Lufthansa/AuA*<sup>32</sup> it was maintained that on short distances, involving a short travel time, only very few non time-sensitive travellers would consider replacing a direct flight by an indirect flight as a result of a price increase for direct flights, and that this share of passengers was too small for indirect flights to exert any competitive pressure on direct short-

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<sup>29</sup> See e.g. European Commission, *United Airlines/US Airways* (see footnote 11 above), para. 14.

<sup>30</sup> See e.g. OFT, *BMI/United Airlines* (see footnote 21 above); European Commission, *United Airlines/US Airways* (see footnote 11 above), paras. 13-19.

<sup>31</sup> European Commission, *United Airlines/US Airways* (see footnote 11 above), paras. 13-19.

<sup>32</sup> See European Commission, *Lufthansa/AuA* (see footnote 6 above), para. 53.

haul routes.<sup>33</sup> As an exception to this general presumption, the European Commission in the recent merger case Air France/KLM<sup>34</sup> concluded that on two city pairs on the Franco-Dutch bundle (Bordeaux-Amsterdam and Marseille-Amsterdam) the indirect services of Air France did constitute a competitive alternative to non-stop services. Air France's indirect services on these two individual routes were particularly attractive to time-sensitive passengers because Air France offered a higher number of frequencies in relation to Basiq Air's direct service and thus the only possibility for a one day return trip. In BMI/United Airlines the OFT considered indirect flights for UK passengers flying to the US. The OFT concluded that it was not generally an attractive option to fly indirectly via another airport in Europe (as this usually involves back-tracking) - an indirect flight via another US gateway was considered a more likely alternative.<sup>35</sup>

#### *3.4.2. Charter flights and alternative modes of transport*

18. From the customer's viewpoint charter flights and other modes of transport may be possible substitutes for certain scheduled air transport services. However, generally charter flights are (still) not sufficiently substitutable for scheduled services (see para. 20) to be included in the same market.<sup>36</sup> Whether other transport modes (i.e. rail, road, water) are suitable substitutes for scheduled air services depends on several factors, for example the type of passengers and their needs (in particular whether they are time-sensitive or non time-sensitive), the distance of the journey and the relative travel time, as well as the cost of the journey. Whether certain alternative modes of transport belong to the same product market can only be assessed in an individual case on a route by route basis, although in several cases high-speed rail transport has been considered

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<sup>33</sup> The same conclusion was drawn by the Italian Competition Authority in the Alitalia/Volare code sharing case (see footnote 28 above) due to the fact that all the routes involved were national or short-haul routes within Europe.

<sup>34</sup> See European Commission, case COMP/M.3280 - Air France/KLM, 11.02.2004, para. 80 (hereinafter: Air France/KLM) (see on the website of the European Commission at [http://europa.eu.int/comm/competition/mergers/cases/decisions/m3280\\_en.pdf](http://europa.eu.int/comm/competition/mergers/cases/decisions/m3280_en.pdf)).

<sup>35</sup> See footnote 21 above, paras. 62-65.

<sup>36</sup> However, there might be exceptions. In BA/City Flyer (see footnote 18 above) and Air Canada/Canadian Airlines (see footnote 10 above) the CC found that charter flights offered some competition in relation to leisure travellers.

as offering a possible intermodal alternative to air travel as far as time-sensitive passengers are concerned.

19. In *European Night Services*<sup>37</sup> the European Commission demonstrated that the substitutability of different transport modes depends in particular on the needs of a particular group of travellers. In this decision two relevant service markets were defined: the market for the transport of business travellers and the market for the transport of leisure travellers. On the other hand, in *Lufthansa/AuA* the European Commission found that, in addition to qualitative factors, total travelling time rather than distance is the decisive factor for consumers in relation to the substitutability of alternative means of transport.<sup>38</sup> The European Commission concluded that, as a rule, other means of transport, such as rail and road, do not offer an alternative for time-sensitive travellers on direct routes between Germany and Austria.<sup>39</sup> In the recent *British Airways/SN Brussels Airlines* case the European Commission found that the relevant market in the Brussels O&D pair was broader than direct air services and included high-speed rail transport (i.e. the Eurostar).<sup>40</sup> Rail was considered to be a competitive alternative to air transport for both non time-sensitive and time-sensitive passengers. In *BA/City Flyer* the UK Competition Commission found that rail services, in particular on domestic routes and the European routes to Brussels and Paris (served by Eurostar), operated in the same market as airlines on these routes.<sup>41</sup> However, in the *Lufthansa/Eurowings* case the German Bundeskartellamt concluded that there is (still) no homogenous market for land- and air-based means of transport for German domestic traffic.<sup>42</sup> The Italian Competition Authority came to the same conclusion in the *Alitalia/Volare* case.

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<sup>37</sup> European Commission, case 34.600 - *European Night Services*, OJ 1994 L 259/20, paras. 26-27 ([http://europa.eu.int/smartapi/cgi/sga\\_doc?smartapi!celexapi!prod!CELEXnumdoc&lg=EN&numdoc=31994D0663&model=guichett](http://europa.eu.int/smartapi/cgi/sga_doc?smartapi!celexapi!prod!CELEXnumdoc&lg=EN&numdoc=31994D0663&model=guichett)) (hereinafter: "European Night Services").

<sup>38</sup> *Lufthansa/AuA* (see footnote 6 above), paras. 57-58.

<sup>39</sup> *Ibid.*, para. 61.

<sup>40</sup> See European Commission, case 38.477 - *British Airways/SN Brussels Airlines*, paras. 18 ff. (<http://www.europa.eu.int/comm/competition/antitrust/cases/decisions/38477/en.pdf>).

<sup>41</sup> See footnote 18 above.

<sup>42</sup> See *Lufthansa/Eurowings*, see footnote 19 above. The Bundeskartellamt reasoned that travelling by rail normally takes considerably longer than by plane. Even where rail travel times are becoming shorter and consequently coming more into line with air travel times (e.g. in the case of the "Sprinter" fast-train service between Frankfurt and Berlin), the frequencies offered are still insufficient, at least from the point of view of business travellers. At any rate the price level of domestic German flights at the time of the merger were significantly higher than Deutsche Bahn AG tariffs.

20. The European Commission has not so far considered charter flights as sufficiently substitutable to scheduled services, at least for time-sensitive passengers. With particular regard to non time-sensitive passengers, however, a different situation may arise in the case of significant seat-only sales by charter operators. For example, in KLM/Alitalia the European Commission found that charter air transport was an activity distinct from scheduled air transport, although the markets were considered to be closely related.<sup>43</sup> In BA/Iberia/GB Airways it was recently found when analysing the London-Alicante and London-Malaga routes that charter flights were not a sufficiently substitutable option for time-sensitive passengers.<sup>44</sup> However given the particular circumstances of the case,<sup>45</sup> the possibility that charter flights were sufficiently substitutable for non time-sensitive passengers could not be eliminated and the European Commission left this question open. The UK Competition Commission found in BA/City Flyer and Air Canada/Canadian Airlines that charter flights (either as part of a holiday package or on a seat-only basis) offer some competition in relation to leisure travellers.<sup>46</sup>

*3.5. Substitutability with respect to other aspects ('Low-cost' carriers, regional carriers and 'feeder' flights)*

21. In recent years distinctions have been drawn within the airline industry between different kinds of scheduled services. For example, flights by 'low cost' carriers, flights by 'regional' carriers or so-called 'feeder' flights, and flights by 'traditional' or 'full service' carriers. However, there does not seem to be any clear-cut definition of what is meant, for example, by the expression 'low-cost carrier' or 'regional carrier'. Moreover, most of these characterisations and distinctions have been defined by the airlines themselves and thus may have a particular relevance from a supply side (in particular, strategic) point of view.

22. 'Low cost' carriers can be characterised not only by their cost structure and the typical quality of service ("no frills") but also by other factors like destinations

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<sup>43</sup> See European Commission, KLM/Alitalia (see footnote 34 above), paras. 55 ff.

<sup>44</sup> See European Commission's notice in case BA/Iberia/GB Airways (see footnote 26 above), paras. 29-32.

<sup>45</sup> Namely given the relative importance of charter flights, the rather substantial percentage of seat-only charters and the apparent all year round availability notably on the routes London-Alicante and London - Malaga. (ibid., para. 31)

<sup>46</sup> See footnotes 10 and 18 above.

flown, airports used, aircrafts used, pricing policy, type of tickets (e.g. restricted/unrestricted tickets) and maybe also type of passenger. Generally, there will be some degree of substitutability between the services of traditional carriers and 'low cost' carriers in O&D markets at least as far as non time-sensitive passengers are concerned. For time-sensitive passengers the degree of substitutability between low cost services and traditional services depends on a number of factors.<sup>47</sup> Such factors include, among other things, whether 'low cost' carriers offer frequent and convenient departure times as well as flexible fares and tickets which are comparable to those offered by traditional carriers. Another important factor is whether 'low cost' carriers offer flights between main airports. If they use secondary airports then barriers to entry will in general be lower for 'low cost' carriers than for full service carriers (see para. 45). The question of airport substitutability may arise (see paras. 13 ff.). For example, in BA/Iberia/GB Airways the European Commission accepted substitutability between services of traditional carriers and 'low cost' carriers for non time-sensitive passengers on the routes between London and Spain.<sup>48</sup> In addition, it concluded that 'low cost' carriers were sufficiently substitutable for a not unsubstantial percentage of time-sensitive passengers.

23. Regional carriers, in contrast to traditional carriers, are smaller airlines which have a specialised business model insofar as they have focused their operations on a particular airport or a particular region, generally using smaller aircraft or turboprop machines. From the customer's viewpoint flights by regional carriers are in principle comparable to those by traditional carriers.<sup>49</sup> However, the question of substitutability can arise in the case of O&D routes where regional carriers offer direct flights whereas traditional carriers offer only indirect flights, or where regional carriers use secondary airports whereas traditional carriers use main airports.

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<sup>47</sup> The question of whether in recent years there has been a tendency among business travellers towards increased price-sensitivity needs further discussion. In particular the empirical results of the European Commission's industry dialogue on air transport competition policy is expected to provide further clarification.

<sup>48</sup> See the European Commission's notice in case BA/Iberia/GB Airways (see footnote 26 above), para. 28.

<sup>49</sup> See e.g. Swedish Competition Authority, case dnr 768/2001 - SAS/Skyways.

24. The concept of 'feeder flights' is a term used in the airline industry with respect to hub-and-spoke systems (this aspect is also discussed in para. 28). A feeder carrier can be described as a carrier that co-operates with an airline which operates a hub within a hub-and-spoke system on flights between smaller airports and the hub airport. Usually the objective of such co-operation is to make better use of the respective hubs and to harmonize the flight schedule of feeder flights with that of connecting flights.<sup>50</sup> Generally, a feeder flight can be understood to be part of an indirect flight (see para. 16) rather than a separate market. The analysis of feed traffic relates to the discussion on the treatment of connecting passengers (see para. 10).

### *3.6. Alternative approaches to market definition when considering network effects*

25. Whether network effects in the air traffic sector can be taken into consideration in market definition cannot ultimately be answered at this stage. In this respect, at least, a distinction can be made between those aspects of network competition that can easily be dealt with in the framework of the O&D approach (e.g. the role of connecting traffic, the substitutability of indirect services<sup>51</sup>) and those aspects that cannot. In BMI/United Airlines the OFT described network effects as "the broader competition issues which, in a number of previous decisions, have been discussed in addition to individual O&D markets, such as competition between airline hubs and between alliances."<sup>52</sup> However, the appropriate definition of what should be included in the expression 'network effects' in the airline industry needs further explanation.<sup>53</sup> Generally, consideration of network effects can be justified in cases where not all of the relevant competition issues are captured by an O&D approach.<sup>54</sup> Alternative approaches to market definition may be used by competition authorities instead of an O&D approach or to define additional markets that need to be analysed.

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<sup>50</sup> See e.g. European Commission, Lufthansa/AuA (see footnote 6 above), para. 38.

<sup>51</sup> See European Commission, Air France/KLM (see footnote 34 above), para. 18.

<sup>52</sup> See footnote 21 above.

<sup>53</sup> For example, the expression could be also used – explicitly or implicitly - to refer to the inclusion of indirect flights in the definition of an O&D market.

<sup>54</sup> For example, the range of routes offered by an airline or an alliance group could play an important role in determining the attractiveness of a corporate deal with it.

26. To date only limited case law exists. In the Lufthansa/Eurowings<sup>55</sup> merger proceedings the German Bundeskartellamt defined additional markets and considered the market for domestic air traffic to be the relevant product and geographic market (air traffic to neighbouring countries was regarded as a separate market in this particular case). The Bundeskartellamt argued that in this case, merger related network effects could be demonstrated more convincingly in relation to a market defined as comprising the whole relevant (sub-)network than with regard to each and every single O&D pair. In certain cases<sup>56</sup> the OFT and the European Commission considered network effects but did not deviate from the O&D approach to market definition. In Air France/KLM the European Commission concluded that demand substitution justifies the O&D approach in defining the relevant market, although in the case of corporate customers it was recognised that demand is driven both by network effects and by O&D considerations.<sup>57</sup>

## 4. Competition Assessment

### 4.1. Introduction

27. The welfare effects of airline mergers and alliances are twofold. On the one hand they can trigger efficiency gains by reducing costs and may result in benefits for passengers;<sup>58</sup> on the other hand there is a risk that a merger or alliance restricts or eliminates competition on the affected routes. European competition authorities generally pursue the aim of maintaining effective competition on all routes affected by a merger or alliance. In order to be able to approve a

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<sup>55</sup> See footnote 19 above.

<sup>56</sup> For example, the OFT addressed network issues in BMI/United Airlines (see footnote 21 above); see also European Commission, case Swissair/Sabena IV/M.616, paras. 22, 38 (hereinafter: "Swissair/Sabena") ([http://europa.eu.int/comm/competition/mergers/cases/decisions/m616\\_en.pdf](http://europa.eu.int/comm/competition/mergers/cases/decisions/m616_en.pdf)); and KLM/Alitalia (see footnote 11 above), paras. 22, 45.

<sup>57</sup> See European Commission, Air France / KLM (see footnote 34 above), para. 16. The Commission's reasons for these findings are as follows: "As most corporate customers conclude such contracts with several airlines / alliances, whenever flying on a specific O&D pair, among other elements, they will consider the prices charged on this particular route and the overall discount. The more advantageous the latter is and the better the carrier's network covers the customer's travel needs, the more likely it is that the corporate customer remains with one carrier / alliance. In that case the customer's choice is determined by network competition and not by competition on individual city pairs." (ibid., para. 15).

<sup>58</sup> See, for example, the description of the cooperation agreement between Lufthansa and Austrian Airlines in Lufthansa/AuA (see footnote 6 above), paras. 26 ff.

particular merger or alliance remedies have to be imposed in relation to those routes on which competition is restricted (see section 5.).

28. The competition assessment of mergers and alliances in the air transport sector is generally more complex than in many other economic sectors because of the network nature of the industry. Each alliance as well as each of the major airlines carry passengers on a multitude of different routes which are interconnected and constitute a network.<sup>59</sup> A proposed merger or alliance may result in adverse competition effects at a network level (as well as at an O&D level) which have to be taken into account in the assessment.
29. It should be stressed that given the specific circumstances of each individual case, every merger and alliance has to be assessed on a case-by-case basis. The underlying competition analysis is largely similar for mergers on the one hand and alliances - as defined above - on the other. In general, there is the presumption that both mergers and alliances will result in the total elimination of (actual and potential) competition between the parties on the routes affected.<sup>60</sup> However, one difference is that once approved, mergers are unlikely to be dissolved or revisited whereas alliances are usually less binding and the analysis could be reviewed in the event of a material change in circumstances.
30. The legal test applied in merger cases and in alliance cases is different. The legal test used for alliances is laid down in Article 81 EC and/or in Article 53 of the EEA-Agreement and in the corresponding provisions of the national competition laws of the national states. The legal test used for mergers is provided by the EC Merger Regulation, Article 57 of the EEA-Agreement and by the merger control regimes of the national states.
31. In most of the member states a market dominance test is used as the basis for establishing that a merger leads to a significant restriction or elimination of competition. However, some of the national authorities<sup>61</sup> as well as the European

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<sup>59</sup> Probably the most efficient way to run such an aviation network is the hub-and-spoke mode of operation. Today, nearly all of the larger European airlines operate hub-and-spoke systems which allow hub routing ("hubbing") in contrast to linear routing with only point-to-point services. Simple hub-and-spoke systems use only one hub airport, whereas in multiple hub systems two or more hubs are connected in the route network.

<sup>60</sup> However, in the case of mergers there might be an exception when minority shareholdings are caught by national merger control regimes. In the case of alliances there might be an exception when the scope of the alliance agreement is only limited.

<sup>61</sup> At present, the UK, Spanish and Irish competition authorities.

Commission<sup>62</sup> from May 2004 will use other tests for assessing concentrations, such as a substantial lessening of competition ("slc") or a significant impediment of effective competition ("siec"). Nevertheless, in most of the merger cases the result of the competition assessment will be similar, irrespective of which test is applied.

#### *4.2. Route by route competition*

32. For the purpose of the competition assessment two broad types of affected markets can be categorised: overlap markets (or overlap routes) and non-overlap markets. The first category addresses actual competition issues and the second category potential competition issues.
33. Mergers and alliances typically affect a large number of overlap routes, particularly if indirect services are taken into consideration. In relation to intra-European cases those overlap routes will generally be restricted to direct routes (see paras. 16 and 17). In contrast, in relation to long-haul routes, indirect routes may also be included in the relevant market. Competition concerns may therefore arise with respect to a whole range of affected overlap routes irrespective of whether they are direct or indirect. In general it is possible to distinguish between three categories of overlap routes: direct-direct, direct-indirect and indirect-indirect. In individual cases attention should be focused on those routes where competition concerns are likely to arise.<sup>63</sup> Generally competition is particularly likely to be restricted on (overlap) routes between the respective hubs of the parties. In BMI/United Airlines it was noted that the impact of an alliance between the parties would be greater on those routes between Heathrow and United's hub airports. The prospects for competitive entry on these routes would be reduced, as potential entrants would not have the same level of access to connecting passengers as BMI and United Airlines.
34. Mergers and alliances may also affect non-overlap routes if potential competition is restricted. A merger or alliance with a potential competitor may have significant anti-competitive effects if the potential competitor ex ante exerts a significant

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<sup>62</sup> See Article 2 § 2 EC Merger Regulation.

<sup>63</sup> So far, no market share thresholds have been identified which could be useful as a filter for excluding those kinds of routes where the parties are unlikely to have any market power. There is also a danger that the use of such thresholds might result in routes that are of interest being excluded from the analysis.

competitive constraint on the acquiring airline.<sup>64</sup> From an economic point of view the non-operating party should be considered a potential competitor only if there is a real, concrete possibility for it to compete with the operating party on the relevant O&D-markets in the foreseeable future (i.e. there is a 'real possibility of entry'). A mere theoretical possibility of market entry in general is not sufficient.<sup>65</sup> In general, an airline will be considered a potential competitor on a specific non-overlap route only if that route is either directly linked to one of its hubs or there is sufficient local traffic to allow market entry on a point-to-point basis.<sup>66</sup>

#### 4.3. *Criteria for the assessment of market power*

35. There are a number of criteria that are usually taken into account in assessing market power in merger and alliance cases in the field of air transport. However, these criteria are not applied in a mechanical way in the sense of a check-list, and they will have differing levels of importance in different cases. As with the structural analysis of the market in any other sector, market shares and the conditions of market entry play a key role when assessing the competition effects of an airline merger or alliance.

##### 4.3.1. *Market shares*

36. The (combined) market share of the parties in the relevant markets is one important indicator of market power. This provides information on the relationship between the parties and their competitors.<sup>67</sup> Generally, market power is more likely to exist if an undertaking has a (persistently) high market share. A "high" market share can be understood relative to absolute thresholds or relative to other competitors. When analysing the structure of the market it is also important to consider the market shares of the parties' competitors. Some national states'

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<sup>64</sup> For a general discussion see, for example, European Commission, Guidelines on the assessment of horizontal mergers under the Council Regulation on the control of concentrations between undertakings, OJ C 31 of 05.02.2004, p. 5, paras. 58 f. ([http://europa.eu.int/eur-lex/pri/en/oj/dat/2004/c\\_031/c\\_03120040205en00050018.pdf](http://europa.eu.int/eur-lex/pri/en/oj/dat/2004/c_031/c_03120040205en00050018.pdf)) (hereinafter: "EC horizontal Merger Guidelines").

<sup>65</sup> See CFI, T-374/94 - European Night Services, ECR 1998, II-3141, para. 137 (<http://curia.eu.int/jurisp/cgi-bin/form.pl?lang=en&Submit=Submit&docrequire=alldocs&numaff=T-374%2F94&datefs=&datefe=&nomusuel=&domaine=&mots=&resmax=100>). See also the analysis of the OFT in the BMI/United Airlines case (see footnote 21 above).

<sup>66</sup> See for example Lufthansa/AuA (see footnote 6 above), para. 103 and 99 lit b).

<sup>67</sup> In addition, with respect to the market share also the increment can be an important factor.

competition laws provide market share thresholds, in particular with respect to mergers.<sup>68</sup>

37. When calculating market shares in passenger air transport cases different methods and proxies are used. A frequently used basis for calculating market shares with respect to passenger services in air traffic is the 'actual number of tickets sold per relevant market' or the 'actual number of passengers conveyed' ("O&D passenger numbers")<sup>69</sup>. Alternatives to this would be to look at market shares by value or market shares expressed in terms of frequencies. However, this list is not exhaustive. It should be emphasised that each of those methods and proxies has its pros and cons. Therefore, when calculating market shares in the passenger air transport sector different proxies should be used depending on the circumstances of the particular case (e.g. the availability of data), and to provide different perspectives on market power.
38. The calculation of market shares on the basis of O&D passenger numbers is a well established practice in the case law of the national competition authorities as well as the European Commission. The European Commission has used O&D passenger numbers in most of the merger and alliance cases concerning passenger air transport that it has considered. National competition authorities' practice can be illustrated by several cases. For instance, in the Bundeskartellamt's Lufthansa/Eurowings merger decision the parties' market shares on the domestic German air transport market for passengers were determined by their share of overall passenger numbers on the relevant domestic German air transport market in the year 2000. In BMI/United Airlines, BA/City Flyer and Air Canada/Canadian Airlines the UK's competition authorities used passenger numbers<sup>70</sup> for the relevant O&D markets, although in these cases the frequency shares of direct flights for each airline on the route were

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<sup>68</sup> For example, according to the German Act against Restraints of Competition (Sec. 19 (3)) concerning merger cases and cases of abuse of a dominant position there is a legal presumption of a dominant position if a single firm has a market share of at least one third.

<sup>69</sup> It should be noted, that the number of 'tickets sold' is not necessarily equal to the number of 'passengers conveyed' because of the effects of code sharing.

<sup>70</sup> In addition, the Italian Competition Authority in Alitalia/Volare (see footnote 28) used the number of O&D passengers transported on each route by the airlines involved in the code sharing and by their competitors in order to calculate market shares.

also analysed. In Lufthansa/AuA the European Commission established market shares in terms of frequencies.<sup>71</sup>

#### 4.3.2. Conditions of market entry

##### 4.3.2.1. Overview

39. Analysis of market entry conditions is a second key element in the competition assessment of mergers and alliances. The likelihood that a merger or alliance will result in a restriction or elimination of competition in general decreases as the possibility of market entry increases.<sup>72</sup> In other words, barriers to market entry are an important indication of the parties' market position with regard to potential competition and market contestability, as in other industrial sectors.
40. A range of factors is usually taken into account in order to determine the conditions of market entry, some of which are sector-specific. In each individual case it is necessary to establish which factors are relevant and the extent to which they will affect entry barriers. Generally these factors can be categorised into structural, regulatory and behavioural factors; network effects could form a separate group. This categorisation can be adapted to the requirements of each particular case as appropriate.
41. The factors which are usually taken into consideration in passenger air transport cases are:
- *Structural factors* such as slot shortages in congested airports, high frequencies, the hub-and-spoke structure (see also under network effects) and - to a lesser extent - ground handling infrastructure and ground handling services;
  - *Regulatory factors* such as pricing restrictions for indirect flights, administrative slot allocation systems, the lack of necessary route rights because of restrictions in bilateral air service agreements, tariff conferences and state aids;
  - *Strategic behaviour*, especially the potential for predatory conduct such as strategic pricing and/or frequency increases (see also under network effects);

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<sup>71</sup> See for example Lufthansa/AuA (see footnote 6 above), paras. 62 ff.

- *Network effects* such as the hub-and-spoke structure of the flight network, frequent flyer programmes (FFPs), corporate discount deals, travel agent agreements or computerised reservation systems (CRS).

In each individual case it is necessary to establish on a route by route basis which of these conditions of market entry or barriers to entry exist and whether market power resulting from these factors is likely to restrict or eliminate competition. However, it should be noted that not all of the factors listed above will be relevant in every case, nor is this list exhaustive.

42. Mergers and alliances can be accepted even where the parties have a high market share on overlap and/or non-overlap routes providing that there are no barriers to entry and the remaining actual and potential competition was sufficient to constrain the competitive behaviour of the parties.<sup>73</sup> On the other hand, significant entry barriers in combination with a high market share of the parties on overlap and non-overlap routes typically indicate market power which is likely to restrict or eliminate competition.<sup>74</sup>

#### 4.3.2.2. *Structural factors*

43. Slot shortages have been considered in the analysis of entry barriers in a number of cases. For example, the European Commission considered slot shortages as an entry barrier in Lufthansa/SAS/United Airlines<sup>75</sup> with respect to Lufthansa's hub in Frankfurt and in the merger case Air France/KLM. The Bundeskartellamt considered slot shortages in its analysis of structural factors at a number of German airports in Lufthansa/Eurowings<sup>76</sup>. The OFT has found that, in general, full service carriers face entry barriers which are significantly higher than those

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<sup>72</sup> See, for example, European Commission, EC horizontal Merger Guidelines, paras. 68 ff.; Bundeskartellamt, Principles of Interpretation, October 2000, p. 23 f. (<http://www.bundeskartellamt.de/Checkliste-E02.pdf>).

<sup>73</sup> For the practice of the European Commission see, in particular, case 36.111 - KLM/Northwest, decision of 29.10.2002 (notice published in OJ 2002 C 264/11; press release IP/02/1569) (hereinafter: "KLM/Northwest"), where the European Commission accepted a combined market share of up to 90 % on the direct overlap routes. They did so in the absence of any direct competition and without imposing remedies because no significant entry barriers were identified.

<sup>74</sup> See e.g. European Commission, case 36.201 - Lufthansa/SAS/UA (notice published in OJ 2002 C 181/2; press release IP/02/1569; for the commitments see notice in OJ 2002 C 264/5) (hereinafter: "Lufthansa/SAS/UA").

<sup>75</sup> Ibid.

<sup>76</sup> See footnote 19 above.

for low cost carriers.<sup>77</sup> The most significant barrier to entry is access to slots at airports in the South East of England, in particular London Heathrow. In Air Canada/Canadian Airlines the UK Competition Commission considered terminal capacity as a potential constraint.<sup>78</sup> In Alitalia/Volare the Italian Competition Authority considered the number of slots available for the two airlines in the congested and fully regulated airport Milano-Linate as a barrier to entry on the routes from and to Linate.<sup>79</sup>

44. Other structural factors have also been analysed in the assessment of market entry in a number of cases. The European Commission has taken into account the hub-and-spoke structure. For example in Lufthansa/AuA Lufthansa's hub dominance at the Frankfurt airport was found to be an entry barrier.<sup>80</sup> In the Swissair/Sabena merger case the European Commission found that the situation in relation to ground handling did not constitute an additional barrier to market entry because self-handling was allowed at all the airports in question and neither of the parties enjoyed monopoly rights with regard to third-party handling.<sup>81</sup> In relation to national authorities' case law, one example is the Bundeskartellamt's consideration in Lufthansa/Eurowings<sup>82</sup> of structural factors such as high frequencies operated by the parties. In some cases the reputation of the incumbent airline was also an important factor,<sup>83</sup> as this may act as a barrier to entry because new entrants will face sunk costs associated with promotion and brand advertising. The Italian Competition Authority in Alitalia/Volare also considered the incumbents' reputation, with respect to Alitalia.
45. In general, structural barriers to entry will be particularly high on markets where the parties operate a hub airport on both ends of the route.<sup>84</sup> In these cases the

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<sup>77</sup> In its advice on the easyJet/Go merger the OFT found that, in general, with no slot constraints on secondary airports, liberalised European air space and an established cost business model to follow, barriers to entry by low cost carriers were not high. The main costs of entering and remaining are those associated with promotion and brand advertising.

<sup>78</sup> See footnote 10 above, paras 4.26-4.29.

<sup>79</sup> The shortage of slots in Milano-Linate together with the slot allocation based on the level of the historical traffic in the airport was also considered a significant regulatory barrier to entry.

<sup>80</sup> See European Commission, Lufthansa/AuA (see footnote 6 above), paras. 78, 98 (a).

<sup>81</sup> See European Commission, Swissair/Sabena (see footnote 56 above), para. 34.

<sup>82</sup> See footnote 19 above.

<sup>83</sup> For example, the Hellenic Competition Authority has taken into account the high reputation enjoyed by the national air carrier Olympic Airways in the case Aegean/Air Greece (Decision No 105/II/1999).

<sup>84</sup> See e.g. Air France/KLM (see footnote 34 above), paras. 69 ff..

ability of new entrants to attract connecting traffic to the airports concerned is a critical factor. In Air France/KLM the European Commission's market investigation found that other network carriers were not interested in operating on the Paris to Amsterdam (hub-to-hub) route. Competitors argued that the merged entity's dominance at their respective hubs in Paris and Amsterdam makes entry particularly unattractive on this route.<sup>85</sup>

#### 4.3.2.3. Regulatory factors and strategic behaviour

46. In the transatlantic alliance cases KLM/Northwest<sup>86</sup> and Lufthansa/SAS/United Airlines, and in Air France/KLM,<sup>87</sup> the European Commission considered the existence of significant regulatory and structural entry barriers. In Lufthansa/SAS/United Airlines the restrictive price control by the German government over indirect services on several transatlantic routes was considered to be an entry barrier.<sup>88</sup> In the transatlantic alliance cases the conditions of market entry were also determined by the existing restrictions in the bilateral Air Service Agreements (ASAs). The OFT has considered that restrictions in ASAs are a major barrier to entry on O&D routes between Member States and third countries. In BA/City Flyer it was found that the UK was party to around 120 of such ASAs. The Bermuda II bilateral agreement, for example, represents a major barrier to entry regarding flights between the UK and the US as it limits the number of airlines that can operate on routes between London Heathrow and the US. In this respect, the outcome of the ongoing negotiations between the European Commission and the US government on an open skies agreement for

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<sup>85</sup> See also para. 73.

<sup>86</sup> See European Commission, KLM/Northwest (see footnote 73 above).

<sup>87</sup> The European Commission in Air France/KLM (see footnote 34 above) found that remaining national regulatory restrictions may also prevent free competition especially with regard to indirect flights on long haul routes which were taken into account as a factor moderating the finding of dominance. In order to address the Commission's competition concerns about these indirect flights the Dutch and French national authorities have assured the Commission they will give traffic rights to other carriers wishing to stop over in Amsterdam or Paris en route to United States and other non-EU destinations. They also assured the Commission they will refrain from regulating prices on long haul routes. (see European Commission, press release of 11.02.2004, [http://europa.eu.int/rapid/start/cgi/questen.ksh?p\\_action.getfile=gf&doc=IP/04/194|0|RAPID&lg=EN&type=PDF](http://europa.eu.int/rapid/start/cgi/questen.ksh?p_action.getfile=gf&doc=IP/04/194|0|RAPID&lg=EN&type=PDF)).

<sup>88</sup> The German aviation authorities required that published fares for indirect services were filed with them and they were able to prohibit fares that undercut fares for non-stop services on the same route by a German or US carrier. See the European Commission in the case Lufthansa/SAS/UA (see footnote 74 above) (OJ 2002 C 181/5, para. 31).

the transatlantic air traffic will be of particular importance for future transatlantic cases.

47. Behavioural factors such as the potential for aggressive or predatory behaviour have so far not played a major role as a barrier to entry in the case law on mergers and alliances in the air transport sector. In addition, the past behaviour of airlines might also be considered in the competition assessment, for example, in providing an indication of the likelihood of coordinated behaviour when analysing issues of collective dominance.<sup>89</sup>

#### 4.3.2.4. *Network issues*

48. As already noted in the discussion of market definition issues (see paras. 25 and 26) network aspects may also be a relevant issue in the competition assessment. However, the existing case law on network issues is rather limited.
49. Both the national competition authorities and the European Commission have taken network effects into consideration in the context of the competition assessment in some cases. In BMI/United Airlines<sup>90</sup> the OFT found that, although the O&D approach to market definition was considered sufficient to analyse the case, network effects may exist in the context of competition for corporate deals<sup>91</sup> or for members of FFPs. This was because a corporate customer's or FFP member's choice of an airline or alliance for a particular journey may be influenced by the network of the carrier(s), as well as the service on the particular route. Also in Air Canada/Canadian Airlines<sup>92</sup> it was found that FFPs acted as a barrier to entry for UK operators. In Alitalia/Volare the Italian Competition Authority considered among other things network effects: Alitalia and Volare, as the first and the fourth carrier respectively in Italy, combined their networks at national level and pooled their frequent flyer programmes. The agreement was declared to violate Italian competition law as far as domestic routes were concerned.<sup>93</sup>

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<sup>89</sup> See e.g. European Commission, EC horizontal Merger Guidelines, para. 43.

<sup>90</sup> See footnote 21 above.

<sup>91</sup> Corporate deals can also act to 'lock' corporate customers into using a particular airline on certain routes, effectively preventing entrants from competing unless they can provide a similar network.

<sup>92</sup> See footnote 21 above.

<sup>93</sup> See Italian Competition Authority, Alitalia/Volare (see footnote 28 above).

50. Network aspects were also considered by the European Commission in the Lufthansa/AuA decision.<sup>94</sup> Among other aspects, the hub dominance of Lufthansa at Frankfurt and the difficulties other airlines face in obtaining slots in peak times at this congested airport, the pooling of frequent flyer programmes, and the tying effects of corporate customer deals were identified as barriers to entry on the Vienna-Frankfurt route. In the European Commission's recent merger decision in Air France/KLM some competitors argued that the merger effectively reduced the number of world-wide alliances from four (SkyTeam, Star, Wings and OneWorld) to three, as the Wings and SkyTeam alliances merge and that this would have a serious impact on network competition.<sup>95</sup> However, the European Commission found that the network effects of the merger between Air France and KLM did not raise serious concerns. This conclusion was also considered to apply to corporate customers where a market investigation rejected the hypothesis that corporate customers would be negatively affected by the merger as far as network/alliance competition is concerned. In Swissair/Sabena<sup>96</sup> the European Commission took into account "the effect of the combination of the parties' network at a wider European level, out of the total number of passengers transported within W. Europe" and Swissair's participation in the European Quality Alliance (EQA). The European Commission also found that "the co-existence of the three alliances, namely the proposed concentration, the EQA and the Lufthansa/SAS cooperation agreement, will enable the participating parties to establish an extensive integrated European network."<sup>97</sup> In KLM/Alitalia<sup>98</sup> the European Commission found, with respect to the effect of the coordination of the parties' networks at a European and worldwide level, that the alliance would not give rise to a dominant player. In SAS/Spanair the European Commission found that "the network effects arising from the proposed

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<sup>94</sup> See European Commission, Lufthansa/AuA (see footnote 6 above), para. 99.

<sup>95</sup> See European Commission, case COMP/M.3280 - Air France/KLM (see footnote 34 above), paras. 129 ff.

<sup>96</sup> European Commission, Swissair/Sabena (see footnote 56 above), paras. 38 - 41.

<sup>97</sup> Ibid.

<sup>98</sup> See European Commission, KLM/Alitalia (see footnote 11 above), para. 45.

concentration do not raise serious doubts as to the creation or strengthening of a dominant position"<sup>99</sup> on EEA-markets by the Star Alliance.

#### 4.3.3. Other factors

51. Other factors that can be usually considered in the overall competition assessment are the financial strength of the parties and their access to supply and sales markets.<sup>100</sup> In addition, pre-existing membership of an alliance or co-operation agreements with other airlines can constitute relevant factors in the assessment.<sup>101</sup> The factors noted here should not be considered an exhaustive list of relevant issues and their importance will vary in each particular case.

#### 4.4. Collective dominance

52. An airline merger or alliance may also cause a substantial restriction or the elimination of competition through the creation or strengthening of a position of collective dominance held by two or more firms. The provisions of European and national competition law which are relevant for the competition assessment of collective dominance are not specific to the air traffic sector. In general, the risk of creating or strengthening a position of collective dominance increases with the level of concentration in the market, market transparency and a history of coordinated behaviour by the firms. For example, concerns about collective dominance are particularly likely to arise if there has been coordinated behaviour between the firms in question in the past (e.g. weakened price competition in the form of price parallelism) and the relevant market characteristics have not changed appreciably.<sup>102</sup>

53. At present, the ECA has limited experience of enforcement action in relation to collective dominance arising from mergers and alliances in the field of passenger air transport. Most of the national competition authorities have not explicitly addressed the issue of collective dominance in relation to air traffic, although the

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<sup>99</sup> European Commission, case No COMP/M.2672 – SAS/Spainair, paras. 33–35 ([http://www.europa.eu.int/comm/competition/mergers/cases/decisions/m2672\\_en.pdf](http://www.europa.eu.int/comm/competition/mergers/cases/decisions/m2672_en.pdf)).

<sup>100</sup> See, for example, case Alitalia/Volare (see footnote 28 above), where the Italian Competition Authority considered the financial strength of Alitalia together with its distribution capacity a relevant factor in the overall competition assessment.

<sup>101</sup> See, for example, OFT, case BMI/United Airlines (see footnote 21 above), where the OFT considered efficiency claims put forward by the parties and found that some of the proposed efficiencies had already been achieved to some extent through the parties membership in the Star Alliance.

issue has been addressed by the European Commission, in particular in its decision in 1999 concerning the proposed SAir Group/AOM merger.<sup>103</sup> The European Commission considered whether the concentration would give rise to concerns about collective dominance by the parties (Swissair and AOM) on the one hand and Air France on the other. In the assessment several factors which are likely to increase incentives for parallel behaviour were considered, such as market and price transparency and other market conditions (e.g. demand growth, shifts in market shares). However, in this case the European Commission left open the question of whether Swissair and Air France held a position of collective dominance in the markets in question.

#### 4.5. Buyer power

54. In merger and alliance cases buyer power, in particular countervailing buyer power, may also constitute a relevant issue in the competition assessment. One or more buyers enjoy countervailing buyer power if they, by making use of their bargaining power, have the ability to obtain favourable purchasing terms vis-à-vis their suppliers. As a result suppliers may face competitive restraints stemming not from competitors but from buyers. With respect to the air traffic sector the general rules provided by European<sup>104</sup> and national law<sup>105</sup> are relevant for the assessment of buyer power. Neither European law nor the laws of the national states provide any sector specific rules.

55. Current case law of the European Commission and the national competition authorities regarding countervailing buyer power in the context of mergers and alliances in the field of passenger air transport is rather limited. None of the national competition authorities have explicitly addressed the issue of buyer power in relation to air traffic cases. However, it would be too early to draw the conclusion that countervailing buyer power is only a minor issue in the assessment of mergers and alliances in the field of air traffic. While in general individual customers (i.e. passengers) do not have any buyer power in relation to

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<sup>102</sup> See for example European Commission, EC horizontal Merger Guidelines, para. 43.

<sup>103</sup> See European Commission, case No IV/M.1494 – SAir Group/AOM, paras. 33 ff ([http://www.europa.eu.int/comm/competition/mergers/cases/decisions/m1494\\_en.pdf](http://www.europa.eu.int/comm/competition/mergers/cases/decisions/m1494_en.pdf)).

<sup>104</sup> See in particular European Commission, Commission Notice, EC horizontal Merger Guidelines, paras. 64 ff..

<sup>105</sup> See e.g. Bundeskartellamt, Principles of Interpretation, p. 31-33, 47f.

corporate suppliers (i.e. airlines),<sup>106</sup> some degree of buyer power might exist on the side of corporate customers. However, generally buyer power that arises only in relation to some segments of demand does usually not constitute a sufficient counterweight vis-à-vis a dominant position on the supply side.<sup>107</sup>

56. The issue of buyer power on the part of airlines, in particular in relation to travel agency services, has been considered by a number of competition authorities. However, this issue has tended to arise in cases of abuse of dominance rather than mergers and alliances. For example, the Italian Competition Authority found in the Alitalia/Assoviaggi case that Alitalia held a dominant position in the market for air transport travel agency services, and that Alitalia's conduct in relation to incentive schemes for travel agents constituted an infringement of Article 82 EC.<sup>108</sup> A second case of abuse concerning a failure to comply with the original decision was determined in 2002 and a fine was imposed on Alitalia.

#### 4.6. *Efficiencies*

57. As noted above, mergers or alliances, whether they take place in the field of air traffic or in other sectors, may have positive welfare effects in the form of efficiencies. However, the net welfare effect will generally only be positive if consumers (i.e. the passengers) benefit to a reasonable extent from the expected efficiency gains. In addition, in order to take account of the efficiencies claimed by the parties in the assessment there must be a causal connection between the merger or alliance and the possible benefits. As in other industrial sectors, the efficiencies claimed by the parties to a merger or alliance in the air traffic sector are usually of a productive or technical nature.<sup>109</sup> However, the ways in which these efficiencies are generated are specific to the air transport sector.

58. In general, the nature and extent of possible efficiency gains which can be realised by mergers on the one hand and alliances (as defined above) on the

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<sup>106</sup> In particular, when the supply side is highly concentrated as is frequently the case in markets for air transport.

<sup>107</sup> See, for example, European Commission, EC horizontal Merger Guidelines, para. 67; Bundeskartellamt, Principles of Interpretation, p. 33.

<sup>108</sup> See Italian Competition Authority, case Alitalia/Assoviaggi, decisions of June 2001 and July 2002. (see at [www.agcm.it](http://www.agcm.it)).

<sup>109</sup> From an economist's perspective three broad classes of efficiencies can be distinguished: allocative, productive (or technical) and dynamic (or innovative) efficiencies.

other are the same, although the legal framework under which they are assessed is different. The rules for the competition assessment of alliances are laid down in Article 81 (1) and (3) EC and Article 53 (1) and (3) EEA-Agreement or in the corresponding provisions of the national competition laws of the national states, whereas the assessment rules applied to mergers are provided by the EC Merger Regulation or by the merger control regimes of the national states.<sup>110</sup> The merger regimes of some national competition authorities (i.e. the German Bundeskartellamt) do not take into account efficiency gains.

59. To date the enforcement experience of national competition authorities regarding efficiencies in the field of air traffic is limited in relation to mergers, although there are several decisions concerning alliances. For example, the Italian Competition Authority considered efficiencies in its assessment of the code share agreements Alitalia/Volare and Alitalia/Meridiana.<sup>111</sup> In these cases the claimed efficiencies were measured mainly on the basis of load factors obtained after the agreement. In order to verify whether the efficiency gains would be transferred to the passengers the market structure was analysed. It was assumed that the greater the number of competitors operating on the route in question the more likely it was that the benefits would be passed on to consumers. In Alitalia/Volare the exemption was finally granted for 5 out of the 14 domestic routes included in the code sharing arrangement.
60. In BMI/United Airlines, the OFT considered an exemption application by BMI and United Airlines relating to their Alliance Expansion Agreement.<sup>112</sup> It was found that the proposed alliance did warrant an exemption under Article 81 (3) EC. The main efficiencies claimed by the parties were of a productive/technical nature arising from improvements to the quality and efficiency of services.<sup>113</sup> The OFT largely accepted the efficiencies put forward by the parties, although it argued

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<sup>110</sup> Generally there are no sector-specific rules in either EC or national competition laws concerning the consideration of efficiencies in alliance or merger cases in the field of air traffic.

<sup>111</sup> See Italian Competition Authority, Alitalia/Volare (see footnote 28 above); and Alitalia/Meridiana (see at [www.agcm.it](http://www.agcm.it)). In Alitalia/Volare efficiency gains were considered in order to evaluate whether it was possible to grant an exemption under Art. 4 of the Italian Competition Law n.287/90.

<sup>112</sup> See OFT, BMI/United Airlines (see footnote 21 above).

<sup>113</sup> It was expected that the alliance would lead to the rationalisation and harmonisation of services, the provision of new services and enhanced frequencies to city-pairs already operated. This was expected to result in an overall increase in traffic demand and economies of scale and scope arising from joining together the parties hub and spoke systems.

that some of these had already been achieved to some extent through the parties' membership in the Star Alliance. The OFT stated that it generally expected the alleged efficiencies to be quantified, although in this particular case, given the relatively limited overlap of the parties services, it was satisfied that there were sufficient benefits for an exemption to be warranted without further quantification.

61. The European Commission has considered efficiency gains in the air transport sector in several of its decisions concerning proposed alliances. A recent exemption decision is the Lufthansa/AuA alliance case noted above. While the agreement was found to be caught by Article 81 (1) EC, the European Commission considered that the agreement would contribute to economic progress within the meaning of Article 81 (3) EC. It was found that the parties' networks largely complemented one another and that these complementary networks would result in important synergistic effects as well as attractive connections for customers<sup>114, 115</sup>. However, the European Commission was not convinced that the agreement would allow customers to share the benefits of the expected cost savings and thus exempted the agreement subject to certain conditions. These are discussed in the section below.

## 5. Remedies

### 5.1. Introduction

62. The previous section described specific circumstances under which mergers and alliances in the air traffic sector may have significant anti-competitive effects. This discussion showed that it is likely that a merger or alliance will raise particular competition concerns in relation to one or more specific routes but in most cases, will not raise significant concerns in relation to the majority of routes affected by it. In such cases the competition authority faces a trade off between the overall positive welfare effect the merger or alliance is expected to have and

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<sup>114</sup> In particular, passengers were found to benefit from a wider choice of air transport services to more destinations, better connections and convenient scheduling.

<sup>115</sup> In 2001 the Hellenic Competition Commission cleared the merger of AEGEAN and CRONUS airlines (Decision Nr. 197 / ???/ 2001) also on the grounds that the operations of the merging parties were to a large extent complimentary, as AEGEAN operated exclusively on domestic routes, whilst CRONUS operated mainly on international routes and only up to a 30% on the domestic air traffic market.

the risk that effective competition will not be maintained on all routes affected. In this type of case the appropriate approach is for the competition authority to impose adequate remedies to deal with the competition concerns identified.

63. The legal framework for the imposition of remedies is defined by the relevant EC<sup>116</sup> and national competition law. As a rule, when designing remedies the principle of proportionality has to be taken into account.
64. With respect to the air traffic sector, designing remedies which are effective in preventing the anticompetitive effects of a merger or alliance is a relatively complex task. The specific features of the markets concerned, in particular the conditions of market entry, usually give an indication as to the possible types of remedies. Firstly, it has to be considered whether or not the markets affected are characterized by significant entry barriers. In the majority of cases remedies are directed at reducing existing entry barriers and enabling new airlines to enter the market, although remedies which promote links between various modes of transport may also be useful in certain cases (see below).

## 5.2. Types of remedies in the air traffic sector

### 5.2.1. Overview

65. The question of which remedies are appropriate in order to maintain effective competition in a particular case can not be answered in general terms. Rather, the remedies applied will vary depending on the competition analysis in an individual case. The following types of remedies - all of them aimed at reducing existing entry barriers and enabling newcomers to enter the market - have been applied in a number of cases:

- obligations regarding the *surrender of slots* at congested airports,
- obligations regarding *interlining and codeshares*,
- obligations regarding *conditions pertaining to blocked space agreements*,
- obligations to *open up frequent flyer programmes* of the parties to new entrants,
- obligations to *freeze or reduce frequencies*.

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<sup>116</sup> For a general discussion of remedies in merger cases under European law see European Commission, Notice on remedies acceptable under the Council Regulation (EEC) 4064/89 and under the Commission Regulation (EC) 447/98, OJ C 68 of 02.03.2001 ([http://europa.eu.int/eur-lex/pri/en/oj/dat/2001/c\\_068/c\\_06820010302en00030011.pdf](http://europa.eu.int/eur-lex/pri/en/oj/dat/2001/c_068/c_06820010302en00030011.pdf)).

Also other types of remedies have been used in specific cases, in particular obligations:

- regarding the *sale of particular assets*,
- involving *tariffs (so-called price reduction mechanism)*,
- for the parties to *enter into intermodal agreements*.

However, it has to be emphasised that not all of the remedies listed will be appropriate in every individual case, nor is the list exhaustive. In the following section each of the particular types of remedy mentioned is discussed further.

### 5.2.2. Discussion of particular remedies

66. Obligations regarding the *surrender of slots* at congested airports have been considered by national competition authorities as well as by the European Commission.<sup>117</sup> Such obligations have been considered to be essential in cases where potential entrants would not have been able to obtain slots at the airport at one or both ends of a route in question through the normal slot allocation procedure. The lack of adequate take-off and landing slots is generally a considerable entry barrier for potential entrants. The number of slots surrendered needs to be high enough to enable new entrants to operate a sufficient number of frequencies to exercise a significant competitive constraint on the parties.

67. In some cases a *cap on the percentage of slots available to the parties* at a congested airport may be appropriate. In BA/City Flyer,<sup>118</sup> the UK Competition Commission recommended that the share of slots available to British Airways (and its subsidiaries) be capped at 41 per cent of the available slots. It was also recommended that its share of slots available in any one hour be capped at 70 percent and its share of slots in any two-hour period be capped at 65 percent.

68. Obligations regarding *interlining and codeshares* have been used in some cases with the aim of enabling new entrants to effectively offer a higher frequency service.<sup>119</sup> They are useful in cases where a low frequency entrant has to

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<sup>117</sup> The surrender of slots was ordered, for example, in the following cases: European Commission, Air France/KLM (see footnote 34 above); Lufthansa/SAS/UA (see footnote 74 above); Lufthansa/AuA (see footnote 6 above), paras. 105 ff.; and Bundeskartellamt, Lufthansa/Eurowings (see footnote 19 above).

<sup>118</sup> See footnote 19 above.

<sup>119</sup> See e.g. European Commission, Lufthansa/SAS/UA (see footnote 74 above); Lufthansa/AuA (see footnote 6 above), paras. 105 ff. and annex; and case Air France/KLM (see footnote 34 above), para. 157 lit. (b) and annex.

compete with a high frequency incumbent, although their attractiveness to new entrants may be limited by the fact that they involve relying on their competitor to serve their customers.

69. Codesharing can be done on either a 'free flow' or 'block space' basis. 'Blockspace' code shares allocate a carrier (the marketing carrier) a certain number or percentage of reserved seats (blocked space) on flights of another party (the operating carrier). 'Free flow' codeshares allow the marketing carrier access to the operating carrier's inventory. The key difference between the two types of codeshare is that under blocked space arrangements the marketing carrier takes the revenue risk. As this generates increased competition between the marketing and operating carriers, blocked space codeshares are likely to be preferable as a remedy. For example, in Lufthansa/AuA and Air France/KLM *conditions pertaining to blocked space agreements* have been applied.<sup>120</sup>
70. Obligations to *open up frequent flyer programmes* of the parties to new entrants have also been applied in a number of cases.<sup>121</sup> However, such an obligation may involve some disadvantages from the entrants' perspective, as it provides the parties with details of the entrants' customers. Furthermore, as with obligations regarding interlining and codeshares, obligations to open up frequent flyer programmes have the inconvenience for new entrants of requiring them to rely on their competitor to serve their customers.
71. Obligations to *freeze or reduce frequencies* are aimed at preventing the parties from reacting aggressively towards a new entrant, thereby allowing the entrant to become established in the market.<sup>122</sup> However, the positive competition effects of these kinds of obligation must be weighed against possible negative effects on competition that may arise from preventing the parties from responding to changes in the markets. The length of the time period during which the parties are obliged to maintain the frequency freeze or reduction is a critical factor. For example, in Lufthansa/Eurowings the parties were obliged not to change their

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<sup>120</sup> See European Commission, Lufthansa/AuA (see footnote 6 above), paras. 105 ff. and annex; European Commission, Air France/KLM (see footnote 34 above), para. 157 lit. (f) and annex.

<sup>121</sup> See, for example, the European Commission, Lufthansa/SAS/UA (see footnote 74 above); Lufthansa/AuA (see footnote 6 above), paras. 105 ff.; Bundeskartellamt, Lufthansa/Eurowings (see footnote 19 above).

frequencies and seat capacities on particular routes from the winter 2001/2 levels during a start-up period of three years unless the competitor EAE was unwilling or unable to serve an increase in demand.

72. Obligations regarding the *sale of particular assets* (as for example the transfer of certain route services) was considered in exceptional circumstances by one of the national competition authorities. In Lufthansa/Eurowings<sup>123</sup>, Eurowings was obliged to sell at least five aircraft of the ATR 42 type to its competitor European Air Express (EAE) in order to enable EAE to start services on particular German domestic routes at the start of the winter 2001/2002 season as those assets had not been available to EAE on the open market.
73. Obligations involving *tariffs (the "price reduction mechanism")* have only been applied in a few alliance cases. As there is limited experience of such behavioural obligations they need to be applied very carefully on a case-by-case basis. The price reduction mechanism obliges the parties if they reduce fares on city pairs where entry occurs to also reduce fares by a similar amount on two or more routes on which they do not face any competition.<sup>124</sup> This remedy has two main objectives; it should ensure that price reductions by the incumbent are transferred to other routes where entry has not occurred; and it should prevent predatory responses by the parties. However, the positive effects of this kind of obligation must be weighed against possible negative effects on competition. As some price cuts which would have been introduced in the absence of the obligation might not take place or might be smaller, the price reduction mechanism may stifle competition that would otherwise have arisen from new entry.
74. Obligations for the parties to *enter into intermodal agreements* in particular with railway companies have been applied by the European Commission in specific

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<sup>122</sup> See, for example, European Commission, Lufthansa/AuA (see footnote 6 above), paras. 105 ff. and annex; Air France/KLM (see footnote 34 above), para. 157 lit. (d) and annex; Bundeskartellamt, Lufthansa/Eurowings (see footnote 19 above).

<sup>123</sup> See Bundeskartellamt, Lufthansa/Eurowings (see footnote 19 above); in contrast to this, the European Commission has never used commitments regarding the sale of particular assets in air transport cases.

<sup>124</sup> See e.g. European Commission, Lufthansa/AuA (see footnote 6 above), paras. 105 ff. and annex; Air France/KLM (see footnote 34 above), para. 157 lit. (g) and annex.

cases.<sup>125</sup> The aim of this remedy is to promote intermodal competition. The remedy is likely to be effective in markets where other forms of transport are substitutable for air transport, at least for non time-sensitive customers, and it is only likely to be relevant to short-haul routes. However, as experience of this type of remedy is limited, its effectiveness needs further observation.

### 5.2.3. Remedies of structural and behavioural nature

75. Pursuant to EC<sup>126</sup> and national<sup>127</sup> competition law as far as mergers are concerned, structural remedies are considered more straightforward than behavioural remedies because they are generally more clearly defined and/or identifiable and they are easier to enforce. However, under EC law whether a proposed remedy is behavioural or structural is not critical, the key factor is whether the proposed remedies are capable of rendering the concentration in question compatible with the common market.<sup>128</sup>

76. The enforcement experience of the European Commission and the national competition authorities in the airline sector shows that in most cases (including alliance cases) the imposition of structural remedies (alone) was not an option and it has been necessary to impose a coherent package of different remedies to tackle competition concerns. In the Air France/KLM merger<sup>129</sup> the European Commission designed the "slot surrender" remedy in a different manner to previous alliance exemption decisions in order to give a more durable effect to the "slot surrender" remedy. Firstly, the duration of the obligation to surrender slots is unlimited. Slots may be claimed by competitors at any point in the future,

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<sup>125</sup> See e.g. European Commission, Lufthansa/AuA (see footnote 6 above), appendix, no. 7: "At the request of a railway or other surface transport company operating between Austria and Germany (an intermodal partner), the Parties shall enter into an intermodal agreement whereby they provide passenger air transport on their services between Austria and Germany as part of an itinerary that include surface transportation by the intermodal partner (an intermodal service)."

<sup>126</sup> Under European competition law structural remedies are, as a rule, preferable in merger cases as the Court of First Instance stated in its' Gencor decision (CFI, T-102/96 – Gencor, ECR 1999, II-753, para. 319); see also European Commission's notice on remedies acceptable under Council Regulation (EEC) No 4064/89, and under Commission Regulation (EC) No 447/98, OJ 2001/C 68/03, para. 9.

<sup>127</sup> For example, pursuant to German competition law remedies in merger cases must be structural in nature. Pursuant to sect. 40, para. 3 of the Act Against Restraints of Competition, conditions and obligations imposed "dürfen sich nicht darauf richten, die beteiligten Unternehmen einer laufenden Verhaltenskontrolle zu unterstellen." ("[...] shall not aim at subjecting the conduct of the participating undertakings to a continued control.")

<sup>128</sup> See CFI, T-102/96 – Gencor (see footnote 126 above), paras. 318, 319.

<sup>129</sup> See Air France/KLM (see footnote 34 above), annex.

although the parties may be released from the obligation under the review clause. In that case, the entrant may continue to use the slots it has already requested and if it stops using these slots, they are surrendered to the slot coordinator and are not given back to Air France/KLM. Secondly, for a number of reasons entry on the hub to hub route (Amsterdam-Paris) was considered to be particularly difficult and concerns about hub dominance at the Paris airport were raised by competitors. In order to make entry more attractive, under certain conditions new entrants may be able to obtain grandfather rights for the slots released so that, once a new entrant has operated this route for a minimum of six IATA seasons, it may thereafter use the slots released at its discretion for any other city pair.

### *5.3. Monitoring issues*

77. In those cases where the remedies imposed on the parties require continued monitoring various mechanisms and procedures may be used. For example, in order to effectively monitor the parties' compliance with the conditions and obligations imposed in the recent Air France/KLM case the European Commission made a monitoring trustee part of the commitments package.<sup>130</sup> The 'monitoring trustee' was required to be an individual or institution appointed by (one of) the parties but independent of the parties and approved by the competition authority, charged with the duty of monitoring the parties' compliance with the conditions and obligations imposed.

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<sup>130</sup> See European Commission, Air France/KLM (see footnote 34 above), annex attached to the decision.