

**WORLDWIDE AIR TRANSPORT CONFERENCE: CHALLENGES AND
OPPORTUNITIES OF LIBERALIZATION**

Montreal, 24 to 29 March 2003

DRAFT REPORT ON AGENDA ITEM 2.3

Agenda Item 2: Examination of key regulatory issues in liberalization
2.3: Fair competition and safeguards

PART 1 – SAFEGUARDS TO ENSURE FAIR COMPETITION

Note - Consideration of this Item was divided into two parts: 1) Safeguards to ensure fair competition, and 2) Sustainability and participation.

2.3.1 Documentation

Secretariat (WP/11) examined the issue of how to ensure fair competition in a liberalizing environment, and believed that appropriate safeguard measures are needed during the transition. Such measures may include progressive introduction of liberalization, general competition laws, and/or aviation-specific safeguards. It also presented a proposal for a regulatory arrangement in the form of a model clause in air services agreements which States may use as an additional means to identify, prevent and eliminate anti-competitive abuses.

Georgia (WP/40 and WP/42) presented its views on a need for phased liberalization in tariff regulation, and on a need to assist weak airlines in developing countries through comprehensive commercial agreements.

Pakistan (WP/56) believed that effective measures to ensure meaningful participation should be in place before liberalization, and that a mechanism for maintaining healthy competition needs to be developed. It recommended that the Conference define criteria for determining what is capacity dumping or insufficiency.

United States (WP/47) believed that one of the most effective curbs on anti-competitive behaviour is operation of normal, undistorted market forces, and effective mechanisms are already in place, including general competition law, appropriate transition arrangements and other provisions of bilateral air services agreements. It saw no need to develop a sector-specific safeguard mechanisms for international air transport.

53 African States (WP/87) highlighted fair competition mechanisms being instituted in Africa to enable the continent to participate fully in air transportation, and expressed its concurrence with the conclusions and the proposed model clause in WP/11.

Members of ACAC (WP/70) recognized the importance for a system that guarantees fair competition in a liberalized environment and the need for a code of conduct and a dispute settlement mechanism, and suggested that ICAO update the code of conduct and safeguards related to fair competition and develop a dispute settlement mechanism for inclusion in the Template Air Services Agreements.

Members of LACAC (WP/99) presented, *inter alia*, their position on competition and safeguards, and believed that there should be safeguards to ensure fair and equitable

competition opportunities for the provision of air transport services in the liberalization process.

IATA (WP/28) emphasized the importance of and the need to maintain the IATA multilateral interline system and called on States to support the system and avoid its fragmentation.

ALADA (WP/71 - information paper) noted the LACAC position on this issue, and considered it necessary to reach an international agreement for application of competition laws so as to avoid legal uncertainty in the light of the new open competition scenarios.

2.3.2 Discussion

2.3.2.1 There was a wide range of views on the need for a safeguard to ensure fair competition when States undertook the liberalization of air transport services. In one view existing competition law was adequate for this task, but, in this connection, it was pointed out that not all States had competition laws, and moreover, there were differences in States understanding and application of such laws. Predetermination of capacity and double approval of tariffs along with other *ex ante* and *ex post* measures were offered as a means to prevent anti-competitive actions but there were concerns that this approach would nullify the benefits of liberalization. Furthermore, a detailed prescriptive list of what might constitute anti-competitive behaviour was not regarded as a good idea. Previous efforts to quantify terms involved in defining anti-competitive actions such as predatory pricing and capacity dumping had proved unsuccessful and it was pointed out that what might constitute unfair competition in one market may be acceptable competition in another one.

2.3.2.2 Nevertheless, a substantial number of developing States, citing the imbalance in their economies and airlines *vis-a-vis* those of developed States, saw a need for an aviation mechanism to ensure fair competition and safeguard their effective and sustained participation in international air transport. There was strong support for the mechanism proposed by the Secretariat in WP/11. However, care should be taken that this safeguard mechanism is not used to frustrate liberalization or result in pre-liberalization practices such as the predetermination of capacity.

2.3.2.3 There was also support for a code of conduct for fair competition which would rely on general principles. In this connection, it was noted that the Air Transport Regulation Panel had previously addressed this issue.

2.3.2.4 There was support for maintaining IATA's global multilateral interlining system although the increase in number and operations of low-cost air carriers and airline alliances appeared to undermine industry support for this program which enjoyed a privileged place in the international community. It was pointed out, however, that the number of airlines participating in the interline system remains high and efforts were being made to make it more efficient.

2.3.3 Conclusions

2.3.3.1 From the documentation and the ensuing discussion on safeguards to ensure fair competition under Agenda Item 2.3, the Conference concluded that:

- a) Liberalization must be accompanied by appropriate safeguard measures to ensure fair competition, and effective and sustained participation of all air carriers, regardless of their size and competitive strength. Such measures should be an integral part of the liberalization process and a living tool corresponding to the needs and stages of liberalization. Such measures may include progressive introduction of liberalization, general competition laws, and/or aviation-specific safeguards.
- b) While general competition laws may be an effective tool in many cases, given the differences in competition regimes, the differing stages of liberalization among States and the distinct regulatory framework for international air transport, there is in most cases a need for aviation-specific safeguards to prevent and eliminate unfair competition in international air transport. This may be done by means of an agreed set of anti-competitive practices which can be used, and if necessary modified or added to, by States as indications to trigger necessary regulatory action.
- c) In cases where national competition laws are applied to international air transport, care should be taken to avoid unilateral action. In dealing with competition issues involving foreign air carriers, States should give due consideration to the concerns of other States involved. In this context, cooperation between or among States, especially between or among competition authorities, and between such authorities and aviation authorities has proved useful in facilitating liberalization and avoiding conflicts.
- d) Harmonization of different competition regimes continues to be a major challenge. In cases where disputes arise from the use of aviation-specific safeguards or the application of competition laws, States should seek to resolve their disputes through the consultation and dispute settlement mechanisms available under relevant air services agreements, and in the case of the latter, by making use of the existing ICAO guidance on competition laws contained in Doc 9587.
- e) The extraterritorial application of national competition laws undermines cooperative arrangements regarded by many as essential for the efficiency, regularity and viability of international air transport, certain forms of which benefit both users and air carriers alike. Consequently, where antitrust or competition laws apply to such arrangements, appropriate immunity and exemption should be made available to permit inter-carrier cooperation, including interlining, to continue where they benefit users and air carriers.
- f) ICAO should continue to monitor developments in this area, and update its guidance material on competition and safeguards, where necessary and in light of the evolution of liberalization.

2.3.3.2 The Conference agreed that States should give due consideration to the following draft model clause as an option for use at their discretion in air services agreement.

“Safeguards against anti-competitive practices

1. *The Parties agree that the following airline practices may be regarded as possible unfair competitive practices which may merit closer examination:*
 - a) *charging fares and rates on routes at levels which are, in the aggregate, insufficient to cover the costs of providing the services to which they relate;*

- b) *the addition of excessive capacity or frequency of service;*
 - c) *the practices in question are sustained rather than temporary;*
 - d) *the practices in question have a serious negative economic effect on, or cause significant damage to, another airline;*
 - e) *the practices in question reflect an apparent intent or have the probable effect, of crippling, excluding or driving another airline from the market; and*
 - f) *behaviour indicating an abuse of dominant position on the route.*
2. *If the aeronautical authorities of one Party consider that an operation or operations intended or conducted by the designated airline of the other Party may constitute unfair competitive behaviour in accordance with the indicators listed in paragraph 1, they may request consultation in accordance with Article [_ on Consultation] with a view to resolving the problem. Any such request shall be accompanied by notice of the reasons for the request, and the consultation shall begin within 15 days of the request.*
3. *If the Parties fail to reach a resolution of the problem through consultations, either Party may invoke the dispute resolution mechanism under Article [_] to resolve the dispute.”*

PART 2 - SUSTAINABILITY AND PARTICIPATION

2.3.4 Documentation

Secretariat (WP/12) addressed, in the context of fair competition and safeguards, the issue of sustainability of air carriers and assurance of services, including the provision of State aids/subsidies. It concluded, *inter alia*, that States should ensure that aids/subsidies for the purpose of restructuring of air carriers and assurance of services do not adversely impact on competition by taking transparent and effective measures. The paper also discussed regulatory measures to ensure the effective and sustained participation of developing countries in international air transport, and proposed a regulatory arrangement on participation and preferential measures in the form of a framework for a “Transition Annex”.

53 African States (WP/82) reiterated the need for preferential measures on a non-reciprocal basis for developing countries as adopted by the 32nd Assembly. The paper pointed out that the situation in developing countries has still not improved despite the significant developments of air transport, and thus proposed that ICAO develop a model clause on preferential measures to facilitate their implementation.

2.3.5 Discussion

2.3.5.1 There was support for reaffirming the validity of preferential measures. There was also broad support for the measures to ensure sustained participation in air transport contained in the Secretariat paper WP/12, although the view was expressed that there was no need for the proposed Transition Annex if the existing bilateral agreement or its route schedule could be changed to achieve the same ends.

2.3.5.2 State aids/subsidies to airlines, which were transparent and did not distort competition, were regarded as acceptable means to sustain participation in international air transport. In view of the importance of tourism to the less developed countries, it was suggested that subsidized air services for essential tourism development routes, similar to the essential air services or public interest routes in developed countries, would be appropriate.

2.3.6 Conclusion

2.3.6.1 From the documentation and ensuing discussion on sustainability and participation under Agenda Item 2.3, the Conference concluded that:

- a) In a situation of transition to liberalization or even in an already-liberalized market, States may wish to continue providing some form of assistance to their airlines in order to ensure sustainability of the air transport industry and to address their legitimate concerns relating to assurance of services. However, States should bear in mind that provision of aids/subsidies which confer benefits on national air carriers but are not available to competitors in the same market may distort trade in international air services and may constitute unfair competitive practices.
- b) Because of the lack of an acceptable quantification method and the existence of various non-monetary measures, it is very difficult to estimate accurately the full scale of State assistance and the impact of specific State assistance on competition. Given this difficulty, States should recognize that any actions against foreign airlines which receive aids/subsidies might lead to retaliatory action by the affected State and hamper the ongoing liberalization of international air transport;
- c) There may be some instances where State assistance can produce economic and/or social benefits in terms of restructuring of air carriers and assurance of services. Even in such special cases, however, States should take transparent and effective measures accompanied by clear criteria and methodology to ensure that aids/subsidies do not adversely impact on competition in the marketplace;
- d) States should consider the possibility of identifying and permitting assistance for essential service on specified intra-regional routes of a public service nature in their air transport relationships;
- e) To ensure the effective and sustained participation of developing countries and to facilitate the liberalization process, States should take into consideration in their air transport relationships the interests and needs of States with less-competitive air carriers and, wherever appropriate, grant preferential and participation measures. Such measures may be incorporated in the "Transition Annex" in their air services agreements.

2.3.6.2 The following regulatory arrangement, in the form of a framework for a Transition Annex together with explanatory notes for its use, is proposed for consideration by the Conference for Contracting States to use at their discretion in air services agreements.

The following transitional measures shall expire on (date), or such earlier date, as is agreed upon by the Parties:

1. *Notwithstanding the provisions of Article ____ (or Annex ____), the designated airline (or airlines) of Party A (or each Party) may (shall)*
2. *Notwithstanding the provisions of Article ____ (or Annex ____), the designated airline (or airlines) of Party A (or each Party) may (shall) ... as follows:*
 - a) *From (date) through (date), ...; and*
 - b) *From (date) through (date),*
3. *Notwithstanding the provisions of Article ____ (or Annex ____), the following provisions shall govern*

***Explanatory Notes**

- a) The first clause would be used when a particular Article (or Annex) would not take effect immediately but be implemented in a limited way during the transition period. The second clause would be similar to the first clause but with phase in periods. The third clause would be used when an Article (or Annex) would not take effect immediately and a different scheme would be applied during the transitional period; and
- b) The following is an indicative list in the form of a framework for a Transition Annex, and is proposed for consideration by the Conference for Contracting States to use at their discretion in bilateral, regional or plurilateral air services agreements. The language in the Annex proposed by the Secretariat is a framework, into which the Parties would need to agree on the terms and wording. Doc 9587 contains material on possible participation and preferential measures.

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