



WORKING PAPER

**CONFERENCE ON THE ECONOMICS OF AIRPORTS AND
AIR NAVIGATION SERVICES**

Montréal, 15 to 20 September 2008

**Agenda Item 2: Specific issues related to airport economics and management
2.4: Non-discrimination aspects**

DIFFERENTIAL CHARGES

(Presented by the Secretariat)

SUMMARY

This paper discusses the positive and negative effects associated with differential charges and the ways to protect users from the negative effects. While differential charges could enhance economic benefits such as efficient use of resources, they could inherently distort competition both between airports and between users with the overall net effect varying according to a range of factors. The paper concludes that States should assess those effects on a case-by-case basis and ensure that differential charges meet the principles of non-discrimination, no cross-subsidization, transparency and time-limitation. To clearly reflect these principles, an amendment of the related text in *ICAO's Policies on Charges for Airports and Air Navigation Services* (Doc 9082) is proposed.

Action by the Conference is in paragraph 5.

1. INTRODUCTION

1.1 In recent years, airport operators have developed various forms of differential charges to attract and retain new air services, for example, incentive schemes for particular users and discounts on passenger service charges. Although the differentiation of airport charges *per se* is consistent with *ICAO's Policies on Charges for Airports and Air Navigation Services* (Doc 9082) and is a recognized commercial practice in the aviation industry, there is a concern that some of these charges might be discriminatory and non-transparent, and therefore anti-competitive.

1.2 This paper discusses the positive and negative effects associated with differential charges, as well as how to assess the overall net effect of the specific form of differential charges, and considers the ways to protect users from the negative effects. It also reviews the current relevant text of Doc 9082 related to differential charges.

2. DISCUSSION

2.1 There are various forms of differential charges, such as introductory discounts or rebates to airlines setting up new services (start-up aids), volume discounts, different charges levels at different times of the day (peak/off-peak pricing), and lower passenger service charges for terminals tailored specifically for low-cost carriers. If the different charges reflect differences in the cost of supplying the services, they can be regarded as cost-based. In many circumstances, however, the differences in the charges do not correspond directly to differences in the costs incurred in the provision of airport services but reflect rather the users' willingness to pay for the services concerned. The discussion below concentrates on such differential charges.

2.2 On one hand, differential charges could enhance economic welfare in terms of outputs and investments if properly designed. For example, at smaller airports, the provision of a start-up aid for airlines, which could reduce the risk of opening new routes, might enable them to attract more air services, and therefore reach the critical mass and the break-even point. At some congested airports, peak-hour charges might encourage more efficient use of existing capacity than a uniform charging system. Also, in capital-intensive industries like an airport, varying charges might improve investment signals in that particular airport market and facilitate the recovery of investment costs, thereby helping to secure that timely investments take place.

2.3 On the other hand, differential charges may have inherent adverse effects on both airports' and users' competition. For example, when airports have a great degree of market power, the differentiation of charges might be part of a credible strategy to prevent certain providers of airport services to enter the market. When airports are owned and operated by public authorities (which do not act as a private investor would in a market) or receive subsidies from States, the offering of lower airport charges for specific users may constitute a form of State aid for those users. The subsidization of the airport by the State could distort competition between airports and indirectly benefit specific users, for example, through lower airport charges, and thereby distort competition between users.

2.4 The magnitude of the overall net effect associated with a particular form of differential charges varies according to a range of factors, including the degree of market power of the airport (in general, the more competitive the markets is, the less likely that differential pricing will have any negative effects), the degree to which charges diverge from costs, the duration of the differentials scheme, and the number and categories of users affected. Whether specific differential charges are beneficial or harmful to users requires, therefore, a case-by-case assessment according to a particular situation. Considering that a certain form of differential charges could be harmful to users in some situations but beneficial in others, it would not be practical to try and identify any specific forms of differential charges in ICAO's policies in Doc 9082. Instead, it is more appropriate that the policies be confined to describing high-level principles for safeguarding users against potential negative effects of differential charges.

2.5 In this respect, some principles are already included in paragraph 23 iii) of Doc 9082, which recommends that differential charges should be in conformity with Article 15 of the *Convention on International Civil Aviation* (Chicago Convention, Doc 7300) and other principles in the policies, including two principles listed in paragraph 23, namely: a) non-discrimination between foreign and domestic users, as well as between two or more foreign users; and b) no cross-subsidization, i.e. any resultant under-recovery of costs properly allocable to the users concerned should not be shouldered on to other users. In practice, the principle of non-discrimination could be interpreted as "all categories of users meeting the same criteria and offering the same or similar air services should be treated equally".

2.6 Transparency is another important principle in the context of differential charges and should be included in paragraph 23. It should be noted that this principle does not mean that airports

should have to disclose any commercially sensitive information to the public, but to publish the existence of differential charges together with the purpose and the criteria on which they are offered. Also, where State aid is used to differentiate airport charges (and/or maintain charges at an artificially lower level), States should follow the conclusion of the fifth Worldwide Air Transport Conference (ATConf/5, 2003), i.e. States should take transparent and effective measures accompanied by clear criteria and methodology to ensure that aids/subsidies do not adversely impact competition in the marketplace.

2.7 There is another widely recognized principle with respect to the amount of time that an airport may provide particular categories of users with discounts, special rebates and other reductions of charges. Since the air services receiving preferential treatment are ultimately expected to become profitable (except for some essential air services of a public or social service nature¹), the imposition of the time-limitation may be appropriate specifically for start-up aids and similar incentive schemes to attract and/or retain new air services. The time-limitation of start-up aids has already been applied by airports in many parts of the world. Currently, however, only the *Airport Economics Manual* (Doc 9562) refers to the principle of time-limitation. In light of its general acceptance, the principle of time-limitation for start-up aids should also be reflected in Doc 9082.

3. CONCLUSIONS

3.1 From the foregoing discussion, the following conclusions may be drawn:

- a) In performing their economic oversight function States should, where necessary, assess the positive and negative effects associated with specific forms of differential charges applied by airports on a case-by-case basis according to local circumstances.
- b) States should ensure that differential charges are offered on a non-discriminatory basis; that they are transparent in terms of their creation, purpose and the criteria on which they are offered; that costs associated with them are not allocated, either directly or indirectly, to those other users not benefiting from them; and that, if the purpose is to attract and/or retain new air services, they are only offered on a temporary basis.
- c) ICAO should amend paragraph 23 of Doc 9082 to reflect the principles of transparency and time-limitation for start-up aids in the application of differential charges.

¹ The term essential air services refers to air services that a State may consider needs to be provided and where the market may not have sufficient incentive to do so (for example, lifeline air services for remote or peripheral destinations). In this respect, the ICAO Secretariat published a study on an Essential Service and Tourism Development (ESTDR) scheme in cooperation with the World Tourism Organization (UNWTO) in 2005 (www.icao.int/icao/en/atb/epm/Ecp/EssentialRouteScheme.htm).

4. PROPOSED AMENDMENTS OF POLICIES

4.1 In accordance with conclusion c) of paragraph 3.1, it is proposed to amend sub-paragraph 23 v) of Doc 9082 as follows:

- v) *Where any preferential charges, special rebates, or other kinds of reduction in the charges normally payable in respect of airport facilities are extended to particular categories of users, States ~~governments~~ should ensure transparency in terms of their creation, purpose and the criteria on which they are offered. ~~so far as practicable, that~~ Any any resultant under-recovery of costs properly allocable to the users concerned should not be shouldered on to other users. If the purpose is to attract and/or retain new air services, such reduction in the charges should only be offered on a time-limited basis.*

5. ACTION BY THE CONFERENCE

5.1 The Conference is invited to:

- a) review and adopt the conclusions in paragraph 3.1; and
- b) review and endorse the proposed amendments of Doc 9082 in paragraph 4.1.

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