

GOVERNMENT INTERVENTION IN AIR TRANSPORT IN THE EUROPEAN UNION

(Presented by Albania, Armenia, **Austria**, Azerbaijan, **Belgium**, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, **Denmark**, Estonia, **Finland**, **France**, **Germany**, **Greece**, Hungary, Iceland, **Ireland**, **Italy**, Latvia, Lithuania, **Luxembourg**, Malta, Moldova, Monaco, **Netherlands**, Norway, Poland, **Portugal**, Romania, Serbia and Montenegro, Slovakia, Slovenia, **Spain**, **Sweden**, Switzerland, The former Yugoslav Republic of Macedonia, Turkey, Ukraine, **United Kingdom**)¹

1. INTRODUCTION

1.1 Prior to liberalization in the EC, governments had traditionally played a major role in air transport provision, often being closely involved with the day-to-day operation of their national airlines. This was often based on an understandable wish to ensure that minimum levels of service were guaranteed and that the state maintained a viable domestic air transport industry.

1.2 However, in a liberalization process involving a number of states, such as the EC Single Market, it is important to ensure that competition between carriers from the different participating states is fair. The benefits of liberalizing a market will not be realized if certain players in the market are subject to special treatment by their governments. Discriminatory measures and, most importantly, State financial aid can distort competition by preserving over-capacity and enabling air carriers to engage in uneconomic pricing. In the case of the EC, the potential problems were recognized both in its founding treaties and subsequent legislation, which require non-discriminatory treatment for airlines and rigorous scrutiny of state aid.

1.3 Nonetheless, it was recognized in the early 1990's that after liberalization, governments would still retain certain strategic concerns about the level of air service provided on their territory and the need to maintain a viable domestic industry.

2. THE NEEDS OF THE AIR TRANSPORT INDUSTRY

2.1 The liberalization process removed the regulatory protection that most national airlines had enjoyed. In the early to mid 1990's, this led to a series of major financial problems at various European air carriers. A number of EC governments developed plans for capital injections and restructuring to ensure that those airlines survived.

2.2 The European Commission, which is charged with the enforcement of the state aid rules in the EC, accepted that there was a need for a period of restructuring in the airline industry. There was a clear need

¹ The 15 Member States of the European Union appear in bold

to allow some airlines to rebuild their balance sheets, restructure their operations and find a firm footing if they were to be able to take advantage of the new commercial opportunities available.

2.3 This restructuring was, however, subject to the so-called “one time, last time” rule, the idea being that this should be a one-off chance to restructure finances and operations. Prolonged government help would risk damaging the Community’s more competitive and successful carriers. Therefore, after this one-off restructuring, each company was required to survive on their own efforts according to normal commercial conditions. In this way, the means were found of guiding this strategically important industry through the initial shock of liberalization and laying the foundations for a competitive and vibrant market.

3. ONGOING INVESTMENTS

3.1 A small number of EU airlines remain partly or wholly state-owned. In order to ensure that shareholding governments and airlines conduct their relations on a commercial basis, all investments by governments are scrutinised by the European Commission. They are tested against the “market investor” principle - that is, the government must act in the same way as a commercial investor and is not permitted to give the airline terms that are unduly favourable. Capital injections from governments must normally be accompanied by similar injections from private investors.

4. REACTING TO A CRISIS

4.1 EC rules do also make provision to provide financial assistance to an industry in the event of a crisis. The tragic events of 11 September 2001 presented all airlines with just such a sudden economic problem of unforeseen gravity. The suspension of flights, the immobilization of equipment and the withdrawal of war risks cover, left the European industry with a serious financial shortfall and, in the area of insurance, an operational problem.

4.2 Governments were authorized to provide financial assistance in two ways. They were permitted to compensate their airlines for the losses they incurred as a result of airspace closure and were permitted to establish state systems to provide war-risks insurance in return for the payment of substantial premiums. Within a liberalized system, it is possible to give emergency assistance, but it is important to do so on the basis of strictly enforced common rules and non-discriminatory treatment.

5. ENSURING THAT SOCIAL AND REGIONAL NEEDS ARE SATISFIED

5.1 A further concern upon liberalization was the fate of routes that were uneconomic, but essential in social terms - typically those connecting peripheral regions with centres of commerce and government. Prior to liberalization, flag carriers often provided such services of social importance within their home state in their role as monopoly or state-sponsored provider.

5.2 In the process of restructuring and placing all airlines on a normal commercial footing, it was recognized as important for essential regional services to survive, even if they were not economic. It is important to note that the overall number of scheduled routes flown within the EU has grown substantially, however, there remain some thin routes that are vital to the health of a community, which must be preserved.

5.3 EC legislation therefore provides for a system of “public service obligations”, in which states may identify routes which are vital and conduct a tendering process in which all Community carriers have a right to participate, before awarding a contract to the best offer. This transparent system has ensured that the application of market economics to the air transport sector has not resulted in the loss of essential services.

6. CONCLUSION

6.1 State aid has to be reduced and controlled within a liberalized market in order to ensure that competition between airlines became fair and based solely on commercial principles. In the European Community, it proved possible to manage the withdrawal of government influence over airlines in such a way as to give the airline industry a one-off chance to adapt to the new conditions, and to introduce new mechanisms to ensure that communities do not lose essential air services.

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