

# Effective Regulatory Institutions for Air Transport – A European Perspective

**Prof. Dr. Hans-Martin Niemeier**

Round Table of 2-3 December 2010 on  
“Effective Regulatory Institutions: The Regulator’s Role  
in the Policy Process”

# Issues

- **Airline airport relationship under stress:**
  - “Airports are exploiting, in many cases, their natural monopoly position” (IATA, 2007)
  - “Airports are in tough competition” (ADV, 2007)
- **OECD: Need for rational dialogue**
- **Evaluate current regulation**
- **Options for regulatory reform BUT focus:**
  - **Institutional design of regulation**
  - **Value chain of air transport**

# Agenda

## I. Introduction

- why air transport is special

## II. Effective regulatory institutions for air transport

- Rationale of independent regulator

## III. Value Chain of Air Transport and Contracts

## IV. Regulatory intervention

## V. Summary: Reform of regulatory institutions

# I. Introduction

- **Airport commercialisation & partial privatisation**
- **Regulatory failure & reform: price caps & monitoring**
- **Competition among airports: De-designation of Manchester, but not of Stansted**
- **Commercialisation and Privatisation of ATC**
- **Liberalisation & privatisation of airlines: Access to & pricing of often scarce infrastructure**
- **External shocks risk of substantial losses**
- **Policy makers will face substantial rent seeking**

# I. Introduction

- Air transport is an industry with a mixture of competitive and monopolistic elements, different forms of ownership and levels of commercialisation all influenced by different types of implicit and explicit regulatory regimes.
- Two research questions:
  1. What parts of the value chain of air transport are ex-ante regulated?
  2. Is this ex-ante regulation carried out by effective regulatory institutions or should the regulatory institutions be reformed?

## II. Effective regulatory institutions

- Two rationales for an effective regulatory institution:
- *Economic rational* of ex-ante regulation:
  - Persistent market power & welfare gain
  - Regulated private monopoly
  - How to encourage private investment ? Not easy, because of
    - durable and immobile assets
    - specific exchange relation
    - information asymmetry and hold up.
  - Necessary: stability and commitment
- **Solution: Independent regulator, an institution with limited discretionary power which provides long term creditability and trust**

## II. Effective regulatory institutions

- *Political rationale* independent regulator
- Should politicians delegate discretionary power to an agency in order to avoid both inconsistent decisions over time and opportunistic behaviour ?
  - Public air transport infrastructure with long-term immobile asset-specific character
  - BUT elected governments only have power for a short period of time and cannot bind future governments
  - **Solution: Democratically governments should assign limited discretionary power to independent regulators which have expertise and are committed to long-term political goals.**

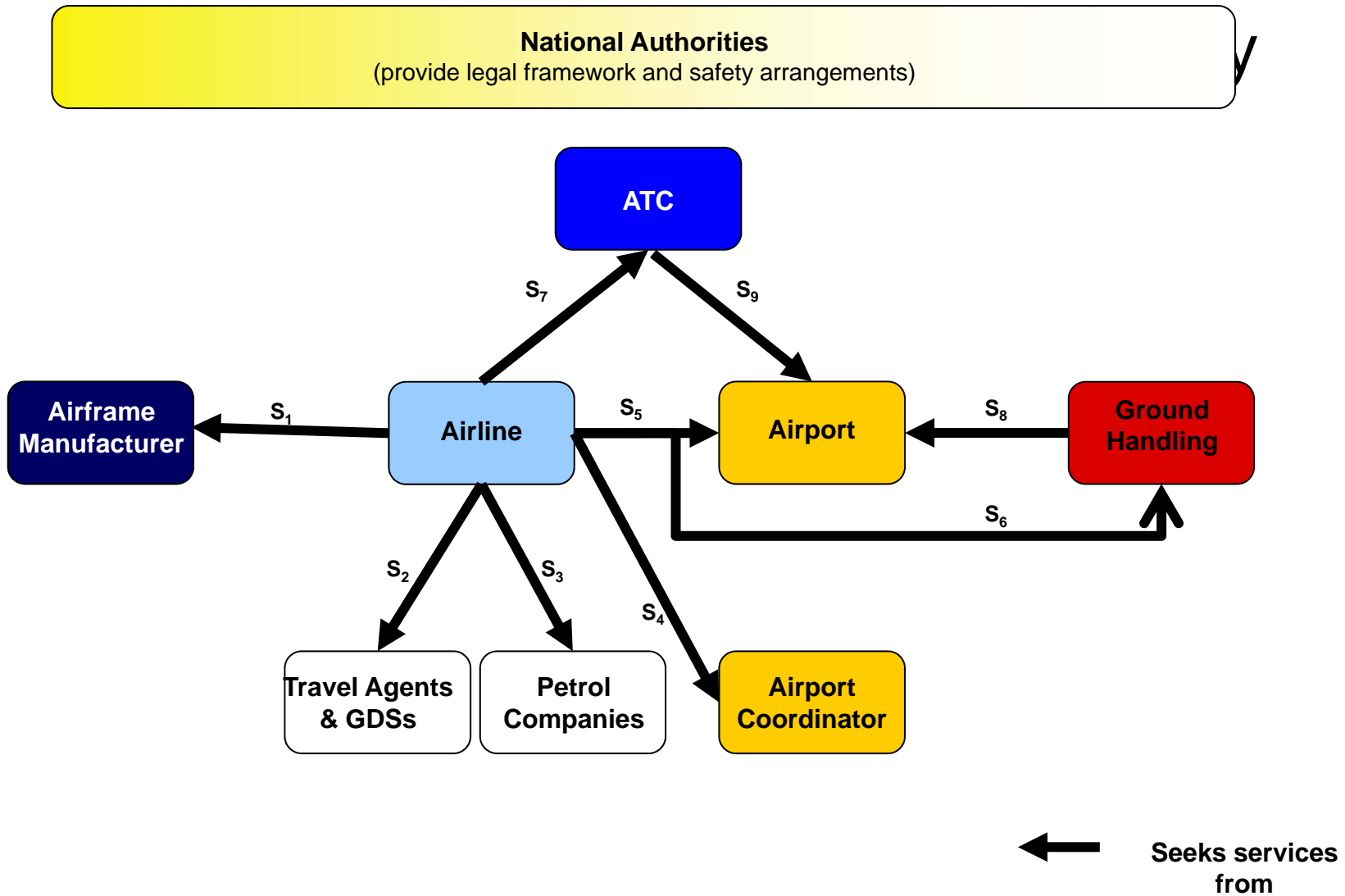
## II. Effective regulatory institutions

- Principles and criteria for effective regulatory institutions:
  - Legislative mandate from elected legislature
  - Independency and accountability to democratic bodies
  - Fair, accessible and open process
  - Cost effective regulatory processes
  - Well targeted and temporary





### III. Value Chain of Air Transport



# III. Value Chain of Air Transport

- **Forms of organization:**
  - **spot markets, private contracts, concession contracts, discretionary regulation, public enterprises and hybrid forms**
  - **All these organizational forms are practiced in air transport with the exception of a privatized vertically integrated public utility subject to regulation.**
  - **Typically a disaggregated approach has been adopted consisting of regulated infrastructure and a partly liberalized downstream market.**

## IV. Regulatory intervention

- In which parts of the value chain is it necessary for economic or for overriding political reasons to regulate ex ante?
- Which institution fulfils this task?
- Is this institution well designed or could it be more effective?

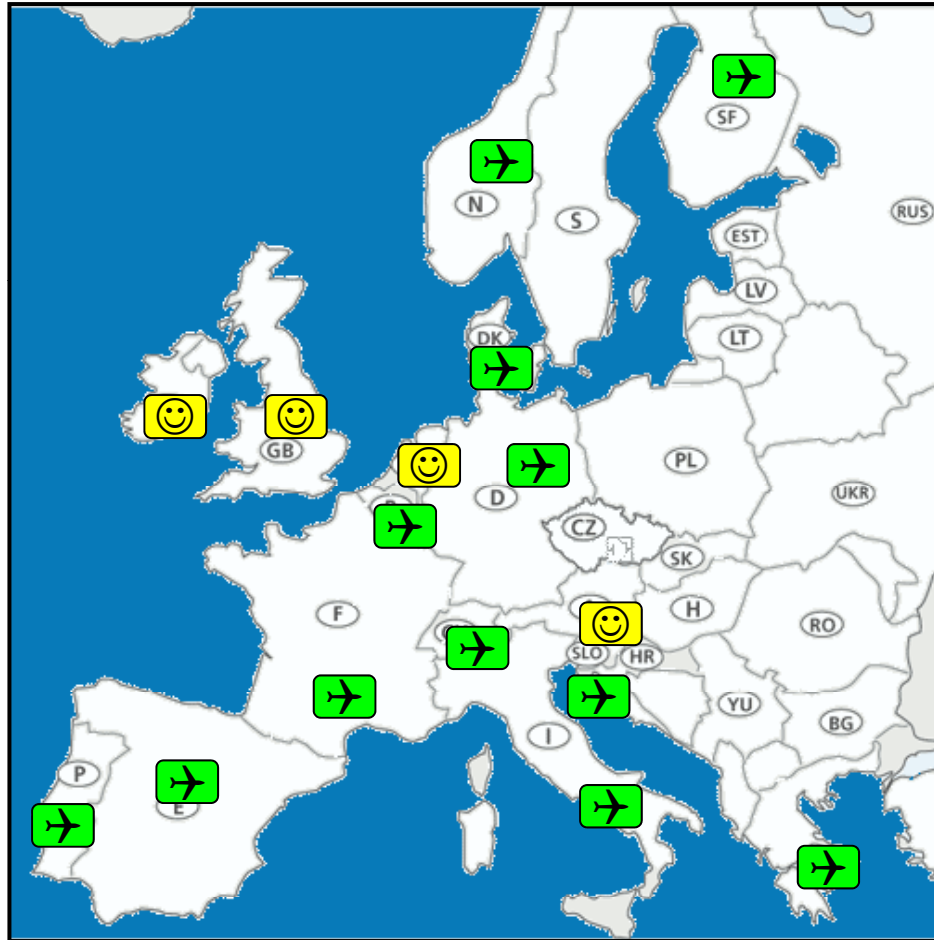
## IV. Regulatory intervention

- *Airlines*
  - Who decides on air service agreements (ASA)?
  - Who designates which competing carriers?
  - Who designates which competing airports?
- Department of Transport
  - ASAs create substantial rents for which stakeholders lobby effectively
- Australia:
  - DOT decides on ASA
  - International Air Services Commission allocates capacity

## IV. Regulatory intervention

- *Airports*
  - Are airports regulated by an independent body?
- *“Member States shall ensure that the independent supervisory authority exercises its powers impartially and transparently.”* EU directive on Charges
- **BUT:** Independency is not clearly defined and the directive allows member states to keep the status quo

# Regulation of European Airports



☺ Independent regulator (all with user consultation)

✈ User consultation without independent regulator

- Improved consultation
- **Lack of independent regulator**
- **Regulatory capture**

\* User consultation at Malta International Airport

OECD & ITF,  
Leipzig, 26 May 2009

Source: Gillen & Niemi, 2006

## IV. Regulatory intervention

- *Airports*
  - Who decides which airports are subject to regulation?
  - Who decides which airport services should be regulated?
- EU:
  - Directive: 5 Mio passengers
  - Only the UK, Netherlands and Australia have analysed the market power of individual airports
- Only few regulators have analysed in which services airports have market power. E.G. Australia

## IV. Regulatory intervention

- *Ground handling in EU*
  - How to provide non-discriminatory access to central infrastructure?
  - How to tender out the right to provide services at airports with a restricted number of providers?
- **Some EU Member States:**
  - Too many activities are declared central
  - Fee for central infrastructure not regulated
  - Tender process done by ministries with a majority share in airport providing ground handling services

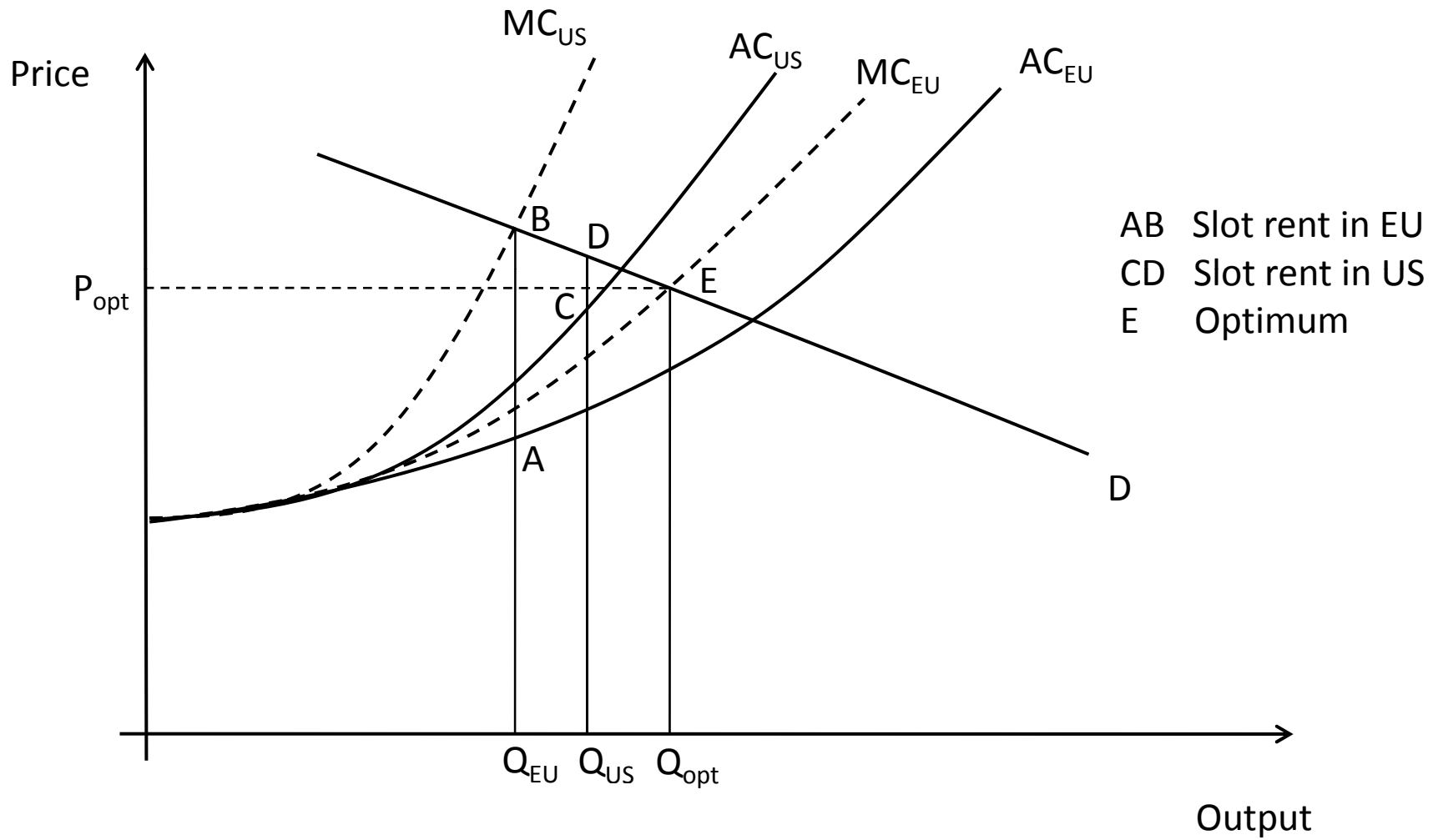


## IV. Regulatory intervention

- *Slots*
  - How independent is the slot coordinator?
  - And who sets the slot limit?
- EU:
  - IATA guidelines attempt to change the old system where slot coordinators cooperated with the dominant airline in the country.
  - DOT on EU member states set slot constraint.

Does the DOT get it right?

# Model of EU and US slot constrained airport



# V. Regulatory Reform

- *ATC*
  - How independent is the regulator of ATC?
- Single European Sky: “*The national supervisory authorities shall be independent of air navigation service providers*”. (Art. 4)
  - Dual role of EUROCONTROL
  - Australia , Ireland and UK have independent regulator. France not.

## VII. Conclusions

	Regulatory reform	Country
<b>Air Service Agreements</b>	First option, full liberalization. Second option, ASA by DOT and designation be independent commission.	<b>Australia</b>
<b>Airports</b>	Independent regulator for airports with market power. Designation of airports by DOT or commission.	<b>UK, Ireland</b>
<b>Ground handling</b>	First option, full liberalization. Second option, central infrastructure charge regulated by airport regulator and tender by independent airports or independent regulator	<b>Denmark, Ireland, Netherlands, Sweden UK</b>
<b>Slot allocation</b>	Independent slot coordinator with independent regulator on slot constraint.	<b>Australia</b>
<b>ATC</b>	<b>Independent regulator</b>	<b>UK</b>

## VI. Regulatory Reform

- **Current regulatory institutions are far from being effective to increase economic welfare.**
- **The greatest tensions are created when downstream markets are liberalized while the upstream the infrastructure market remains regulated by dependent regulators.**
- **Parts of air transport are unlikely to be subjected to effective competition**
- **Dependent regulators might effectively prevent competition by turning former natural monopolies into legal monopolies and allowing access discrimination.**

**Thank you very much!**

**Prof. Dr. Hans-Martin  
Niemeier**

# IV. Regulatory intervention

Service	Market power	Assessment
Air craft movement facilities	High	Essential facility
Passenger processing facilities	High	Essential facility.
Lounge	Low	No evidence to constrain supply of space
Vehicle access facilities	High	Incentive to shift demand to car parking
Car parking	Low/mod.	Short term parking limited by other modes
Taxi facilities	Low/mod.	Charges limited by competing modes
Aircraft refueling	Mod./high	High switching cost for refueling
Aircraft light maintenance	Mod.	Access to side for third parties
Aircraft heavy maintenance	Low	Low switching costs
Flight catering facilities	Low	Good off airport locations available
Freight facility & storage sites	Low	Good off airport locations available
Waste disposal facilities	Low	Good off airport locations available
Administrative office space	Low/mod.	Incentive to constrain supply of space
Commercial & retail services	Low	Retail rentals reflect locational rent

**Australian  
Productivity  
Commission  
(2002)**

**Prof. Dr. Hans-Martin  
Niemeier**

## IV. Regulatory intervention

### Ground handling in EU countries

Country	Deregulation	Regulation
Austria	Market share of partially privatised Vienna airport from 100% to 93 % in 1996 to 93 in 2002 to 89 % in 2007.	DOT decides on tender. DOT is separated from owner
France	ADP offers ground handling. AF self and third party handling. Penauille Servisclair is third part provider. Market shares in 2004: AF 65 %, 13 % ADP, Servisclair 13 %, Others 8 %.	Regulatory conflict as DOT is part government with majority stake in ADP and a minority share in AF/KLM
Germany	All airports offer ground handling except Berlin. Dominant position. Major shifts in Hamburg (0% of independent handler); Düsseldorf 30%, Munic 11 % for independent handler.	Regulatory conflict as Landesluftfahrt-behörde is part of government which has a majority share