TRANSPORT & ENVIRONMENT

September 2013

Briefing

State Aid for Airports & Airlines

Context

On 3 July 2013 the European Commission published revised draft guidelines on State aid to airports and airlines. The guidelines need to be urgently reconsidered as they risk further distorting competition, wasting scare public resources and expanding billions of euros in climate harmful subsidies.

Much more State aid than the Commission estimates

The Commission publishes figures for State aid in its scoreboard. The Commission arrives at average annual support over the 2006-11 of €396m a year for air transport[1]. Transport & Environment has performed an own analysis of all aviation cases decided on and reported by the European Commission between 2001 and April 2013. Our database reveals that since 2005 Member States have been granting the aviation industry an average €3bn of State aid every year. This figure is some seven times higher than that in the scoreboard. The real figure is probably much higher still. 70 cases are still pending with the Commission and have not yet been decided. In addition, the cases notified to the Commission by no means paint a comprehensive picture of the situation; much aid is not notified.

We estimate that €3bn of State aid increases CO_2 emissions from aviation by 3-5 Mtonnes.[2] This is the same order of magnitude as reductions coming from the sector's inclusion in the EU Emissions Trading System (with the full scope, i.e. all flights in, from and to EU airports). This conflicts with the Commission's White Paper target to reduce transport greenhouse gas emissions by 60% in 2050 relative to 1990 levels; a 70% reduction from today.

Aviation is very climate-intensive and already heavily subsidised

Aviation is the most climate-intensive form of travel. If aviation was a country it would be ranked 7th in the world for annual CO_2 emissions, between Germany and Korea. Aviation is responsible for about 5% of global warming[3] but is yet to be subject to effective mitigation. Aviation in the EU is exempt from both VAT and fuel tax – basic levies on almost all other sectors of the EU economy. This leaves a gap of almost €40 billion a year in national budgets.[4] The International Monetary Fund further agrees that aviation is undertaxed.[5] Also, it is to be questioned whether those that fly frequently are in need of subsidy at all. Even at Stansted, a UK airport dominated by low-cost airlines, the average household income of UK leisure passengers was more than a third higher than the national average[6].

For these reasons, it is indefensible to exacerbate distortions from under-taxation through direct State aid. This will encourage more flying and hence accelerate global warming. There are more efficient and lower-carbon ways to assist the economies of poorer areas.

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[1] http://ec.europa.eu/competition/state_aid/studies_reports/ws4_42.xls
[2] The climate intensity of low-fare aviation is around 4kg CO2eq/€ (http://www.transportenvironment.org/sites/te/files/media/2006-06_aviation_clearing_the_air_myths_reality_0.pdf) which is around 1.5kg CO2/€. There is currently (at least) €3bn of State aid given a year which leads to >€3bn x 1.5kg = 5MT CO2. An alternative way of estimating the impact is via turnover. €3bn State aid works out at around 2% of €140bn turnover for the EU airlines, which is equal to around a 2% subsidy. This means that fares are around 2% lower than they would be without State aid. With an elasticity of -1 this means 2% higher EU aviation emissions due to the subsidies, which works out at around 3MT of CO2.
[3] http://www.ipcc.ch/ipccreports/sres/aviation/index.php?idp=64
[4] http://www.transportenvironment.org/publications/does-aviation-pay-its-way
[5] Indirect Taxes on International Aviation, Michael Keen and Jon Strand, IMF, WP/06/124S
[6] http://stopstanstedexpansion.com/documents/For_richer_and_poorer_(FV).pdf

State aid to airports and airlines should be very limited

In some very limited circumstances there may be social and equity reasons for State aid to the aviation industry. There may well be a case for State aid to support services to remote islands in Greece for example or to the northern regions of Scandinavia. However, such services, which can genuinely benefit the public good, can be provided under a Public Service Obligation (PSO). This allows aid where: "part of the area potentially served by the airport would be, without the airport, isolated from the rest of the EU to an extent that would prejudge its social and economic development." However, potentially hundreds of 'regional' airports across Europe are in receipt of substantial taxpayer monies without providing a corresponding public benefit. These are the airports that this briefing focuses on.

The draft guidelines have no economic underpinning

We fail to identify a credible economic underpinning of the proposals for continued State aid. The Commission acknowledge that operating aid destroys the level playing field, "*operating aid is in principle a very distortive form of aid and can only be authorised under exceptional circumstances*." However, implicitly the draft guidelines suggests that improved connectivity and lacking economies of scale of smaller airports could justify State aid.

Improved connectivity cannot be a ground for State aid

The available documents do not demonstrate that aid to small regional airports would really promote regional growth. There is simply a presumption that this is the case because of better 'connectivity'. The most comprehensive study on this issue by consultancy CE Delft failed to find a causal relationship between the connectivity provided by such airports and economic growth.[7] What is more, if improved connectivity were reason enough for State aid, any transport activity or business could be subsidised.

Lacking economies of scale is a very questionable ground for State aid

The Commission document seems to implicitly say that that lacking economies of scale could justify State aid. *'Airports that have fewer than 1 million passengers per annum [are] typically struggling to cover their operating costs. Consequently the vast majority of regional airports are subsidised by public authorities on a regular basis'.* There is nothing exceptional to any small or medium enterprise having higher fixed costs, proportional to units of output, than larger enterprises. Such a justification could be used to allow State aid across the board in all sectors, thus this cannot be a justification to grant aid to small regional airports.

In addition the State aid currently given does not 'correct' for lacking economies of scale – it completely overturns them. After all, landing and passenger fees are generally much *lower* at smaller airports than at larger ones, not *higher*. If indeed smaller airports lack economies of scale, the fact that they offer lower rates can only be explained by excessive State aid.

Unsurprisingly, over the past decade, airports under than 1m passengers grew by 135%, airports under 5m passengers by 79%[8] and airports over 5m passengers by 'only' 29% between 2004 and 2012[9]. It seems small airports are exploding rather than struggling. State aid is the primary reason that smaller airports have grown so much faster than larger airports. This serious and unfair distortion of competition must be addressed urgently.

This also means that phasing out State aid is unlikely to lead to massive closures across Europe; more likely it will even out growth rates. Charleroi airport will not close down if Ryanair has to pay the real cost of the infrastructure. It will diminish the disparity in per-passenger fee paid by airlines at Charleroi and Zaventem (roughly €1.50 to €20). The

[7] http://www.cedelft.eu/publicatie/the_economics_of_airport_expansion/1363. *'Many studies find a positive correlation between aviation and economic growth, but no causal relationship between connectivity and economic growth was found.'*
[8] http://centreforaviation.com/news/aci-europe-regional-airports-have-seen-sustained-growth-of-international-traffic-over-past-decade-223054
[9] Analysis of Eurostat data from http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=avia_paoa&lang=en

levelling of the playing field will also likely mean that Charleroi's 15%-a-year growth rate will start to resemble more Zaventem's 2%. In fact, State aid should be out of the question as long as Charleroi offers rates so far below market rates.

This also means that much more transparency about these rates, including mandatory publication and inclusion in a publicly accessible database, is indispensable. Railway track access charges have to be published in a standardised format to ensure fair competition. This approach needs to be copied for aviation.

The consultation period should be extended

The draft guidelines are open to public consultation for less than three months, from 3 July to 25 September 2013. Most of this time is over the summer break, thereby restricting the ability of the public and the Members of the European Parliament to comment. It is vital that MEPs are given full opportunity to comment as the guidelines are in the sole control of the Commission and can be finalised without any Parliamentary scrutiny. Moreover, the Commission only proposes to release the Impact Assessment (the study of economic, social and other impacts) in conjunction with the final guidelines. This deprives the public, and the parliament, of the opportunity to comment on and understand the Commission's economic rationale for revising the guidelines as proposed. Thus we call on the Commission to release the Impact Assessment immediately and provide a further three months for public and parliamentary comment.

In detail - the proposed guidelines, and our views

The Commission proposes guidelines for three categories for aviation aid: infrastructure aid, operating aid for airports, and operating aid for airlines.

Infrastructure aid – what the Commission proposes ….
The Commission proposes to allow such aid in principle, but to vary the percentage of total infrastructure cost that can be subsidised between 0% and 75% depending on airport size. The smaller the airport, the higher the proportion of aid it is allowed to receive.

… and what should be done
We welcome the restriction on infrastructure aid but would urge a phase-out over time, and that any aid given in the transitional period should come in the form of a loan, not a grant.

Operating aid for airports – what the Commission proposes …
The Commission now propose to retroactively give the green light to past grants of illegal operating aid and to make operating aid legal for a transitional period of 10 years. In addition, they propose to apply the new rules to all pending cases concerning operating aid, regardless of whether the aid was illegal or not when granted. Meanwhile *existing* operating aid needs to be reduced by 10% a year, but there is no explicit prohibition on new grants of operating aid during this time, nor a requirement that new aid grants must be reduced year by year.

…and what should be done
Grants of operating aid that were illegal at the time they were given must be declared to be illegal. The retroactive approval of illegal behaviour by the many and various authorities involved working in close collaboration with the aviation industry will only ensure that the new guidelines are ignored as well.

We have grave concerns that the current proposal will allow for a mountain of new aid to build up over the next decade. The illegal nature of a large part of aid previously given may have acted as a break on such activities. Legalising it may well simply serve to open the flood gates. Where operating aid is already being issued, it is to be phased out by 10% a year. However, in the meantime the Commission proposes to continue allowing new grants of aid without such a mandatory gradual reduction. This will likely make it politically all but impossible to end the granting of operating aid in 2023. Limits need to be placed on the total aid, existing as well as new, during those 10 years to ensure that aid does not build up during this "phase-out". Thus we propose that the maximum intensity of old and new aid combined that can be granted to airports should decrease by 10% a year, in line with the reductions required of airports which are already receiving aid, so that if aid is granted in the 10th year of the phase out, it can only be for 10% of operating costs. Under the current proposal it seems that you could initially subsidise 100% of operating costs as there are no restrictions on the intensity of operating aid allowed to be given, the only restriction is that operating aid cannot be given at airports with more than 3m passengers.

More stringent requirements should be required for assessing business cases for the granting of aid. There should not be an automatic presumption that if the project fails there will be no requirement to pay back the aid. Also, such failed proposals should be taken into account when considering new proposals for other airports with similar passenger numbers.

Finally it is not clear how the Commission will ensure that the aid is reduced by 10% a year. Currently, much aid is not notified to the Commission and much illegal aid is given. States have become more and more sophisticated in making the aid less obvious (e.g. through intermediary companies and by underwriting debts). If the Commission does not have a full figure for all aid currently given across the EU, how the reduction of aid over a 10 year time period will be ensured is to be seriously questioned.

Start-up aid for airlines: what the Commission proposes ….

Start-up aid will now only be allowed for a two year period and only up to 50% of costs.

… and what should be done

While we welcome the tightening of this form of aid, we very strongly feel that – apart from some PSO cases as described above - direct State aid to airlines can never be justified. If airlines do not want to invest in new routes, despite enjoying almost €40bn worth of indirect operating subsidies annually, the routes simply should not be opened. Supporting some airlines but not others is bound to distort competition.

In addition to these comments on the specific types of aid, the following must be taken into account with regard to the draft guidelines in general:

- The final date for public comment must be extended so that there can be a proper debate on this subject;
- The Commission must release the Impact Assessment immediately and at least three months before closing the consultation;
- All grants (real and potential) of State aid must be notified to the Commission individually and clearly accounted for in one publicly available and transparent database. This is absolutely essential if the Commission is to continue with the idea that operating aid will be reduced by 10% a year;
- The transparency of airport charges required along the lines of rail track access charges, so that distortion of competition through state-financed ultra-low charges ends quickly.

The reasons illustrated in this short briefing add up to a powerful argument to phase out the use of taxpayer money for subsidies to the aviation industry as quickly, robustly and transparently as possible. The only justifiable aid to the industry can be in the form of a Public Service Obligation to an isolated region.

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