

# Reforming airport slot allocation in Europe: Making the most of a valuable resource

## purpose

This paper sets out the CAA's views on future reform of the European Regulations covering slot allocation and transfers, and explains why such changes are important to making the best use of Europe's busiest airports.

## how are slots allocated now?

The allocation of slots at all of Europe's most congested airports is governed by European Regulation 793/2004. This specifies the administrative allocation of unused slots ("the slot pool") by an independent slot coordinator and sets out the criteria and procedures to be used.

Under the current Regulation, once slots have been allocated by the coordinator, they can be exchanged, one for one, between airlines to allow for increased scheduling flexibility. The current surplus demand for slots at a number of congested airports in the UK and elsewhere across Europe means that coordinators have to rely on administrative rules to decide between competing demands for slots. As a result, an airline may be more likely to obtain a slot because of the nature of the rules, despite another valuing the slots more highly. Under the current rules, for example, airlines that have been in the queue for a long time or "new entrants" holding less than five slots a day at an airport have priority in the allocation system. These and other rules mean that slots are not necessarily allocated in a way that best reflects underlying airline and passenger demand.

Although the Regulation was reformed in 2004, the changes were technical and did little to change the fundamental rules governing slots. The CAA believes that more substantial reform is needed if better use is to be made of Europe's most congested airports.

## why change the rules?

The CAA has been a leading proponent of slot reform in Europe and has been exploring alternatives to the current administrative system of slot allocation. There are a number of reasons for this.

### **The issue is particularly important to airports in the UK...**

The UK has the most congested airports in Europe, so there is plenty of experience of the problems caused by demand exceeding supply. See Chart 1, overleaf, for an illustration of congestion at Heathrow.

## timetable

September 2004  
European Commission  
consults on slot reform

December 2004  
CAA and UK Government  
responses to EC consultation  
support secondary trading  
and auctioning

June 2005  
OFT and CAA complete joint  
report on 'Competition issues  
associated with the trading of  
airport slots.'

**Start 2006**  
**UK Government launches  
consultancy project to  
examine auctioning and  
other mechanisms for  
allocating new capacity**

Stage 1\*  
Possible publication by EC of  
proposals for reform of slot  
regulations

Stage 2\*  
Negotiations on reform of slot  
regulations completed

Stage 3\*  
Reformed regulations 'signed  
off'

Stage 4\*  
Regulations come into force

UK and other  
European member States  
implement reforms

Note: the timings of  
the stages marked \* are outside  
of the CAA's control

We also know that a secondary market for slots works; the UK already has significant experience of slot exchanges, which has provided a useful gauge of the likely demand from airlines for this form of additional flexibility. At London Heathrow, for example, slot transfers have exceeded the number of slots allocated from the pool for three of the last four years (see Chart 2 below right).

### ...but it's increasingly a pan-European issue

Making the best use of congested airports would bring benefits for passengers across the EU. For example, over 15 per cent of the 67 million passengers using the very congested Heathrow airport every year are non-UK Europeans.

Furthermore, the level of congestion at some European airports is increasing, as the popularity of air transport grows and the constraints on the expansion of airports tighten. This means that "capacity squeeze" is going to become a familiar problem across the continent. Frankfurt, Dusseldorf, Milan Linate, Paris Orly and London Heathrow and Gatwick already have excess demand throughout their operating day<sup>1</sup>. Such excess demand affects airlines' ability to access slots at these airports.

Furthermore, Eurocontrol<sup>2</sup> estimates that by 2010, more than twenty airports are expected to be short of capacity if current growth continues. This is estimated to rise to more than 60 airports by 2025, even allowing for the construction of all new capacity currently being built or considered.

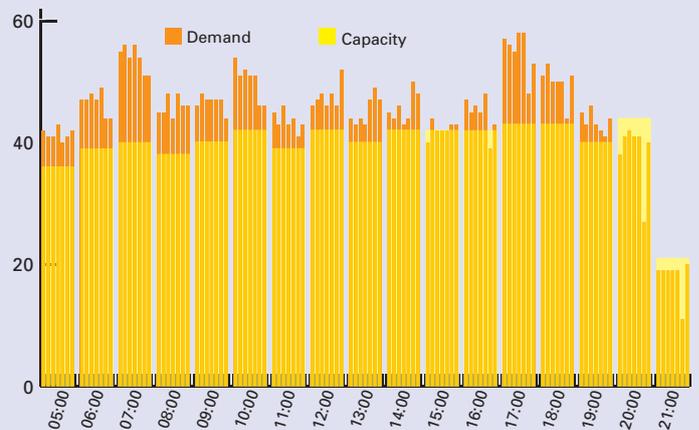


Chart 1: Excess demand over capacity at LHR (All arrivals, IATA Summer 2005 season)

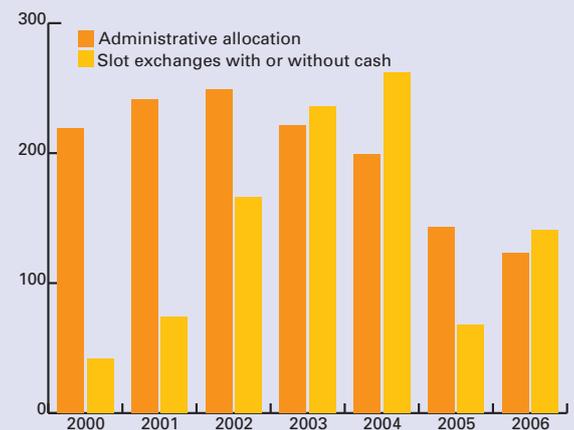


Chart 2: History of slot activity at Heathrow (2000-2006)  
(Source: UK Slot Coordinator, ACL Ltd.)

## the options for reform:

The following sets out the main options for reform to both the trading of slots by airlines (secondary trading) and the initial process of slot allocation (primary allocation).

### Secondary Trading

The existing Regulations allow for slot exchanges between airlines. Reforms could address:

- *The rules governing the exchange of slots.* This could confirm the legality of airlines exchanging slots where accompanied by payments in the form of cash or other consideration, as well as permitting straight money-for-slot purchases.
- *Trading design issues.* This would address questions such as whether there should be a minimum level of transparency for such transactions and whether bodies other than airlines should be able to participate in trades.

### Primary Allocation

The European Commission has examined a number of options for slots reform, ranging from minor changes to the administrative criteria currently used to allocate slots to more radical reforms involving the use of auctions to determine the initial allocation of new capacity:

- *Administrative improvements.* Altering the administrative criteria against which slot allocation decisions are made.
- *Posted Prices.* A process by which a fee is attached to each slot at an airport, thereby reducing demand by raising the cost of use. More sophisticated designs would differentiate prices between peak and off-peak slots, reflecting varying demand for slots at different times of the day.
- *Auctioning of slots.* Allowing slots to be allocated according to monetary bids submitted by airlines or other bodies.

Each option has different implications for the way in which slots would be allocated and the likely beneficiaries of slot transactions.

<sup>1</sup> Report commissioned by the European Commission: NERA (2004) *Study to Assess the Effects of Different Slot Allocation Schemes*.

<sup>2</sup> Eurocontrol (2004) *Challenges to Growth 2004 Report*.

## the CAA's favoured approach:

### **Secondary Trading**

The CAA believes that secondary trading of slots would benefit users and the long-term sustainability of the industry by allowing slots to be bought by those who value them most, reflecting the underlying demand from passengers. In the main, the CAA believes that the fewer restrictions on secondary trading, the greater the likely benefits. Slots should therefore be commercially tradeable for alternative slots or other forms of payment. Non-airline interests, such as regional bodies, should also be able to purchase slots, which could then provide an additional means of protecting regional air services.

However, some "light-touch" rules would be desirable. The CAA believes that a prohibition on the placing of restrictive covenants (conditions) on sales should be introduced to stop sellers fettering the future use of the slot. In addition, a rule requiring publication of the details of slot trades would help to encourage trading by making it clear what prices could be achieved. Finally, the requirement on minimum use (the "use-it-or-lose-it" rule) should be retained to ensure that valuable slots are not underused.

### **Auctioning of slots from new capacity, subject to proof of practicality**

Under an auction system, slots would be auctioned to the highest bidder (and then be tradeable in the secondary market). The CAA believes that the auctioning of slots from new capacity is attractive in principle, but recognises that there are practical issues to be resolved in relation to the ownership of slots, the mechanics of complex auction schemes and the interaction with any system of economic regulation of airports. The CAA is working with the UK Government and industry stakeholders on these issues.

### **A permissive approach to auctioning**

The need for auctioning at airports will depend largely on the competitive pressures and the degree of congestion experienced. Given these circumstances, *a permissive approach to reform that allowed individual countries to introduce more demand-responsive systems of allocation would be the best solution.*

This would allow airports in countries experiencing severe congestion to implement auctioning or other non-discriminatory systems of allocation at those airports, whilst leaving flexibility for others to apply traditional administrative approaches to allocation.

## reforms would benefit a range of stakeholders

### **For airlines, better access to scarce and valuable airport capacity would be attractive...**

Where airports have plenty of spare capacity, the allocation of take-off and landing slots is determined by the airline notifying the airport of its intention to operate a service and subsequent negotiation between those two parties.

However, as airports become more congested, the way in which slots are allocated takes on greater importance for airlines as it may effectively determine which airlines can operate services from that airport, and whether airlines are able to deliver the services passengers most want. This process therefore becomes of direct interest to all airlines and their customers.

### **For passengers, better methods of allocation would better reflect patterns of demand...**

Passengers benefit from airlines offering services and routes that most closely match their preferences and willingness to pay. A system of slot trading is the best way to ensure that slots go to the airlines that will most closely meet passenger needs.

### **For the environment, slot reforms would help make better use of existing capacity...**

Building additional runways and associated infrastructure brings with it environmental downsides in the shape of increased noise, air pollution and other local effects. It is therefore important to try to make the very best use of existing infrastructure - which slot trading (and, potentially, auctioning) would help to deliver - although more efficient slot use will rarely be a total substitute for new airport capacity.

## what are the challenges for reform?

### Ensuring the reforms are practical and workable...

The CAA and UK Government have both been keen to ensure that any alternative to the current system is *practically workable* - *not simply theoretically attractive*. For example, any reforms to the slot regulations will have to ensure that the new system is compatible with any bilateral obligations on slots and the regional IATA slot coordination conferences, which form the basis of international scheduling arrangements.

### Competition concerns...

How airlines and others access slots affects how competition in the relevant markets affected by congested airports might evolve over time. A joint report by the OFT and CAA shows that secondary trading should enhance efficiency and benefit airlines and consumers using Europe's most congested airports<sup>3</sup>. In the main, the fewer restrictions on secondary trading, the greater the likely efficiency benefits.

Nevertheless, the report notes that competition concerns could arise where secondary trading enables an airline to create or enhance a dominant position at an airport. The report suggests that this would best be addressed through a market investigation before trading has been introduced or afterwards if problems emerge. This would allow for a case-by-case approach, with remedies focused on the particular circumstances, rather than as a more onerous "one-size-fits-all" measure.

Competition could also be dampened through strategic behaviour by airlines when selling or leasing slots. The report argues that the design of the slot trading system should take account of this by preventing sellers from placing restrictions on how slots can be used in the future.

### Protecting against state aid...

It is important that the effects of any reforms are fair to all users. The rights of foreign carriers using European airports would be protected by a requirement for any trading scheme to be based on the principles of neutrality, non-discrimination and transparency.

One concern could be that state aided foreign carriers might unfairly outbid EU airlines for slots. Such concerns can be addressed through the system of international bilateral agreements, which gives Member States the ability to withhold the granting of additional access rights to partner states where they believe a foreign carrier or State is acting anti-competitively. The European Commission could also apply Regulation 868/2004, which is designed to investigate unfair pricing practices and subsidisation of third country airlines, to enable remedial action to be taken where unfair competition is identified.

### Promoting regional services...

Another concern could be that trading may result in a loss of regional services. However, any revision to slot rules would not affect the existing powers available to Governments to protect essential regional services through the Public Service Obligations ("PSOs") legislation. Slot trading could also open up opportunities for non-airline interests, including regional bodies, to purchase slots and thus protect regional services.

<sup>3</sup> OFT and CAA (2005) Competition issues associated with the trading of airport slots. London, HM Stationery Office. [www.caa.co.uk](http://www.caa.co.uk)



## responses to this paper

Queries or comments relating to the content of this briefing sheet should be sent, if possible by e-mail, to [dan.edwards@caa.org.uk](mailto:dan.edwards@caa.org.uk). Alternatively, they may be posted to: Dan Edwards, Economic Regulation Group, 4<sup>th</sup> floor, CAA House, 45-59 Kingsway, London WC2B 6TE.

**The CAA** is the UK's independent aviation regulator, with responsibility for all civil aviation regulatory functions: economic regulation; airspace policy; safety regulation; and consumer protection.