

# THE CAA'S REPORT INTO THE IMPACTS OF GRANTING FIFTH-FREEDOM RIGHTS TO PASSENGER SERVICES FROM UK REGIONAL AIRPORTS:

## SUMMARY OF STAKEHOLDER CONSULTATION RESPONSES

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### **Purpose of this document**

- 1.1 The CAA consulted on a draft version of the regional fifth-freedoms report between 21 March and 13 May 2005<sup>1</sup>. This paper details the main points made by consultees in that consultation and sets out the CAA's response, including any changes that have been incorporated in the final version of the regional fifth-freedom report.
- 1.2 Written responses were received from: the Airport Operators Association, BAA, British Airways, British Midland Airways, Manchester Airports Group, Monarch Airlines and Virgin Atlantic.

### **Recommendation: A Presumption in Favour of Granting Fifths**

#### ***The CAA's Initial proposals***

- 1.3 The CAA proposed that, consistent with the Government's policy on encouraging growth of the UK's regional airports and its general policy of pursuing sustainable liberalisation of existing aviation agreements, the Government should change its regional fifth freedom policy to one of a presumption in favour of granting fifths unless it can be credibly shown that it would have a net negative effect overall on UK interests.

#### ***Respondents' Views***

- 1.4 Respondents to the consultation document, voiced views ranging from a concern that the proposals did not go far enough, to a statement from one airline that liberalisation of fifth-freedoms from regional points should not be countenanced in the absence of reform of the restrictive UK-US Bermuda II agreement.
- 1.5 In the main, the level of support was broadly split between airlines and airports, with airports supportive of the change and the airlines more critical.
- 1.6 The main responses to the general policy recommendations outlined in the report were:

##### ***Airlines***

- a. One airline argued that the distortions brought about by the Bermuda II restrictions mean that no transatlantic fifths should be considered until full liberalisation of traffic rights between the UK and US has been achieved.
- b. Applications for fifth-freedoms should only be considered from countries with reciprocal arrangements.

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<sup>1</sup> The CAA also hosted a consultative meeting on 18 May to give respondents the chance to discuss views in person. No new points were raised at that meeting.

- c. Applications for fifth-freedoms should only be considered from countries with a high level of regulatory convergence, most notably in the area of state aid, as, without this filter, unfair competition would be encouraged.
- d. In light of the importance of the UK/US market, westward fifths from the UK should be treated differently from eastward fifths.
- e. Applications from airlines that plan to operate fifth-freedom services in competition to existing third/fourth-freedom services should be considered a 'special case', and the presumption should be against granting the rights.

#### **Airports**

- f. Fully support liberalisation of regional fifths.
- g. Freight services should be looked at similarly.
- h. Disappointed that Stansted and Gatwick were not considered as part of the study.

### **The CAA's Response**

#### *Linkage with Bermuda II*

- 1.7 In light of the responses, the CAA has considered its policy recommendations. On a fundamental level, it does not accept that the restrictions created by the Bermuda II agreement is a justifiable reason, either economically or strategically, to prevent the liberalisation of services from regional points, which are not directly affected by the access restrictions placed on London as a result of that agreement. UK carriers benefit from greater freedom to fly transatlantic services from regional airports and, although some distortions may arise through the displacement of what may otherwise be London-based services to regional points, this is insufficient justification to prevent further liberalisation of the routes.

#### *Reciprocity, State Aid, Westward 5ths*

- 1.8 The CAA acknowledges the points made on reciprocity, state aid and the difference between westward and eastward fifths from the UK. However, it believes that the policy of a reversed presumption in favour of granting the fifths still allows these issues to be properly considered on a case-by-case basis. Indeed, consideration of these issues could lead the Government to conclude that the request for fifths is best dealt with in bilateral discussions with the applicant nation.

#### *Effect on 3<sup>rd</sup>/4<sup>th</sup> freedom services*

- 1.9 In terms of the importance of direct third/fourth services to the industry and consumers, the CAA agrees that such direct services are generally of higher value than fifth-freedom services. Consequently, where a fifth freedom service can be shown genuinely to threaten to displace an existing direct service, then this might represent grounds for disapproving the application. However, the CAA does *not* believe that the existence of a third/fourth-freedom service should *automatically* trigger the refusal of an application, as certain routes may be capable of supporting additional services.

#### *Freight*

- 1.10 Addressing the concerns about the focus on passenger services in the study, the CAA recognises the value that could come from conducting a similar study into freight. However, freight tends to show vastly different characteristics to passenger operations, and as a consequence, it would not be possible to build freight into the models used in this study and a separate, very substantial piece of work, would therefore be necessary. It appears unlikely that the CAA will have the necessary resources to carry out such a study in the near future.

*Stansted & Gatwick*

- 1.11 In terms of the airports used for the study, the list of case studies was jointly agreed with the DfT in order to reflect the typical types of fifth-freedom request received and to be compliant with the definition of regional airports. The policy recommendations made by the study apply solely to UK regional airports, as the circumstances at London are different: fifth-freedom rights from London are likely to be more valuable and may therefore be a significant bilateral bargaining chip; the use of these rights is more likely to affect directly the operations of UK airlines; and the possibility that fifth-freedom services would bring net new activity or use spare capacity is lower.

**Recommendation: A Time-Limited Process for the Consideration of Applications**

***The CAA's Initial Proposals***

- 1.12 The report also consulted on the possibility of an expedited process for the consideration of applications, with the aim of deciding on applications within six weeks of receipt.

***Respondents' Views***

- 1.13 The time-limited process for the consideration of applications also received a number of comments:

***Airlines***

- a. Stakeholders should have the ability to submit views from day one on any application, rather than having to wait for the DfT to opine whether the application should go out for views, as proposed in the CAA's provisional report.
- b. Challenged what they saw as the implication in the report that a number of grounds for opposing an application would be "inadmissible".
- c. Suggested that the CAA should carry out an impact assessment on each application.

***Airports***

- d. Extremely supportive of the clear, time-limited nature of the process, which they regarded as an excellent marketing tool for attracting new business.
- e. Would like to see criteria for the refusal of fifths clearly and objectively set out.

## **The CAA's Response**

### *Submitting views earlier*

- 1.14 Generally, the positive response to the time-limited nature of the proposed process was encouraging. Nevertheless, it was recognised that the proposed procedure could be improved, most notably by enabling stakeholders to express their views at an earlier stage in the process. Consequently, the final report recommends publication of details of the application on receipt, allowing two weeks for interested parties to send in their views. This also has the benefit of shortening the overall length of the decision-making process.

### *Setting of criteria for the refusal of applications*

- 1.15 Given the varying circumstances that might apply in the consideration of any fifth-freedom application, it would appear unwise to be overly prescriptive in citing the reasons that might be considered as adequate grounds for opposing the granting of additional rights.

### *"Inadmissible" evidence*

- 1.16 The analysis underpinning the report supports the position that the effect of granting the additional rights on both negotiating leverage and existing third/fourth operations should be considered as the *key* issues. However, it does not suggest that other issues should not be 'admissible' where justifiable. Again, after consideration of the responses, the report remains largely unchanged in this area

### *Impact Assessment*

- 1.17 The CAA contends that this report and associated consultation process amounts to a thorough impact assessment of the proposed change in policy. In light of this and the drive for a more streamlined process for consideration of applications, it does not believe that the completion of an individual impact assessment for each application is necessary or desirable, as this would effectively lead to a continuation of the pre-existing process for consideration of appeals, with its long delays. Instead, we consider that the less prescriptive role for the CAA in advising the DfT on stakeholders' submissions is adequate, particularly as this is likely to include some assessment - albeit less mechanistic - of the routes in question. Consequently we have made no change to this part of the process.

## **Comments on the Methodology / Case Studies**

### ***The CAA's Initial Proposals***

- 1.18 The methodology and approach applied to the six case studies used for this report were all both set out in full in both the covering report and individual case studies.

### ***Respondents' Views***

- 1.19 In the main, the studies were praised. However, a couple of substantive points were made:
- a. There was some concern expressed about the assumption that consumer benefits arising from the start of a new service would be more durable than the negative effects on producers brought about by a loss of traffic to the new competitor.

- b. Disappointment that insufficient attention had been given to the indirect catalytic benefits that might arise to an airport and the surrounding economy from the operation of a new service. Had these been taken into account, it was claimed the net benefits from granting fifths would have been yet higher.

### **The CAA's Response**

#### *Durability of benefits*

- 1.20 When establishing the methodology and assumptions underlying the studies, considerable thought was given to the likely durability of both benefits and costs to UK interests. Traffic lost from London services will generally be restored through growth and airline disbenefits there will diminish. However, the report clearly acknowledges that some passenger gains arise purely because temporarily higher airline capacity has caused lower fares and these benefits may also diminish if the new service delays capacity increases in competing services.
- 1.21 Nevertheless, some effects may be more long lasting; for example, the gains to the regional airport from servicing a transit flow, which might otherwise have passed through an intermediate point outside the UK. In some cases a fifth-freedom service may allow passengers to travel direct to their destination from their local regional airport for the first time, creating surface access benefits which represent long-term gains if the route would have been of no immediate interest to a third/fourth-freedom carrier. The CAA therefore considers that the assumption regarding the superior durability of consumer and airport benefits is well based, and no change has been made to the methodology adopted for the studies.

#### *Assessment of indirect, catalytic benefits*

- 1.22 Lastly, the CAA stopped short of trying to assess the catalytic benefits that are likely to arise from the growth of fifth-freedom services at regional airports. Although the report acknowledges their possible existence, the difficulty in quantifying the size of such spin-off benefits was beyond the scope and resources of the study.

Economic Regulation Group

CAA

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