



easyJet's response to the proposed rules concerning the operation of Schiphol Airport

15th September 2014

Introduction

easyJet is Europe's fourth largest airline and flies on more than 700 routes between over 130 airports in 32 countries. We have been operating in the Netherlands since 1996; in fact Amsterdam was the first non UK destination for easyJet. Today, we are the second largest airline at Schiphol with a 9.8% share.

We welcome this opportunity to comment on the proposed Operating Decree in relation to Schiphol airport, which follows extensive discussion with the Ministry of Infrastructure and the Environment about the Dutch Aviation Act.

Throughout this process we have made clear our unease about the rules being put in place for the airport. We refer specifically to our responses to the Ministry's consultation on its proposed amendments to the Aviation Act dated 4th December 2013 and 14th January 2014. In our comments we have expressed our concern about the regulatory design within the Act which allows a dominant airport to set its own price cap using a dual-till approach.

We appreciate the constructive engagement we have had with the Ministry and acknowledge the efforts made to accommodate our concerns with regards to:

- transparency in setting charges and determining infrastructure investments;
- the contribution that that origin and destination traffic (O/D) makes to network quality; and
- a specific role for the Authority for Consumers and Markets (ACM)

Nevertheless, we consider that the regulatory structure does not provide adequate protection for consumers because it allows the airport to set its own charges without appropriate regulatory oversight to ensure that charges are not too high and are not discriminatory. We expect the Operating Decree to mitigate these risks and we outline below how it could better incorporate adequate safeguards in a number of areas.

1. Network quality

Origin and destination traffic makes a significant contribution to the Dutch economy through business and tourism and we therefore welcome the Ministry's proposal that direct connectivity is measured as a key element in network quality.

However, we remain concerned that network quality will be used to justify discrimination across airlines. This has been reinforced by the Ministry's written response to our questions of 19th August 2014.

We understand from Articles 10d and 13d that Schiphol will be required to measure performance of traffic across different segments and also assess the impact of tariffs and conditions on 'network quality' in a document which will be open to comment from airlines. However, since 'network quality' is a clearly stated policy objective, with differentiation of tariffs permitted where it is perceived to be in the public interest, the proposal for the airport to publish a document on network quality does not address the scope for discrimination.

We think it is important that the Ministry set out clear and non-discriminatory guidelines on how network quality should be assessed by Schiphol. Further, in assessing network quality against tariffs, Schiphol should not be able to use tariffs to adjust its network. Tariffs must be cost reflective.

In addition we note that the government should not be able to use Schiphol's tariffs to achieve its own policy objectives – doing this would be inconsistent with Airport Charges Directive, Competition Law and potentially state-aid rules. Network quality, and the value of connections, should be in line with the Luchtvaartnota (Aviation White Paper) - measured in terms of relevance to the Dutch economy and consumers. A strong European network – where The Netherlands earns two thirds of its national income – is therefore indispensable.

We propose that the Explanatory Note of the Operating Decree includes a reference to the Aviation White Paper which clearly links the concept of network quality with benefits for the consumer and the Dutch economy.

2. The dual-till approach

Whilst we recognise that the proposal for a mandatory contribution from non-aviation activities is an improvement on the previous voluntary contribution, we remain concerned about the maintenance of a dual-till arrangement since independent economic analysis concludes that a dual-till pricing results in tariffs above the competitive level, implying excessive prices and excess profits¹.

We also note that Schiphol has some degree of flexibility in determining what it perceives as the appropriate level of contribution given the Ministry of Finance's minimum required return on equity and 'other circumstances and conditions' which are not specified. In

¹ <https://www.frontier-economics.com/documents/2014/07/setting-airport-regulated-charges-frontier-report.pdf>

addition, Article 13c allows the airport to suspend the commercial till contribution due to unforeseen circumstances.

The proposed mechanism for determining the contribution from non-aviation activities leaves the level of charges exposed to the financial performance of activities which are completely unrelated to aviation activities such as real estate. The airport can risk commercial revenues in the knowledge that it may otherwise be forced to use them to lower airport charges. This could introduce distortions into the airports market and foster financial indiscipline at the airport.

We note that through this mechanism, users of Schiphol airport may end up funding Lelystad's infrastructure and operational costs.

If, as the economic analysis suggests, commercial revenues were rightly included in aviation activities, Schiphol would be able to set lower charges which would mirror those which would be set in a competitive market.

Given the above, we disagree that the ACM's duties should be to simply ensure that the process is followed in accordance to the law and ask for independent regulatory oversight which would include an assessment of the contribution required to prevent excessive charging.

3. Project groups on proposed investment plans

We welcome the plans to allow for greater consultation on investment plans, although we note that the project groups will only be formed to monitor the development of investments within the 5-year investment plan which limits the scope of the enhanced transparency to the implementation of Schiphol's overall plan. As we have highlighted in our response the Ministry dated 14th December 2013 the consultation process should ensure that all users' views are taken into consideration and reflected in the investment plan so that infrastructure investments benefit all users and all types of traffic.

In addition, there are areas where the project groups may not result in effective scrutiny. Specifically, Article 8 of the proposed operating decree states that only members of the investment project group will receive detailed information about projects and the Ministry is proposing that Schiphol itself determines the level of transparency about such investments.

It is therefore unclear about how those represented by an organisation e.g. BARIN or the AOC could contribute, for example how much information can an association share with its members in order to get their views? It is also not clear how those not participating in the project groups will be able to undertake informed scrutiny with the required expertise. Indeed there may be risks of 'regulatory overload' for project group members who could be deluged with detailed and complex information.

For these project groups to perform successfully, we therefore suggest that all airlines have full access to information, that they are able to appoint independent experts and that the airport funds the external expertise.

4. Role of the ACM

We welcome the expansion of the role of the ACM to include a process test on tariff proposals and ensuring that users are adequately consulted on investments.

However, we remain concerned that the regulatory design for the airport does not yet support effective independent regulation of the airport. Indeed the enlargement of the scope of the ACM's powers is largely restricted to supervision over the process in respect of tariffs, and of network quality with no scope to assess the justification for tariffs.

In particular, we note that although the ACM is responsible for ensuring that Schiphol has analysed the impact of the tariff proposal on network quality, paragraph 4.1 of the Explanatory Memorandum says that the remaining supervision is the responsibility of the Ministry of Infrastructure and the Environment. *"In view of preventing the abuse of a power position and in order to enforce the competition law, the sector-specific supervision shall remain with the ACM. The remaining supervision, including the supervision of the airport in the broadest sense, is exercised by the Minister of Infrastructure and the Environment."*

We are concerned that the ACM's role is limited to process in this area and also that there may be some ambiguity and duplication in the overlap between their responsibilities in this area and those of the Ministry.

As mentioned above, we are also disappointed that the Operating Decree limits the ACM's role in relation to the appropriate level of contribution from non-aviation activities by explicitly stating that the level is not suitable for assessment by the authority.

Appropriate regulatory safeguards should include a role for the ACM in ensuring that charges are not too high and are not discriminatory.

5. Weighted average cost of capital (WACC)

We do not agree that elements of the WACC should be fixed in law, and in particular the Equity Market Risk Premium which rises to 5.0% from 4.0% previously. These elements should be subject to public consultation and scrutiny in order to better reflect airport market conditions and also to increase transparency in relation to the decision.

6. Benchmarks

We welcome the decision that Schiphol airport (as opposed to the Ministry) should propose benchmarks in consultation with users. We feel that this will lead to a more accurate and informed benchmarking.

- **Quality benchmark.** We welcome the involvement of users in the development of the quality benchmarks. However, it is not clear how the performance of the airport against these benchmarks will be measured and whether there will be any independent and external oversight in this process. Without such a detailed independent oversight of the data, the assumptions underpinning it and how it is compiled we would be concerned that the results of the benchmarking may not be reliable.
- **Cost benchmark.** We welcome the inclusion of cost benchmarks and the role of the airport and users in their development. However, we are disappointed that there will be no

comparative benchmarking with other airports. We feel that the absence of this comparative data will reduce the value of the benchmarking information. Typically, internal benchmarking is most useful when it can be used to compare performance in an organisation across a range of different cost centres performing similar activities. It is unclear how this will be achieved in this case. Further, it is important to separate security costs from those concerned with aviation. We are also unclear about the policies which will be used to depreciate (or discount) the cost data and, again, we are not clear about how performance will be measured against these benchmarks. Without a detailed independent oversight of the data, the assumptions underpinning it and how it is compiled we would be concerned that the results of the benchmarking may not be reliable.

- **Tariff benchmark.** We welcome the inclusion of tariff benchmarks and the role of the airport and users in their development. For these benchmarks to provide meaningful comparative data we consider that it is important that (as far as possible) tariffs are compared for like-for-like services and that security and other non-aviation costs are excluded from the data. Given the complexity of establishing meaningful comparators we consider that it is important that there is detailed independent scrutiny of the data, of the assumptions underpinning it, and of how it is compiled. Without such an oversight we would be concerned that the results of the benchmarking may not be reliable.

Conclusions

easyJet welcomes the positive changes which have been made to the rules such as the inclusion of O/D in the concept of network quality and a mandatory rather than voluntary contribution from non-aviation.

However, while we welcome these changes they fall short of meeting our fundamental concerns about the broad thrust of regulatory policy and the potential for abuse of a dominant position. Under the proposed rules, the airport will still set its own charges under a dual-till approach and towards a broader policy of network quality, with restricted powers of the ACM which will only oversee due process.

Overall, we find it difficult to reconcile the proposed form of airport regulation with either the objectives of ensuring fair competition, as set out in the Aviation White Paper,² or with the principle of non-discrimination (between users of airports) set out in Article 3 of the Airport Charges Directive³.

We would hope, therefore, that there should be a more substantial move to address these issues before these rules are finalised. In particular, we consider that a model whereby tariffs are set using a single-till approach, with equal treatment between transfer and O/D passengers and where there was detailed public consultation about key regulatory issues, such as the cost of capital, would better serve the Dutch economy.

easyJet

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² Luchtvaartnota zoals verzonden aan de Tweede Kamer met brief VenW/DGLM-2009/1446

³ Directive 2009/12 EC: Article 3 reads; "Member States shall ensure that airport charges do not discriminate among airport users, in accordance with Community law."