COOPERATION AGREEMENTS (AIRLINES): THE LUFTHANSA CASE

Subject:	Cooperation agreements Market entry
Industry:	Airlines
Parties:	Lufthansa (Deutsche Lufthansa AG) Austrian Airlines (Österreichische Luftverkehrs AG)
Source:	Commission Statement IP/02/1008, dated 5 July 2002

(Note. The circumstances of this case show how the Air France / Alitalia case may turn out, if the Commission has its way. The terms of the arrangements made by Austrian Airlines and Lufthansa appear to be favourable to the consumer and to facilitate market entry and do credit to the Commission's attempts to remove restrictions on competition in this sector.)

The Commission has approved the partnership between Lufthansa and Austrian Airlines after the two airlines successfully resolved the Commission's concerns that consumers would be left with no choice of carriers between Austria and Germany and with the likelihood of higher prices. To prevent a quasi-monopoly in air services between the two neighbouring countries, the airlines offered to make available to new market entrants up to 40% of the airport slots used to operate flights on all bilateral routes such as for example Vienna-Berlin, Vienna-Frankfurt and Vienna-Stuttgart. Lufthansa and Austrian Airlines also agreed to reduce fares on the routes on which they do not face any competition to an extent similar to the fare reduction on city pairs where rivals start operations. The co-operation agreement was granted antitrust immunity retroactively from 10 December 1999, when it was activated, to 31 December 2005.

In December 1999, Austrian Airlines and Lufthansa notified a co-operation agreement with the Commission requesting an exemption under the European Community's competition rules. The agreement will, amongst other things, allow them to co-ordinate fares and schedules for all flights world-wide. After a careful examination, the Commission issued a Statement of Objections in May 2001, warning that the co-operation agreement, as originally conceived, could not be exempted as it would eliminate competition on virtually all 33 routes between Austria and Germany leaving travellers with no choice of airline and the likelihood of higher prices.

Subsequently, the parties offered a substantial package of remedies with a view to promote competition on the routes concerned and to ensure that consumers would not suffer from the parties' dominant position. Although the European Union's air transport market has been liberalised, high entry barriers, like the shortage of slots at main airports, the parties' high number of frequencies and the pooling of frequent-flyer programmes, prevent other carriers from entering the market. In the case of non-European Union airlines entry is made even more difficult by additional regulatory barriers.

On the basis of the undertakings made by the Parties, the Commission could establish that several competitors are seriously interested in entering major routes between Austria and Gemany. In fact, Adria Airways of Slovenia last year started flying twice a day on the Vienna-Frankfurt route and Air Alps operates a daily flight between Vienna and Stuttgart following the offer by Lufthansa and Austrian Airlines, even before the Commission took its final decision, to apply the remedies. In addition, two other airlines from central and eastern Europe have expressed a serious interest in entering two further major routes between Austria and Germany and a new Austrian airline, Styrian Airways, has been created which plans to start operations on a number of additional routes this autumn.

To create conditions for competition between Germany and Austria, Austrian Airlines and Lufthansa have to make available up to a maximum of 40% of the slots they operate on any given city pair to any newcomer wishing to operate the routes and which would not be able to find those slots through the normal slot allocation procedure. Each time they reduce a published fare on a route where they face the presence of a new entrant, Austrian Airlines and Lufthansa will be obliged to apply the same fare reduction, in percentage terms, on three other Austrian-German city pairs on which they do not have competition. The purpose of this obligation is to ensure that passengers enjoy the benefits of competition including routes on which Austrian Airlines and Lufthansa maintain a monopoly position.

Austrian Airlines and Lufthansa are further obliged to allow new entrants to participate in their frequent flyer programmes if they do not have their own and if they so wish. Other commitments relate, for example, to interlining, that is, the ability for passengers to travel on more than one airline on a given journey based on a single ticket and to enter into special pro rata agreements comparable to those entered into with other alliance carriers. To ensure that new entrants are not squeezed out of the market shortly after entry, parties are obliged to maintain a frequency freeze during a start-up period of two years. Finally, Austrian Airlines and Lufthansa will have to enter into inter-modal agreements in particular with railway companies, to ensure greater choice and better transport services for consumers.

In December 1999, Austrian Airlines and Lufthansa had notified the cooperation agreement to the Commission, requesting an exemption. While examining the notification, the Commission received numerous complaints from individuals as well as corporate customers concerned about high fares between Austria and Germany. The Austrian tourist sector also complained about the potentially negative effects for Vienna as a tourist destination. However, on 14 December 2001, the Commission published a full description of the undertakings made by the parties. It received comments from IATA, the Austrian federation of hotels and a new start-up airline, Styrian Airways, which were taken into account when the Commission reached its final decision. ■