



Konkurransetilsynet
Norwegian Competition Authority

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■ **Comments - Consultation paper on the possible revision of Regulation 2299/89 on a Code of Conduct for computerised reservation systems**

The Norwegian Competition Authority (NCA) refers to The European Commission's consultation paper concerning the possible revision of Regulation 2299/89 on a Code of Conduct for computerised reservation systems.

Below, the NCA will present answers to selected questions presented in the consultation paper.

On a general level

Q1. In the light of the described market developments, is there still a need for the sector-specific competition rules imposed by the Code of Conduct? Or should the Code of Conduct be revised or abolished?

The consultation paper points out that the CRS (Computerised Reservation Systems) market has undergone important changes in recent time. First, direct bookings have increased, due to the Internet, and are expected to be the subject of continuing growth. The growth of direct bookings is decreasing the CRSs role as an essential intermediary in the air travel distribution market. Second, many airlines have divested their CRS ownership. Three of the four CRSs (Galileo, Worldspan and Sabre) are no longer owned by airlines, and airlines only have a minority shareholding in Amadeus. The vertical integration of airlines and CRSs which gave the airline-owned CRSs the incentive and ability to restrict competition in both the airline and the CRS market was one of the main reasons for the adoption of the Code of Conduct. As the airlines to a large extent have divested their ownership in CRSs, it may be argued that there is less grounds for the Code of Conduct in the CRS market today. It is also worth mentioning that the CRS regulation has been abolished in the USA and revised in Canada.

On the other hand the consultation paper shows that CRS still plays an important role in the air travel distribution market. The Commissions estimates show that in 2005, CRS sales accounted for 62 % of the total bookings in the EU27, while direct (non-CRS) sales only accounted for 38 % of the total bookings in the EU27.¹ According to the consultation paper, these figures vary between Member States depending on the market share of low-fare airlines and on Internet

¹ Figure presented in the Consultation Paper page 8



penetration rate in households and companies. The consultation paper also points out that data on the number of bookings may overstate the importance of direct sales in terms of revenue as a higher proportion of high-value tickets are being sold via CRSs (business travels and complex itineraries). Numbers from the Association of European Airlines shows that these airlines get 80 % of their revenue from bookings made by "CRS-powered" traditional travel agents.² The consultation paper also predicts that on-line travel agencies will continue their strong growth rates. These travel agencies represent serious competitors to the airline websites. As they are mostly "CRS-powered", they will help the CRS to partially offset the loss of market share of the traditional brick-and-mortar travel agencies. The CRS providers have already invested in some of the most important online travel agencies: Amadeus in Opodo, Sabre in Travelocity and Lastminute, and Galileo in Orbitz and Ebookers. These travel agencies represent almost half of the online market in Europe. At the same time it is likely that low-fare airlines, in order to tap into the market of the customers of traditional travel agents, may be increasingly interested in utilizing CRS.

As mentioned above, the airlines limited ownership in the CRSs has to some extent reduced the risk of anti-competitive behavior in the relevant markets, but the consultation paper points out that airlines still have a substantial ownership in Amadeus, and some national flag carriers still have stakes in the national marketing company (NMC) which promotes the most common CRS in their home market. Specifically, Finnair, Estonian Air and CSA Czech Airlines own a share of the Amadeus NMC in their home markets. Similarly, Austrian Airlines, Malev and Olympic Airways are part owners of the Galileo NMC in Austria, Hungary and Greece respectively. It is also possible that the airlines consider it profitable to re-establish their control over the CRS if the Code of Conduct is abolished. The airlines and the other participants in the market can also seek to discriminate against competitors through the CRS irrespective of ownership.

Based on the points stated above the NCA believes that there is still a need for the sector-specific competition rules imposed by the Code of Conduct, however market developments and experience with the Code of Conduct indicates that a revision of the rules imposed by it may suffice.

The main objective of the Code of Conduct must be to ensure effective competition in all chains of the air travel distribution market: between airlines; between airlines and the CRS vendors; between airlines and the travel agents; between CRS vendors; between CRS vendors and the travel agents; and between travel agents.

As the CRS still is an essential intermediary for the airlines it is important that the Code of Conduct ensures the airline access to it in order to compete in the air travel market. It is also important to prevent discriminatory behavior from the CRSs, especially in the CRS principal display. This also affects consumers as they need neutral and complete information from the CRS when they search for the most adequate travel option at the best price.

The consultation paper points out that experience with the Code of Conduct shows that the Code's non-discrimination requirement limits price competition, because if CRS vendors provide a discount to one airline, they must provide it to all. Another example is the mandatory participation rule which effectively requires parent carriers to purchase the same level of services from all CRSs, and significantly limits these carriers' leverage to negotiate better fees and terms from any individual CRS. It is also argued that other participating airlines de facto can feel obligated to purchase services from all the CRS providers in order to reach all of their potential customers as travel agents uses different CRSs. As such, CRS vendors may lack normal market incentives to seek increased sales by lowering their fees.

An abolishment of these rules could therefore strengthen price competition in both the airline and CRS market and encourage innovation by allowing airlines to use their leverage to bargain and thus force CRSs to compete more aggressively for airline participation on the basis of price

² Figure presented in the Consultation Paper page 10



Konkurransetilsynet
Norwegian Competition Authority

(booking fees) and service quality. These predicted effects are also stated by the Brattle Group and Norton Rose in their study of the CRS market on behalf of the European Commission, completed in October 2003. However, it is uncertain whether this increased price competition will benefit the consumers sufficiently. The reduced booking fees from the airlines to the CRSs would probably lead to decreased payments from the CRSs to the travel agents. In this case the travel agents may increase their service fees to the consumers to cover up their loss in income. High booking fees can consequently benefit consumers in form of reduced service fees, but the high CRS profit can also represent an efficiency loss as it is not likely that all the profit converts into higher payments to travel agents.

In any case, it is important that the Code of Conduct functions as a safety valve against highly discriminatory pricing that has the same consequences as refusal to supply CRS services.

Q2. Given the described market developments, has the risk of market foreclosure not reduced and are general competition rules (Article 82 of the Treaty in particular) not a sufficient remedy/deterrent against these risks?

Sector-specific competition rules imposed by the Code of Conduct have the advantage - to a greater extent than general competition rules - of preventing anti-competitive behavior. General competition rules only applies when the anti-competitive behavior has happened (ex post), while the Code of Conduct regulates the behavior of participants in the CRS market in such a manner that it effectively prevents anti-competitive behavior ex ante. It is also difficult to detect abuse ex post. The NCA would also like to point out that Article 82 of the Treaty has relatively strict conditions that must be fulfilled before it is applicable; the involved undertakings must have a dominant position in the relevant market, and their actions must constitute an abuse. The Code of Conduct can more easily be applied for securing effective competition in the air travel distribution market. When considering the need for sector-specific competition rules the risk of anti-competitive abuse in the relevant market is decisive, and so are the potential consequences of this abuse.

The NCA believes that the described market developments do not necessitate a total abolishment of the Code of Conduct. The market alterations are not sufficient for such measures. Indeed the CRS have lost some market share to direct booking and the airlines no longer controls the CRSs, but the consultation paper shows that the CRS still plays an important role in the air travel distribution market. Furthermore it is not necessary for the airlines to control the CRSs through ownership in order to use them in an anti-competitive manner. It is also a risk that the airlines will re-establish their interests in the CRSs if the Code is abolished. Since the risk of market foreclosure is not substantially reduced, it is reasonable to say that the general competition rules may not be a sufficient remedy/deterrent against these risks. The risk of anti-competitive behavior is indeed present, and it is therefore a legitimate need for sector-specific regulation. Ex ante regulation is especially needed in markets which contains services that are essential for market participation in other markets; in this case the air travel market. Abuse of CRS in this market can be fatal for targeted airlines. A common objection to ex ante regulation is the danger of unintended consequences of the regulation. This objection is particularly rightful when new regulations are considered imposed. The Code of Conduct was adopted in 1989, and there has been sufficient time to detect its flaws in practice. As such, the NCA is of the opinion that a revision of the Code is adequate, but does not support a total abolishment.

On a more specific level

Q3. Would the air transport distribution market - including small and medium sized companies involved in the market - be ready for the introduction of greater pricing freedom (such as through the removal of the rules of non-discriminatory fees given in article 10)?

Small and medium sized airlines face higher entry barriers if the rules of non-discriminatory fees given in article 10 are removed because they do not have the same amount of bargaining leverage



Konkurransetilsynet
Norwegian Competition Authority

against the CRS providers as the large established airlines. Based on similar reasoning, smaller airlines that already are established in the market faces potentially higher prices that may increase the risk of market exclusion. On this background it is important that the Code of Conduct functions as a safety valve for these situations.

Q4. Given the changes in the market and in the ownership and control structures of the CRS providers, are the specific obligations imposed on parent carriers still needed? Or should these obligations be reviewed or lifted?

As mentioned under question one the airlines may find it profitable to re-establish their control over the CRS if the Code of Conduct is abolished. A vertical integration of this kind would increase the risk of anti-competitive behavior. It is also the case that some national flag carriers still controls national marketing companies (NMC) which promotes the most common CRS in their home market. Consequently the NCA believes that there is still a need for the Code's specific obligations imposed on parent carriers.

Q5. Should airlines remain free to invest in CRS providers and control them or should there be rules that restrict the possibility for airlines or other sectors to control CRSs? Are specific transparency requirements needed for CRS providers that are not publicly listed on a stock exchange?

The NCA believes that it is adequate to regulate the ownership to CRS providers in such a manner that the risk of anti-competitive behavior is reduced. This can be done by separating the ownership to the CRS providers from the participants in the market; in this case the airlines. Airlines who owns essential services like the CRS is, in a competitive environment, likely to favour own interests, inter alia by refusing other airlines to participate in the CRS or to operate with highly discriminatory access conditions. Accordingly, there should be rules that restrict the possibility for airlines to control CRSs. For effective supervision with the compliance of such rules it seems necessary with specific transparency requirements for CRS providers that are not publicly listed on a stock exchange.

The NCA also realizes that vertical integration can lead to efficiency gains, but it is doubtful that these gains compensates for the high risk of anti-competitive behavior in the air travel distribution market.

Q7. Should travel agents' identity no longer be revealed in the Marketing Information Data Tapes (MIDT)?

The NCA, inspired by the study rendered by the Brattle Group and Norton Rose, strongly believes that in fundamental ways the exchange of MIDT can be harmful to competition. By making key competitive data transparent, the MIDT gives the participants in the market the opportunity to determine rival's business strategies. The air travel industry should be treated the same way as other industries, where firms are not given immediate access to competitor's sales data. Consequently a complete ban of the sharing of MIDT should be imposed.

If the Commission finds it necessary to uphold the provisions concerning MIDT, the NCA believes, in accordance with the study by the Brattle Group and Norton Rose, that concealing travel agents' identity in the MIDT will reduce the airlines possibility to pressure travel agents to reduce rival bookings. This solution will also make it more difficult for the airlines to implement commission overrides (programs that large airlines use to induce travel agents to sell their product) and consequently reduce the risk of transforming travel agents from a neutral sellers' agent to a direct distribution agent for a particular airline with no disclosure to the costumer. The risk of abusive use of the information contained in the MIDT is especially high for large airlines. Large airlines can use the information in the MIDT as a way to exclude smaller competitors.

In addition to this, the NCA also believes that the third option presented by the Brattle Group and Norton Rose should be adopted. This option prohibits CRSs from releasing data on any airline



Konkurransetilsynet
Norwegian Competition Authority

that does not give its consent. This option can make it more difficult for established airlines to exclude entrants, for instance by way of targeted pricing. Moreover, some airlines that avoid the CRSs today might participate if they could keep their data confidential, especially low-fare airlines that today mainly uses direct booking systems. In sum the NCA strongly believes in a total aggregation of the figures contained in the MIDT.

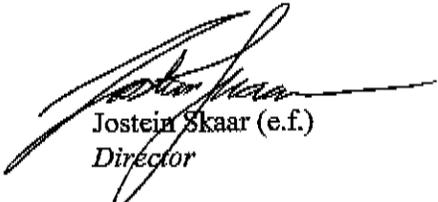
Q8. Are the Code of Conduct's detailed prescriptions with regard to the principal display of a CRS still pertinent in the present market context? Are they still required to ensure a neutral choice? Or can they be simplified or removed? In case stakeholders favour a simplification or removal of these prescriptions, could they - where possible - quantify the reduction in administrative costs that such a regulatory change would induce?

The NCA believes that a neutral principal display of the CRS is an important rule in the Code of Conduct, especially because it is necessary for the consumers when they search for the most adequate travel option at the best price. A detailed prescription of the display requirements in the Code is an effective method to reach this aim and is consequently pertinent in the present market context. If the prescriptions can be simplified and still ensure a neutral choice for the consumer, the NCA supports a simplification, especially if such a measure can lead to a reduction in administrative costs for the participants in the CRS market.

Q9. Would greater pricing freedom with regard to booking fees allow more rail services to be offered on the CRS displays? Do we need additional measures to promote the sale of rail tickets via CRSs?

The NCA agrees with the consultation paper that the existing provisions in the Code of Conduct with respect to non-discriminatory fees reduce the interest of CRSs for rail services. Greater pricing freedom with regard to booking fees would allow the railway companies to negotiate fees with the CRS vendors that are more closely related to the price of the ticket, and consequently the railway companies could find it profitable to subscribe to a CRS. Indeed, as railway tickets are on average of less value than airline tickets, the rule of non-discriminatory fees imposes proportionately higher fees on railway tickets than airline tickets. A higher degree of railway services in the CRSs could strengthen the competition both between the airlines and the railways on routes where they can be seen as substitutes, and also between the railway services that are present in the CRS today and those services who do not subscribe to a CRS.

Yours sincerely



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