



Competition Authority

Competition Act 2002

Decision of the Competition Authority
No. E/02/001

The Reduction in Travel Agents' Commissions by Aer Lingus plc

21 March 2002
(Case: COM/15/02)

SUMMARY

The Authority has decided that the unilateral reduction in commissions by Aer Lingus plc from 9% to 5% effective 1 February 2002 does not, in its view, breach competition law. It is not clear that Aer Lingus plc is dominant, while its conduct does not appear to constitute an abuse. It is arguably pro-consumer and objectively justified.

The Authority's investigation was prompted by a complaint that Aer Lingus plc was abusing its dominant position by reducing commissions.

The Authority considers that the relevant market is for air travel agency services in the State. Aer Lingus plc accounted for between 40%-50% of this market. However, the surrounding market conditions in terms of the relative size of rival airlines and lack of constraints on landing slots at the State's airports raised considerable doubts as to whether Aer Lingus plc was dominant.

Insufficient evidence was presented to show that Aer Lingus plc commission levels were excessively low or that the predicted reduction in travel agent numbers would lead to a decline in competition. Travel agents have the alternative of charging a fee for the service that they provide, while there are an increasing number of sources of information about air travel and fares.

Finally, the conduct of Aer Lingus plc represents a move to a different business model as a result of industry changes. As such it has an objective justification.

1. THE ISSUES

The complaint

1.1 The Competition Authority (“the Authority”) received a complaint in January 2002 alleging that Aer Lingus plc (“Aer Lingus”) had abused its dominant position in the full service airline market in the State by unilaterally reducing the commission on ticket sales from 9% to 5% effective 1 February 2002. It was claimed that this would reduce the number of travel agents in the State leading to a lessening in competition among travel agents.

1.2 The complaint argued that the relevant *geographic market* is the State and that the *relevant product* is the market for full service airlines. Such an airline is defined as one that: interlines; provides long and short haul services; has gradations of service (i.e. business, economy etc) and frequent flyer programmes; uses primary not secondary airports; is a member of a strategic alliance; and, has in flight services included as part of the product. Typical users would be businesspersons. There is another product market according to the complaint consisting of low priced or no frills airlines such as Ryanair Limited (“Ryanair”).

1.3 The unilateral reduction in margins by Aer Lingus would, it was argued in the complaint, result in travel agents going out of business and thus consumers would lose an important source of impartial advice and information. Because of the reduction in travel agent numbers new full service airlines would have difficulty entering the Irish market. Closure of travel agents would adversely affect elderly persons who tend not to have credit cards. If Aer Lingus reduced their commissions then there may have to be add-ons by the travel agents.

1.4 In the complaint it was stated that travel agents accounted for a very substantial share of Aer Lingus sales. Aer Lingus is trying to move towards booking over the Internet. Ryanair have stopped paying any commission on tickets. Since Ryanair

operates point to point it makes it easier to book via the Internet. The complaint states that Aer Lingus customers do not want to book via the Internet, but want to use a travel agent.

The parties

1.5 For reasons of confidentiality the identity of the complaint is not stated.

1.6 The principal activities of Aer Lingus are the provision of operation passenger and cargo air transportation services to the UK, mainland Europe, and the US and within Ireland. Aer Lingus distributes its tickets through its website, travel agents and reservations staff. The closure of all Aer Lingus Travel Shops was announced on 15 January 2002.¹

2. ASSESSMENT

Introduction

2.1 Allegations that an undertaking (or a group of undertakings) has abused their dominant position are covered by Section 5 of the Competition Act 2002 (“the Act”), which reads as follows:

(1) Any abuse by one or more undertakings of a dominant position in trade for any goods or services in the State or in any part of the State is prohibited.

(2) Without prejudice to the generality of subsection (1), such abuse may, in particular, consist in-

(a) directly or indirectly imposing unfair purchase or selling prices or other unfair trading conditions,

¹ The information concerning Aer Lingus is taken from publicly available sources.

- (b) limiting production, markets or technical development to the prejudice of consumers,
- (c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage,
- (d) making the conclusion of contracts subject to the acceptance by other parties of supplementary obligations which by their nature or according to commercial usage have no connection with the subject of such contracts.

An undertaking is defined in the Act as “a person being an individual, a body corporate or an unincorporated body of persons engaged for gain in the production, supply or distribution of goods or the provision of a service.”

2.2 In order to establish that there is a breach of Section 5 of the Act, the Authority must demonstrate in court that the undertaking in question:

- holds a dominant position in a relevant market; and,
- has abused that dominant position.

The creation or existence of a dominant position does not breach the Act; rather it is the *abuse* of that position that constitutes the breach.

2.3 Section 5 is based on Article 82 of the Treaty establishing the European Community. In applying Section 5 the Authority has regard not only to its interpretation by Irish courts, but also to that of Article 82 by the European Commission (“the Commission”), the Court of First Instance (“the CFI”) and the European Court of Justice (“the ECJ”).

The relevant market

2.4 The Commission has analysed the issue of market definition in an analogous situation to the present case at some length in its *Virgin/British Airways* decision² (under appeal). The case concerns allegations that British Airways plc ('BA') abused its dominant position by offering fidelity rebates to travel agents designed to restrict the growth of Virgin Atlantic Airways Limited ('Virgin'). In the Commission decision the appropriate market definition is for air travel agency services within the UK. No distinction is drawn between full service and no-frills tickets. Thus applying this reasoning to the current case the relevant market is for air travel agency services in the State.

Dominance

2.5 In *United Brands*, the ECJ formulated the following test for dominance:

...The dominant position thus referred to by Article [82] relates to a position of economic strength enjoyed by an undertaking which enables it to prevent effective competition being maintained on the relevant market by affording it the power to behave to an appreciable extent independently of its competitors, customers and ultimately of its consumers.³

In assessing dominance the Authority takes into account if and to what extent an undertaking encounters constraints on its ability to behave independently. Those constraints might, for example, be entry barriers that make it difficult for potential competitors to compete effectively.

2.6 Based on data provided in the complaint the market share of Aer Lingus would appear to be between 40% and 50%. In the *Virgin/British Airways* case BA was found to be dominant with a market share of 39.7% in 1998. An important part of the Commission's reasoning in coming to this conclusion was that BA's market share was

² OJ [2000] L 30/1, on appeal Case T-219/99 *British Airways vs the Commission* (judgement pending). See also Case COMP/38.006 – Online Travel Service (2000/C 323/03). Dated 20/11/2001 and 'Commission opens in-depth probe into travel agent joint venture between T-Online, TUI and Neckermann', Press Release IP/01/670. Dated 08/05/2001.

³ Case 27/76, *United Brands v Commission* [1978] ECR 207; [1978] 1 CMLR 429.

substantially larger than its nearest rival (Virgin at 5%) and 2.2 times the combined size of its nearest four rivals in 1998. Furthermore, the slots that BA holds at relevant airports make entry difficult, thus reinforcing BA's dominant position.

2.7 The market share of Aer Lingus, based on information in the complaint, is well above BA's of 39.7%. However, it appears that the market share of Aer Lingus is only four (not eight) times that of its closest rival, but reliable data is not available for other rival airlines. The availability of slots at the States' airports does not appear to constitute a bar on the entry of new airlines: slots at the State's airports are not as scarce or valuable as in UK airports. Thus based on the Virgin/BA case it is not clear that Aer Lingus is dominant.⁴ There would appear to be sufficient competitive constraints on Aer Lingus that would prevent it from acting independently of its rivals by, for example, raising prices above the competitive level. Even if it were the case that these competitive constraints were not sufficient to prevent Aer Lingus acting independently of its rivals, would its behaviour constitute an abuse?

Abuse

2.8 **Excessively low commissions.** It could be argued that Aer Lingus is using its buyer power to dictate excessively low commissions. Arguably this could amount to a breach of Section 5(2)(a) in that it "directly or indirectly imposed unfair purchase or selling prices or other unfair trading conditions." There would appear to have been no successful European Union ("the EU") cases in this regard – i.e. excessively low prices.⁵ In the one unsuccessful case concerning the price paid by French TV channels for broadcasting films, the ECJ argued, "that the complainant had to show that the price was low in relation to each individual film, and that it could not rely on average or undifferentiated figures."⁶ The analogue in the present case is that data must be provided for each individual travel agent.

⁴ Matters might be clarified when BA's appeal has been decided.

⁵ R Whish, 2001, *Competition Law*. 4th Edition. London: Butterworths. Pp. 638-639.

⁶ R. Whish, 2001, *supra* note 5, pp. 638-639.

2.9 The complaint provided information concerning a September 2000 survey on costs.⁷ However, none of the five countries selected as representative of the EU market included Ireland – Finland, Spain, France, UK and Germany – so it is difficult to determine its relevance given the European jurisprudence cited above. Finally in a survey of commission levels in for 2001 Aer Lingus’ levels did not seem out of line with other national flag carriers. Thus there is insufficient evidence to suggest that Aer Lingus is exerting any market power it has to set excessively low commissions.

2.10 **Reduction in competition.** The complaint argued that there would be less competition due to the decline in the number of travel agents. However, a decline in the number of outlets does not necessarily lead to a decline in competition. In one recent Irish decision the judge commented, ‘Even if, contrary to the foregoing, the wholesalers were reduced from five to four, it does not follow that there would be a reduction in the intensity of competition at the wholesaler level.’⁸

2.11 The predicted decline in the number of travel agents in the complaint is not based on any carefully reasoned estimate and thus it is difficult to come to a view as to its accuracy. The estimate is that there will be a fall in employment of 500 or 12 percent. In terms of retail travel agents this would mean, other things being equal, a decline from 470 to 414. However, it would appear that the number of travel agents have been declining in recent years despite considerable economic growth, suggesting that other forms of selling air tickets are more efficient.⁹

2.12 Furthermore there is no reason that travel agents cannot set – separately – service charges for the expertise that they provide for the public. Thus it is not clear that the decline will take place. Finally there are many more sources of information about air

⁷ Deloitte Consulting, 2000, *Schedule Air Product Distribution Costs Study*. A study prepared for the Guild Of European Business Travel Agents

⁸ See *Chanelle Veterinary Ltd v Pfizer (Ireland) Ltd*. [1998] 1 ILRM, 161, 30 July 1997, paragraph 132.

⁹ According to the Annual Reports of the Department of Public Enterprise and the Commission for Aviation Regulation the number of licensed travel agents has declined from 346 in 1998, to 345 in 1999, to 336 in 2000 to 335 in 2001/2. A licensed travel agent may have more than one outlet; hence these data show a smaller number of travel agents than that in the text.

flight now than was the case of few years ago, including an online travel agency in which Aer Lingus is involved.¹⁰

2.13 While the reduction in commissions may affect the welfare of travel agents, it is not clear that there is a corresponding damage to the consumer or the competitive process. For the exercise of any monopsony power¹¹ that Aer Lingus might have to be harmful, this requires that it must be correlated with market power on the seller side. Specifically, a firm with market power on both sides can reduce the price it pays for inputs – the services of travel agents – in order to reduce overall supply of airline tickets sold so that prices to the consumer can be raised. However, as noted below, the strategy that Aer Lingus has adopted is to *lower* prices to the consumer.

Objective justification

2.14 As noted above Section 5 of the Act is based on Article 82 of the EU Treaty and, therefore, the jurisprudence on Article 82 is of assistance in examining an alleged breach of the Section. That jurisprudence has sought to distinguish between abusive behaviour subject to Article 82 and legitimate behaviour outside of it.¹² In doing so the principle of objective justification (and proportionality) has developed. Thus despite the fact that Article 82 (and Section 5) contain no waiver, it nevertheless is the case that EU jurisprudence has developed an approach that plays an analogous role.

2.15 In the case of the reduction in commissions Aer Lingus justifies this as part of the reaction to the events of September 11.¹³ Aer Lingus has decided to reduce their distribution costs by not only closing their travel shops, but also encouraging the use of their website as way of selling tickets. In part this is designed to lower fares so that this

¹⁰ See Case COMP/38.006 – Online Travel Service (2000/C 323/03). Dated 20/11/2001 and ‘Commission opens in-depth probe into travel agent joint venture between T-Online, TUI and Neckermann’, Press Release IP/01/670. Dated 08/05/2001.

¹¹ Market power on the buyer’s side; in this instance Aer Lingus would have to had market power in relation to the purchase of travel agents services.

¹² R. Whish, 2001, *supra* note 5, pp. 180-81.

¹³ Based on an Aer Lingus press release of 15 January 2002, ‘Aer Lingus Confirms Reduction in Travel Agency Commissions.’ This maybe found on their website: www.aerlingus.com.

better places the former national flag carrier to compete with no frills carriers.¹⁴ On other words, Aer Lingus is not limiting competition but switching to a lower cost means of distribution.

3. DECISION¹⁵

3.1 On the basis of the facts and for the reasons set out above, the Authority has decided that in its view the reduction in the commission paid by Aer Lingus to travel agents from 9% to 5% effective 1 February 2002 does not breach Section 5 of the Competition Act 2002.

3.2 This decision of the Authority does not affect the rights of private parties to take an action under the Act.

4. SUBSEQUENT DEVELOPMENTS

Office of Fair Trading Decision

4.1 After the Authority had reached its decision on 21 March 2002 the Office of Fair Trading (“the OFT”) released a decision¹⁶ on 11 December 2002 involving a complaint by the Association of British Travel Agents that alleged British Airways plc was abusing its dominant positioning the market for air travel agency services in the UK by making excessively low booking payments that do not allow travel agents to cover their costs. The OFT concluded that irrespective of whether BA was dominant, the conduct complained of did not constitute an abuse.

¹⁴ See Economist, 2002, ‘Flag Carriers at Half Mast’, *Economist*, 2 March, pp. 61-2.

¹⁵ The Authority made the decision on 21 March 2002. Under Section 30(1)(g) of the Competition Act 2002 the Authority is given the function ‘to carry on such activities as it considers necessary so as to inform the public about issues concerning competition.’ Publishing reasoned Decisions of the Authority is part of that function.

¹⁶ OFT, Decision of the Director General of Fair Trading, No CA98/19/2002, *The Association of British Travel Agents and British Airways plc*, 11 December 2002. The decision is available on the OFT’s website, www.of.gov.uk.

Commission Decision

4.2 The Commission received a complaint dated 17 October 2002 alleging that Aer Lingus had abused its dominant position in the market for travel agency services by reducing travel agency fees from 5% to 1% as from 1 January 2003. The Commission's response on 12 December 2002 was that there did not appear to be an infringement. The Commission reasoned that there is no obligation for an airline, simply by virtue of any market power it may have to cover the costs incurred by travel agents. If no commission is paid the travel agent can charge a fee which will reflect the added value of the services that they provide to consumers.

For the Competition Authority

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10 June 2003