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IMPLICATIONS OF AIRLINE CODESHARING

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FOREWORD

In a rapidly changing global economy, the international air transport industry must continuously find new ways to adapt to trends and to changing and increasingly competitive conditions. Codesharing and other related forms of airline co-operative ventures have been adopted by many international carriers either to extend their global reach or simply to survive in the more competitive environment, enabling them to be better placed in the marketplace. Such agreements have proliferated in the past years and the recent trend shows no sign of abatement. Not all carriers have embraced codesharing, however, and the practice has been contested by some. Because codesharing involves much more than simple marketing or operational techniques, its wide application raises a certain number of potential regulatory concerns, mainly on the consumer and competitive aspects. Such developments have focused the wider attention of the aeronautical community on codesharing and at the same time generated a number of national and regional studies, some of which are still under way.

When the ICAO World-wide Air Transport Conference convened in Montreal from 23 November – 6 December 1994 to explore the future regulatory framework of international air transport, it identified a number of aspects on which further studies were needed. Codesharing was among the topics selected to be examined by the Organization. This study was prepared by the Secretariat in 1996, drawing on available published information, including estimated1995 data where necessary, specific studies already published for the Governments of the United States and Germany as well as for the European Commission, and ICAO's own documentation and research, with input provided by the European Civil Aviation Conference (ECAC) and by different Contracting States.

Since codesharing is a relatively recent phenomenon — at least in its international application — and the situation is constantly evolving, any study on the subject is liable to be quickly overtaken or outdated by new factors. Moreover, the recentness of some of the agreements makes it difficult, in certain instances, to obtain any useful perspective on their results. Subject to these reservations, this study examines the present situation, seeks to address comprehensively the implications of codesharing and identifies certain areas where caution should be exercised by regulatory authorities.

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EXECUTIVE SUMMARY

1. Codesharing and other related forms of airline co-operative ventures have been increasingly adopted by many international carriers to adapt to new trends such as the globalization of businesses as well as the increasingly competitive conditions that are now prevalent in the air transport industry. Because codesharing involves much more than a simple marketing or operational technique, its wide application raises a certain number of potential regulatory concerns.

2. The practice of codesharing, by which one carrier permits a second carrier to use its airline designator code on a flight, or by which two carriers share the same airline code on a flight, can take different forms. It may, for example, involve a major carrier sharing its code with a smaller feeder carrier; it may also be an arrangement between two or, in some instances, three or more international carriers for an international flight operated co-operatively or for a connecting service which uses the same code.

3. Other airline practices, such as blocked space, wet leasing, franchising, joint service and pooling, are often closely associated with codesharing and sometimes receive similar regulatory treatment (see Chapter 1).

4. For purposes of this study, the effects of airline codesharing on traffic development have been assessed — on a preliminary basis because of the recentness of the experiences — on a certain number of routes involving transatlantic crossings for which sufficient data were available. The main findings are that, with a few notable exceptions, in most of the city-pairs examined, codesharing arrangements have not as yet produced fundamental changes in the markets considered. Where changes have been brought about, it has tended to result in a reduction in competition, in terms of the number of operators present in the market, and a reduction in the number of services offered to the public. Because in most of the cases they are the actual carriers under the codesharing agreements, European carriers as a group would appear, on the basis of the data reported, to have fared better than North American carriers as regards improvement of their market share (see Chapter 2).

5. Quantifying the economic benefits derived from the practice of airline codesharing is a difficult exercise and the validity of the results provided in some studies or by participants in such schemes has been challenged. In some cases, airlines that are party to a broader alliance have clearly benefited from the practice in terms of additional traffic and extra revenue, although this has mainly been at the expense of other carriers, since there is no clear evidence of traffic stimulation but rather of traffic redistribution. In some other cases, there may be occasions when, within the context of an alliance, the codesharing arrangement may have the effect of benefiting only other carriers and other countries, since services are exclusively operated by the other party, with possible negative effects on employment and revenue for the first party. For airports and passengers alike, codesharing *per se* will not automatically be beneficial in every situation; on the other hand, when circumstances are favourable, it could be of value for airport operators and the travelling public. However, it remains to be seen how the situation will evolve in the long run if, on a given sector that has a number of operators competing on it, most competitors have either been forced out and/or become part of an alliance, and the market has tended to concentrate (see Chapter 3).

6. Airline codesharing may have advantages for developing countries in so far as it can offer the possibility of serving very thin routes at minimal cost and using heretofore unused rights. It can thus be an instrument to facilitate the participation of developing countries' airlines in international air transport. However, the present situation shows that

the practice has yet to take hold in a substantive way among developing countries' airlines, although this may change as the potential benefits of this form of co-operation come to be viewed as a means of adapting to the changing competitive environment and of enabling developing countries' airlines to participate more economically and effectively in international air transport (see Chapter 4).

7. Airlines' attempts to increase their market access and exposure through commercial alliances have placed codesharing under considerable regulatory attention since it was perceived as a means of indirectly increasing market access. It is now the general practice that international codesharing is dealt with in the bilateral negotiating process and that underlying traffic rights are required in order for any codeshared service to be approved. In some cases, specific provisions in bilateral agreements may also be required for codeshared services, especially when a third country is involved.

8. Therefore, other than its link to underlying traffic rights, codesharing does not have a systematic regulatory treatment, but rather an ad hoc treatment dictated by general aeropolitical considerations. Thus far, this has tended to be a reactive — in some respects, protective — treatment, rather than being based on a more strategically planned or longer-term vision of future policy evolution or aeronautical relationships. Paradoxically, a reliance on codesharing as a means to greater market access, while increasing competition in some circumstances, can in other circumstances actually impede the development of a truly liberalized air transport regulatory framework through limitations on frequencies for codesharing services and, in particular, any multilateral approach to liberalization(see Chapter 5).

9. Codesharing raises the issue of competition in two ways, either as an enhancement of competition through the provision of additional or better service or as a reduction of it through a concentration of the forces playing in the market. Because of the lack of appropriate data and relatively limited experience, the longer-term effects of codesharing on competition are still uncertain. Nevertheless, one conclusion that can be drawn so far is that the potential pro- or anti-competitive aspects of a proposed codesharing operation need to be weighed carefully on a case-by-case basis. With the proliferation of codesharing agreements, there is likely to be increasing resort to competition laws by aeronautical authorities to provide criteria for such assessments. For most countries, it can be expected that, notwithstanding this competition law aspect, the broader aeropolitical and regulatory objectives often associated with codesharing will continue to be pre-eminent considerations (see Chapter 6).

10. Codesharing may give rise to uncertainties concerning carrier liability. Two important legal issues are posed by codesharing: which air carrier is liable under the Warsaw regime and which air carrier is responsible to the passenger in user/consumer-related matters? In the case of the former, it would appear that codesharing, when it involves a connection, need not necessarily be equated to successive carriage such as in the usual case with interlining, but that ultimate legal responsibility could nonetheless be determined by the contract of carriage between the passenger and the contracting carrier, depending on the interest of the passenger or its claimants. Where the codeshared service does not involve successive carriage, then other legal considerations concerning the right of liability redress may arise. With respect to responsibility to user-related issues, the usual airline industry rules and practices would apply, i.e. responsibility rests with the operating carrier. In any event, before engaging in providing services, codesharing partners should meet certain requirements, i.e. agree on liability issues and give notice to the public, so that these become part of the terms and conditions of carriage (see Chapter 7).

11. The consequences of codesharing for the consumer raises the questions as to whether it is a deceptive practice or, alternatively, whether it is beneficial to the consumer. The over-all concern is that information on actual or potential travel given to the travelling public must be accurate and complete and not confusing or in any way misleading. Hence, better information and a measure of consumer protection have been widely advocated. There is now a general recognition that the information provided to the public on codeshared flights is in many instances not sufficient and needs to be improved. If the solution to be adopted is one of placing the burden of responsibility for taking action at the industry level, i.e., mostly on airlines but also on travel agents and other in the information chain, then information to passengers should be provided in the following three ways:

- orally, at the time of booking;

- in written form, i.e. on the ticket itself and/or (if not possible), on the itinerary document accompanying the ticket, or on any document replacing the ticket, such as a written confirmation, including information on whom to contact if problems arise and a clear indication of which airline is responsible in case of damage or accident; and

- orally again, by the airline's relevant airport ground staff at all stages of the journey.

12. Caution is necessary when judging the benefits to the travelling public claimed for the practice of airline codesharing, and the elements of quality of service, flight options and tariffs will be pivotal to any assessment of benefit. The simple fact of a service being codeshared will not automatically result in a better air service than an interline or non-stop one, and each case will need to be judged on its merits (see Chapter 8).

13. The implications of codesharing upon labour are felt mainly at two levels. At the work force level, some airlines may be affected by redundancies, and at the management level, management and staff will need to adapt to new working conditions, possibly to learn new skills and finally to be left with the challenge of making the theoretical or desired benefits work in practice. Thus, the over-all labour context is one of added pressure put on staff by the new trends affecting the industry. However, motivated employees clearly have an influence on airline performance, and their attitudes are of the utmost importance in the relationship between airlines and their passengers. It will therefore be in the interest of all parties concerned to give due consideration to staff concerns during the process of alliance-making, which incorporates codesharing, and in its implementation (see Chapter 9).

14. Clear lines of accountability and responsibility are essential for security/facilitation aspects as well as for safety aspects, since technical and operational regulations may vary considerably from one airline partner in a codesharing arrangement to another, depending on their countries of registration. In terms of environment, the code sharing practice may have both positive and negative aspects in so far as it has the potential of creating new aircraft movements or reducing them (see Chapter 10).