Moorabbin Airport

14th July 2006

Price Regulation of Airport Services Inquiry
Productivity Commission
PO Box 80,
Belconnen ACT 2616

Dear Sirs

**Review of Price Regulation of Airport Services: Submission by Moorabbin Airport Corporation.**

This submission is made by Moorabbin Airport Corporation Pty Ltd ("MAC") which is the Airport Lessee Company ("ALC") for Moorabbin Airport, a federal leased airport under the *Airports Act 1996*.

In making this submission we note that Moorabbin Airport is not a "core regulated" airport (*Sec7 Airports Act 1996*) and is not currently regulated or price monitored in any way under the *Airports Act 1996.* Moorabbin Airport is not and never has been price monitored and has had any prices or services "declared"

We further note that under MAC is required to operate Moorabbin airport as an airport under the terms of its lease with the Commonwealth *(clause 3.1)* and is further required to provide access to the airport. In addition MAC is required to use good business practice in its operation of the airport.

The reason we make a submission to the Productivity Commission is that in recent months there has been some controversy over the rate of charges at the major general aviation airports in capital cities, known as "GAAP" airports. This takes two forms.

Firstly, there has been a concern raised by some members of the aviation industry that GAAP airports have the ability to raise their aeronautical charges without limit due to the fact that they enjoy monopoly powers in their capital city area.

Secondly the charge has been made that as landlords GAAP airports are able to indiscriminately increase land and property rental rates without being "fair" to the aviation industry or without reference to a proper market rate. In this submission we intend to examine each argument.

Please do not hesitate to contact the undersigned if you would like any further clarification of the commercial position of Moorabbin Airport in relation to its customers, tenants and users of the airport. MAC has no objection to this submission being published on your website.

Yours faithfully
For Moorabbin Airport Corporation Pty Ltd

P A McConnell
General Manager Aviation

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# Submission by Moorabbin Airport Corporation to the Productivity Commission Review of Price Regulation of Airport Services.

## 1. Aeronautical Charging.

Moorabbin Airport is a major General Aviation (GAAP) airport recording in excess of 260,000 movements annually. It is home to 10 flying schools, numerous maintenance and charter organizations, and has two low capacity RPT operations. Over 300 aircraft and helicopters are based on the airport and we offer employment to over 800 skilled aviation professionals. We operate in an intensive flying training capacity and regularly operate a two-circuit system to maximize efficiency. It is interesting to note that of the 260,000 movements about 170,000 are for touch and go training and only around 90,000 are full take-off's and landings. Thus we generate around 45,000 actual full-stop landings per year.

As an airport corporation we levy a **daily access charge** on all our based aircraft. This is not a landing fee nor is it a parking charge. It is a charge to access the fixed airport infrastructure and is in addition to any charges applied by Airservices Australia which in our case relates to the Location-Specific **Terminal Navigation Charge. (TNC)**. Moorabbin Airport currently charges $8.00 per 1,000 kg MTOW per day. Substantial discounts are available for yearly pre-payment, which is the option chosen by the majority of aircraft owners. This reduces the charge to $4.00 per 1,000kg MTOW per day incl GST. For the median weight of aircraft present at Moorabbin this eqates to $6.28 per day (incl GST).

It is interesting to note that from 1 July 2006 Airservices Australia will charge $10.49 (incl GST) per 1,000kg MTOW per landing. This is $16.47 for our median aircraft.

### 1.1. The Current System.

The current system is a slightly modified version of the charging system previously adopted by the Federal Airports Corporation and known as the "GAIT" System (*General Aviation Infrastructure Tariff*) which was widely accepted by industry. When MAC became the ALC in 1998 we had no preconception as to what sort of aviation charge should be levied at Moorabbin Airport and in late 1998 we conducted a series of consultative meetings with industry to review what type (as opposed to amount) of aviation charge would be acceptable. The options were:

- **GAIT-type daily access charge**. A fixed charge per day for use of the airport infrastructure. This is based upon an aircraft MTOW (*Maximum Take Off Weight*). It is based upon a properly registered aircraft being present on the airport, with the ability to use the airport, rather than actually using the airport. The charge is levied whether an aircraft is hangared or not. This rate is heavily discountable for pre-payment. At the time of our assumption of the airport lease the yearly discount was 65%. The advantage of this system is that it is relatively easy and efficient to operate, as the majority of users opt to obtain the discount and pay yearly. It advantages those who make frequent use of the airport, such as flying schools, but disadvantages those who make infrequently use such as individual owners

  Other variations to this system were considered, such as charging by the number of engines or charging based upon area of tarmac occupied but none was more efficient than the MTOW-based system.

- **Charge per utilization**. A charge based upon actual use. This would be based on full stop landings with probably a lesser charge for circuits. Airservices Australia charges on this basis although currently only for full stop landings. The advantage of the system is that it is based upon actual use. The disadvantage is that it is a very expensive system to administer as full proof of landing must be obtained, normally from an audio tape that is later transcribed. MAC estimated the set up cost of this system to be well over $40,000 with a yearly operating cost of $30,000 or more, all of which would have to be added in to the ultimate charging basis.

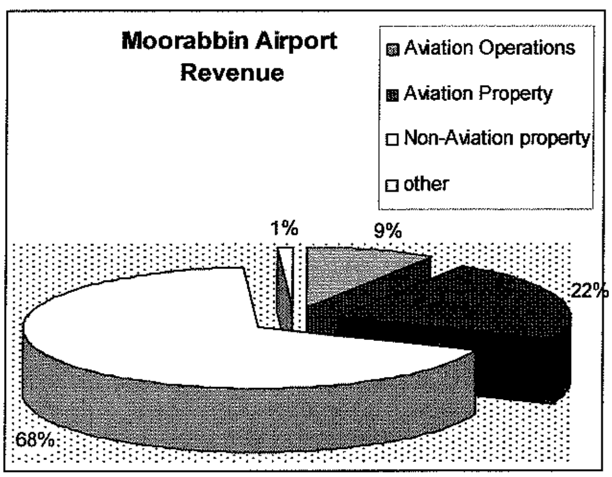
  The system advantages low use customers- those who only fly once or twice a month. It disadvantages those who fly more frequently, especially flying schools, unless a substantial discounted rate can be calculated.

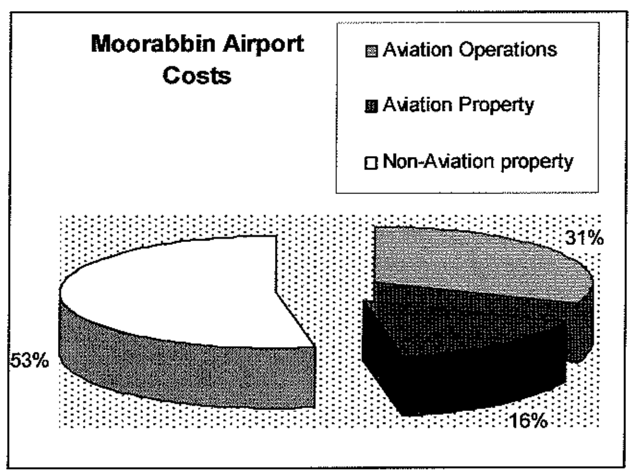
When MAC put these options to its customer base the consensus was strongly for the system that is currently in use.

**1.2. Does the charge adequately cover costs?**

The major problem that we have always had is that the aeronautical charge has never even remotely covered the true cost of aviation at Moorabbin Airport.

As a privately owned corporation we are unable to disclose in public the actual costs we are required to bear in relation to Moorabbin Airport. However this pie chart is enlightening:




Our income from aircraft access charges now comprises 9% of total income. However the direct cost of providing the aeronautical infrastructure to service aviation needs is a staggering 31% of total costs. The cost of provision of aeronautical assets includes maintenance and repair of aeronautical pavement and runways, lighting, provision of adequate drainage services, provision of and operation of safety and emergency planning systems, insurance, and a small amount for amortization and depreciation of assets. In addition MAC has considerable compliance costs as it is an airport certified by CASA and is in addition a security regulated airport under the *Aviation Transport Security Act 2004.*

As an example, in recent years the cost of public liability insurance ("Airport Operators Insurance") has skyrocketed. This is especially so when one considers that the Commonwealth requires MAC to maintain public liability coverage of $150Million, including coverage for acts of terrorism. When MAC took over the airport in 1998 the cost of liability insurance was a reasonable $30,000 per annum. In 2003, the first full insurance year after the 9/11 acts, the initial premium MAC was asked to pay was over $400,000 and this only included coverage for $80Million of terrorism-related cover. That year the total insurance premium exceeded the total amount of earnings for aircraft access charges. In more recent times premiums have reduced considerably but the public liability component of insurance we still pay equates to a sizeable proportion of revenue from aircraft access charges.

It is fair to state that without the income stream from our non-aviation property development MAC would be forced to increase substantially our airport aircraft access charges.

So why do we not do this?

**1.3. Competition to Moorabbin Airport.**

We are acutely aware that we tread a fine line in the amount we charge to our users. Our current rates do not even remotely cover the true cost of provision of aeronautical infrastructure. The reason that we are unable to charge more is largely that we have a considerable amount of competition from other airports in the Port Phillip basin. Airports the size of Moorabbin do not have any claim to monopoly status. To illustrate this, the available airports in the Port Phillip Bay area are:

<u>Towered Airports (and certified by CASA).</u>

| | |
|---|---|
| Essendon. | Asphalt runways. Full tower services, ILS. Circuits not allowed. Lighting. Extensive hangerage. Commonwealth owned leased airport. |
| Avalon | Asphalt runway. Instrument Landing System. Lighting. |

<u>Non-Tower airports. (None certified by CASA)</u>

| | |
|---|---|
| Point Cook | Asphalt runway. Extensive parking and hangarage. Satellite base for GFS (Our biggest customer) Defence airport so no freehold. 50 based aircraft with over 50,000 movements per year. |
| Tyabb | New sealed runway. Lighting. 100 aircraft based. Freehold sites available. Upgrade was paid by state government/Council grant. |
| Tooradin | New sealed runway. New lighting. Freehold sites available. |
| Bacchus Marsh | Sealed runways. |
| Coldstream. | Gravel runway. Satellite for RVAC. |
| Lilydale. | Grass runway. Extensive hangarage. |
| Melton. | Gravel runway. |
| Wallan. | Grass runway. Hangarage. |

All of the above airfields are within a short flight of Moorabbin and the majority are geographically convenient for the population of Melbourne.

Two consequences would flow from a decision by MAC to increase charges at Moorabbin, and the result that aircraft and movements would flow to other airports:

a) Reduce revenue to Moorabbin Airport Corporation. Any outflow of aviation activity would result in a consequential loss of revenue to MAC. This would come from both losses of based aircraft revenue and also in the medium turn the loss of commercial business organizations based at Moorabbin. Although MAC does not currently charge a landing fee to aircraft the situation would be exacerbated if it did.

   The actual size of aviation loss would be to a large extent dependant on the level of increase of charges. However research previously conducted by MAC would indicate that a cost increase of CPI plus 2% can be generally absorbed by the aviation population before any aircraft owners are stimulated to leave by the prospect of lower charges at other airports. If a major flying school was to decide to move its operations the impact on MAC would be catastrophic.

b) Reduce safety in general. When there is an active tower (operated by Airservices Australia) there is a certain measure of safety inherent in these operations, especially in view of the fact that over 250,000 movements per year are handled at Moorabbin Airport under control conditions. However if a move to higher charging was made by MAC, or arguably Airservices, some operators would vote with their feet to move their circuit training to a non-tower airport then, for that airport, safety would have decreased due to the increase in traffic there.

**1.4. Summary: Aviation Charges.**

It is manifestly clear that airports such as Moorabbin do not enjoy monopoly powers. The average aircraft owner can and will relocate to another airport if he thinks he is being overcharged at Moorabbin. MAC has always taken its obligation to operate the airport as an airport seriously but this has only been achieved because MAC has been able to develop an alternate income stream in the form of non-aviation development. The aviation and non-aviation development philosophies at Moorabbin have a symbiotic relationship- one cannot exist without the other. Aviation needs non-aviation to survive, and non-aviation can only be developed within the exacting framework of the Airports Act 1996.

## 2. Property Charges.

Moorabbin Airport Corporation Pty Ltd ("MAC") purchased a 99 year lease 1998, being one of the first general aviation airports to be privatised by the Federal government. As part of the airport sale, Moorabbin Airport was required to submit a Master Plan in order to implement an orderly plan for the future of the airport. Moorabbin has since produced an updated Master Plan in 2004 which was approved by the Federal Minister for Transport in August 2004.

### 2.1 History of Property Charges.

When MAC took over the airport, the Federal Airports Corporation (FAC) had put in place commercial leasing arrangements with a number of aviation and non-aviation tenants on the periphery of the airport. Although these leasing arrangements had not been effectively administered by the FAC, they represented leasing arrangements which would be utilised on comparable commercial land external to the airport with the normal commercial risk and rent controls for the owner and moreover the tenant.

### 2.2. Basis of Current leases.

Although, there are a number of differing FAC leases inherited by MAC as part of privatisation, generally both former FAC leases still operating since the sale to MAC and current MAC leases contain the normal commercial controls including:

- Consistency with the operation of commercial leases in the state of Victoria
- Setting of rentals either on a fixed or market basis. Market rents are set on the basis of comparable rents and appropriate controls/"discounts" according to the particular permitted use under the Lease.
- Time periods for tenants to discuss/negotiate rent reviews with the Landlord.
- Ability for tenants to dispute rents set by MAC with reference to market valuation and determination by a third value either agreed between the parties or appointed by the Australian Institute of valuer's.
- A number of complimentary provisions for the occupation whereby both the tenant and MAC have the normal commercial protections as landlord and tenant.

### 2.3. MAC Policy in respect to leases.

A view which has been expressed by some that somehow airports can operate commercial lease contracts or nullify existing FAC lease contracts at odds with the normal legal requirements for tenancy leasing is totally rejected and based on a misinformed notion that somehow tenancy laws and the need to competitively lease sites on airport do not apply to Commonwealth land.

MAC has spent considerable management effort in order to ensure that leasing arrangements with tenants are clear and contain the usual protections for tenants. MAC are not in a position to employ "take it or leave it" leasing and nor would MAC take such an approach. MAC's objective for the airport, as expressed in the Master Plan is to foster aviation and grow its aviation base whilst providing for timely commercial development on the peripheries of the airport which both strengthen MAC's long term income stream and assist in the continued improvement of airport facilities and growth of the aviation operations.

Since purchasing the airport a number of new tenants have been introduced on airport across the aviation spectrum including aircraft maintenance, hi-tech avionic companies, flying schools, instrument/parts suppliers and aircraft storage and parking in both fixed wing and helicopter operations. Our record of retaining at or close to 100% occupancy in all of our aviation property buildings and sites and incremental introduction of new tenants as demand has allowed to the site speaks for itself.

This would not have been achieved if MAC was seeking grossly over market rent positions particularly with new tenants who have a number of alternate airports in the Melbourne basin (as detailed above). Moreover if this was the case MAC would be experiencing wholesale vacancies at lease renewal by existing long term tenants.

MAC is not suggesting for one minute that there has not been dissatisfaction from existing tenants with rent increases since privatisation of the airport. However one must consider the position with respect to tenancies at the time of the sale.

It is generally accepted that the FAC's approach to administering its leases was not commercial. When MAC took over the airport there were a number of tenants who were on peppercorn rental rates which would have applied to land leases from many decades earlier. These were termed "AVIAC" leases and applied at all FAC airports. In an attempt to "foster" aviation the FAC had set unrealistic rent levels which fostered aviation tenants with marginal at best business plans who could not even afford to pay the peppercorn rent levels let alone compete with other tenants on airport and grow viable aviation businesses.

A number of businesses were already faltering under FAC ownership at these low rent levels because of the un-competitive environment that had been created through the arrangements which had been set in place.

MAC therefore inherited a dysfunctional plethora of differing rent levels seemingly decided by which tenant shouted the loudest to keep their rent at low levels. MAC also faced the prospect of losing tenants to competing airports if the approach taken to re-dress rent levels was not systematic and in keeping with a more professional approach to asset management.

**2.4. MAC Initiatives**

MAC has undertaken a number of in initiatives to both retain existing tenants and foster new tenants onto the airport. MAC has included in its Master Plan a clear growth vision for aviation, setting aside both existing and new aviation zones for both fixed wing and helicopter operations as a part of retaining and growing our aviation asset. Extensive maintenance programs to airport buildings, roads, car parks and runways and taxiways have been implemented. It should be remembered that tenants are not charged for maintenance of this asset except for aircraft access charges (see above) which in no way cover the cost of ongoing maintenance nor the replacement liability of these facilities.

Rent levels have been established for a number of differing zones on airport according to type of operation (on/off taxiway), type of use, proximately to aviation facilities etc. so that identifiable and comparable rent levels are charged according to the type and location of operations. Rent levels have risen over time in an attempt to bring all tenants, comparably according to the zone they operate and their permitted use in to line with reasonable market rent levels. Tenants who are now at or near market rent levels are not experiencing large rent increases but steady rent increases according to the movement in the market.

Given that Moorabbin is a general aviation airport with limited capacity to recover costs of running aviation operations and provision of runways, taxiways, parking zones etc. to aviation property tenants, full cost recovery from aviation tenants would mean significant rent increases above current rent levels including market rent levels. We believe therefore that setting comparable reasonable market rent levels having regard to permitted use, type of site etc. provides for a fair, accountable and competitively neutral method for setting rents.

**2.5. Conclusion:**

- All leases operated by MAC comply with the usual legal requirements for leasing, including those protections afforded to tenants.

- MAC operates in an environment of competition from other airports as does any other landlord.

- MAC sets reasonable commercial rent levels in an attempt to ensure that operations are as profitable as possible whilst recognising that competitive rent levels comparable to the facility operated need to be set to both retain existing and foster new tenants onto the airport.

- MAC has set a clear vision to foster aviation, improve and maintain the existing asset and grow the asset, whilst undertaking commercial development on the periphery of the airport in order to make the airport profitable in the long term and assist in the continued improvement of airport facilities and growth of the aviation operations.