

Supplementary submission on the Productivity Commission's Draft Report on the Economic Regulation of Airports by Margaret Arblaster

Following the public hearings on the Productivity Commission's draft report on economic regulation of airports I am making a supplementary submission to clarify some points. In particular I want to address the general statement the PC's has repeatedly made:

"If we found evidence of an exercise of market power, we would not hesitate in recommending more regulation."

This statement raises a number of issues:

- What would the PC regard as "evidence" of whether airports have used their market power?
- What would constitute sufficient information to establish "evidence" of the use of market power?
- What additional regulation would the PC apply to airports if they found "evidence" of the use of market power?
- How willing would the PC be to apply additional regulation to airports?

What would the PC regard as "evidence"?

To date the PC has primarily relied on international benchmarking studies, as well as on interpreting information provided in submissions to the inquiry related to airport/airport user relations, to suggest that they have not found evidence that airports have used market power. My understanding is that international benchmarking studies are not designed to establish use of market power but as a tool for assessing airport operational efficiency. Potential limitations associated with benchmarking studies have been articulated by the PC, ACCC and others.

The PC has proposed that additional information be obtained in future ACCC monitoring reports. This is expected to put the PC in a stronger position for the next inquiry to establish whether the airports have used their market power, as well as making airport performance more transparent to the ACCC and airport users. However, the additional information proposed by the PC is still based on accounting information and it is not proposed that it should be prepared on the basis of prescribed methodologies. By way of comparison, the information the additional information the PC proposes in its recommendations would result in a significantly less rigorous framework than the Information Disclosure framework available to the New Zealand Commerce Commission. The New Zealand Information Disclosure regulation has allowed the Commission to establish the use of airport market power by some New Zealand airports.

Given the current and proposed approaches to establishing "evidence" of the use of market power by airports, it is highly unlikely in my view that the PC would find "evidence" of whether airports have exercised market power even if use of market power had occurred.

What would constitute sufficient information to establish "evidence" of the use of market power?

Given the limitations of monitoring data and benchmarking studies for the purpose of providing "evidence" of the use of market power, it is not clear what the PC would regard as sufficient information to recommend changes to the current regulatory framework for airports.

There is a range of information currently available to the inquiry. The ACCC has raised concerns about the use of market power based on the airport monitoring carried out from 2002, although they note that the information available to them is not "conclusive" in establishing use of market power. Other

independent analysts, including the Grattan Institute and Professor Peter Forsyth, have indicated that the available information suggests the use of market power by some airports.

Industry stakeholders, including international, domestic and regional airlines, off-airport car parking companies and rental car companies, have provided a wide range of information claiming that airports have used their market power.

Although the PC may not regard the information before them as sufficient “evidence” of the use of market power, it does at a *minimum* raise concerns about ongoing unresolved issues associated with airports in their dealings with users.

What additional regulation would the PC apply to airports if they found “evidence” of the use of market power?

The stronger regulatory measures which the PC has proposed in previous reports, and in the current draft report, could be applied to airports would be ineffective, inefficient or would not involve regulation. The regulatory measures include use of Part VIIA of the *Australian Competition and Consumer Act 2010*, recommendation by the Minister to apply the Part IIIA declaration process and the Government invoking measures under the Commonwealth leases with the airport operators. The 2007 and 2011 Inquiries recommended additional procedures and processes as measures to provide a “credible” threat of stronger regulation, such as the 2007 Inquiry recommendation for a ‘Show Cause’ mechanism.

How willing would the PC be to apply additional regulation to airports?

PC inquiries into economic regulation into industries with monopoly characteristics, including inquiries into the economic regulation of airports, have reflected a strong predisposition against regulation. Discussion of regulation by the PC generally places a strong emphasis on regulatory risk and regulatory error which is not balanced by consideration of the institutional and legislative frameworks in which regulation is undertaken, including the protections available in these frameworks. The PC gives little weight to the experience and practice of regulation in its Draft Report.

The view of economic regulation expressed by the PC could be seen as akin to the use of criminal law, such as the “innocent until proved guilty” philosophy, and a view reflected in the Draft report where regulation is seen as a “penalty” on airports, as opposed to a potential “remedy” for market failure.

Conclusion

In my view, in the Draft Report and in the context of the public hearings, the PC has not provided a convincing approach to establishing whether airports have used their market power. Further, the PC has not made recommendations for specific, credible, efficient and effective regulatory intervention in situations where airports are considered to use market power. These factors do not give me confidence in the PC’s general statement:

“If we found evidence of an exercise of market power, we would not hesitate in recommending more regulation.”

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