



Government
of South Australia

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Mr Garry Potts
Presiding Commissioner
Price Regulation of Airport Services Inquiry
Productivity Commission
PO Box 80
BELCONNEN ACT 2616

Minister for Transport
Minister for Infrastructure
Minister for Energy
12th Floor, Roma Mitchell House
136 North Terrace
Adelaide SA 5000
GPO Box 2969
Adelaide SA 5001
DX 154
Tel 08 8226 1210
Fax 08 8226 0844

Dear Mr Potts

I refer to the Productivity Commission Issues Paper, Price Regulation of Airport Services, dated May 2006, and your request for submissions on this matter.

The South Australian Government supported the substitution of prices monitoring for the regulated price cap at Adelaide Airport in its submission to the Commission of 24 April 2001. Its view then was that Adelaide Airport had insufficient market power to extract excessive profits from aeronautical prices because the airlines had countervailing power to prevent it. Since we then had no experience of deregulated pricing at the leased airports, the South Australian Government suggested that light-handed monitoring was justified to ensure that consumers were protected from any possible use of monopoly powers.

In the five years since then aeronautical prices have increased substantially over their capped level. This appears to be the result of factors including the development of a new terminal, relatively low throughput numbers causing high unit costs and the upward valuation of aeronautical assets to reflect the airport lease price paid. While none of these are necessarily related to monopoly power, the result is nevertheless cause for concern.

The South Australian Government has consulted widely with Adelaide Airport Ltd (AAL) and its airline major customers. There seems to be general agreement that AAL negotiated its terminal pricing, terms and conditions with the airlines on a fully commercial basis. I understand both AAL and the airlines are broadly satisfied with the transparency and pricing certainty that this provides to all parties.

The airlines possessed significant countervailing power to AAL in the negotiation of the terminal development agreement and pricing. The extent of their countervailing power in the negotiation of prices for services outside the terminal, the current agreement for which expires in July 2007, or in the negotiation of new charges, remains to be seen. It is likely to be less.

Under these circumstances while the South Australian Government sees no justification for the reimposition of prices regulation of Adelaide Airport, a continuation of prices monitoring to identify any divergence from commercial practice is probably necessary.

The South Australian Government does not intend to be prescriptive in suggesting how monitoring should be carried out or what prices should be included in a monitoring program. Those are properly matters for your inquiry. I suggest, however, that there are fundamental issues on which a monitoring program should be based and on which the inquiry should focus. They are: the establishment of a consistent methodology for the valuation and revaluation of aeronautical assets and their relationship to aeronautical prices; a methodology for periodic revalidation of pricing efficiency; the rationale for the exclusion from monitoring of a range of fees and charges subject to monopoly power that affect the airport costs of airlines and their customers; and how balance in commercial negotiations between the parties might be assured.

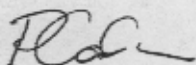
Depending on the degree of countervailing power that the airlines might possess in relation to any particular negotiations – whether over prices or airport services – it is difficult to see sufficient balance being achieved to assure a competitive outcome in the absence of behavioural undertakings by both parties and some sort of timely dispute resolution mechanism. Clearly Part IIIA of the Trade Practices Act, at least in its present form, will not meet those needs.

I see no reason why attention to these core issues should result in a monitoring process any more intrusive than the one presently in place. In fact, I would hope that the Commission will seek ways to reduce the compliance costs of the current program.

Please regard these as my preliminary views. I look forward to the availability of your draft report, on which the Government will comment as necessary.

Thank you for bringing this matter to my attention and providing the opportunity to provide input to your inquiry.

Yours sincerely



HON PATRICK CONLON MP
MINISTER FOR TRANSPORT

27 July 2006