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**SUBMISSION**

# Economic Regulation of Airports

August 2018

The Business Council of Australia welcomes the opportunity to respond to the Productivity Commission's (Commission) Issues Paper on the 'Economic Regulation of Airports'.

## KEY RECOMMENDATIONS

1. The economic regulation of airports in Australia should encourage the efficient use of critical infrastructure, preserve strong incentives to invest and innovate in the long-term interest of consumers, minimise the regulatory burden faced by all parties and promote commercially negotiated outcomes wherever possible.
2. Long-term strategic planning must support improved access to airports, such as preserving transport corridors.
3. More efficient major project approval processes at the state and territory level are needed to speed up investment in airports and the adjacent land transport infrastructure.
4. Operating restrictions at Australia's major airports should be amended where this would result in a net public benefit. For Sydney Airport, there should be greater flexibility in the application of the flight cap and curfew dispensation. Such changes would yield significant increases in productivity and prevent disruptions for passengers, while still preserving the benefits of the operating restrictions for residents that live near Sydney Airport. There should be no curfew at Western Sydney Airport.

## BACKGROUND

Australia's network of airports plays a vital economic role as the gateway infrastructure to our major cities and regions. Over the past decade, Australia's aviation industry has grown strongly, with total passenger numbers at Australia's four largest airports reaching 115 million in 2016–17, up by 30 million (or 34.9 per cent) since 2007–08.<sup>1</sup> Air freight has also continued to grow strongly, with over 1,000,000 tonnes of international air freight arriving in Australia in 2017, an increase of 4.8 per cent from a year earlier.<sup>2</sup>

A range of regulations apply to the operation of airports in Australia. As well as being subject to Australia's general competition laws, Australia's major airports (located in Brisbane, Melbourne, Perth and Sydney) are subject to a price monitoring regime under Part VIIA of the Competition and Consumer Act 2010 (CCA).

In June 2018, the Australian Government asked the Commission to investigate whether the economic regulation of airport services promotes the efficient operation of airports and related industries. The focus of the inquiry is the provision of passenger and freight services at the main passenger airports in Australia's major cities.

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<sup>1</sup> Australian Competition and Consumer Commission, *Airport Monitoring Report 2016-17*, May 2018, p. 12.

<sup>2</sup> Australia's Bureau of Infrastructure, Transport and Regional Economics, *International Airline Activity Annual statistics for FY2016/17*, November 2017.

## POLICY DISCUSSION

### 1. Economic regulation of airport services

This will be the Commission's fourth investigation of the economic regulation of airport services since 2000. The reforms that stemmed from previous reviews by the Commission have helped to ensure Australia has a world-leading aviation sector.

It is vital that the Commission's 2018 investigation continues to promote an evidence-based, targeted and proportionate regulatory framework. If a case for reform is established, then the Commission should identify competition issues with as much granularity as possible and avoid introducing sweeping changes to the entire aviation sector.

The regulatory framework that applies to airports should continue to provide a strong incentive for businesses to improve quality, reduce costs and innovate to meet the needs of consumers. This means we need a regulatory framework that recognises that efficient investment, innovation and increased productivity are crucial to provide consumers with greater choice and quality at competitive prices over the long-term. Striking the right balance between these objectives is key to ensuring vital infrastructure assets such as airports are contributing to a more productive economy and are used as efficiently as possible.

The CCA and the *Airports Act 1996* provide the legislative framework for the ACCC to monitor the prices, costs and financial returns relating to the supply of aeronautical and related services at designated airports.<sup>3</sup> The ACCC releases its airport monitoring report annually. At ministerial discretion, the ACCC can also undertake a price inquiry into airport pricing under Part VIIA of the Act.

In its 2012 Inquiry Report 'Economic Regulation of Airport Services', the Commission concluded that the ACCC's monitoring regime that had operated since 2002:

- had led to a marked increase in private investment at Australia's airports, which meant that Australia's major airports had not experienced the bottlenecks that had affected other key pieces of infrastructure;
- had not led to the inappropriate exercise of market power, with Australian airports' charges, revenues, costs, profits and investment found to be reasonable compared with (the mostly non-commercial) overseas airports; and
- while there were some exceptions, Australia's major airports were regularly regarded as providing either 'good' or 'satisfactory' overall service quality.<sup>4</sup>

The Commission's 2012 Inquiry Report therefore recommended that an airport-specific arbitration regime, activated by deemed declaration of airport services under Part IIIA of the CCA, should not be introduced because it could undermine effective light-handed regulation. The Commission remained of this view in its 2014 National Access Regime Inquiry Report.<sup>5</sup>

However, the Commission's 2012 Inquiry Report did note that fundamental to the effectiveness of the light-handed approach is the existence of a credible threat of sanction for airports that abuse their market power. While the Commission did not believe that this

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<sup>3</sup> Section 95ZF of the Competition and Consumer Act 2010 and Part 8 of the Airports Act 1996

<sup>4</sup> Productivity Commission, *Economic Regulation of Airport Services*, 2012, p. xx

<sup>5</sup> Productivity Commission, *Inquiry Report: National Access Regime*, 2014, p. 27

warranted the introduction of formal ACCC arbitration powers, the Commission's 2012 Inquiry Report did recommend that as part of its monitoring report process, the ACCC should be able to nominate that an airport show cause why its conduct should not be subject to scrutiny under a Part VIIA price inquiry.<sup>6</sup>

In 2015, the Australian Government's Competition Policy Review looked at the economic regulation of airports in Australia and found that, *"The price monitoring and 'light-handed' regulatory approach in aviation appears to be working well overall. However, if prices continue to increase as fast as they have been, that would raise concerns and may warrant a move away from light-handed regulation for individual airports."*<sup>7</sup>

Following on from the completion of the Competition Policy Review, changes were made to the National Access Regime that operates under Part IIIA of the CCA. In November 2017, the government also introduced significant legislative changes to the section 46 misuse of market power provision of the CCA.

In its most recent Airport Monitoring Report 2016-17 (released in May 2018), the ACCC found that its price and service monitoring regime is limited in its ability to address behaviour that is detrimental to consumers<sup>8</sup> and that the monitoring regime does not enable the ACCC to assess in detail whether an airport has exercised market power to earn monopoly profits.<sup>9</sup>

For the 2018 Inquiry into the 'Economic Regulation of Airports', the Australian Government has asked the Commission to consider the effectiveness of the ACCC's price and quality of service monitoring in achieving the following objectives:

- promoting the economically efficient operation of, and timely investment in, airports and related industries;
- minimising unnecessary compliance costs; and
- facilitating commercially negotiated outcomes in airport operations.

The Business Council agrees with the government's emphasis on promoting efficient investment, minimising compliance costs and facilitating commercial negotiation. Policy makers should promote these market characteristics where possible and only regulate where there is a clear rationale and in accordance with best practice regulation principles. The Commission has set out the key elements of best practice in Figure 1 below.<sup>10</sup>

**Figure 1: Productivity Commission's framework for regulation**



<sup>6</sup> Productivity Commission, *Economic Regulation of Airport Services*, 2012, See Recommendation 9.2 on p. 199.

<sup>7</sup> The Australian Government, *Competition Policy Review*, 2015, p. 205.

<sup>8</sup> Australian Competition and Consumer Commission, *Airport Monitoring Report 2016-17*, 2018, p. 9.

<sup>9</sup> Australian Competition and Consumer Commission, *Airport Monitoring Report 2016-17*, 2018, p. 189.

<sup>10</sup> Productivity Commission, *Inquiry Report: Economic Regulation of Airports*, 2018, p. 3.

In the context of Australia's aviation sector, applying best practice regulation principles means that:

**1. The problem to be solved is well understood:** Policy-makers must first understand the problem or policy priority in depth. Is the current framework sufficient and have circumstances changed since the previous reviews by the Commission and the National Competition Policy Review?

**2. Regulation is subject to cost–benefit analysis:** The costs and benefits of regulation are thoroughly assessed and tested with the community through a consultation process.

**3. Regulation achieves its objectives at least cost:** Regulation is carefully targeted to achieve its stated objectives and minimise cost impacts, which ultimately impact on consumers. Regulation is easily applied and understood by regulated entities. Opportunities should be sought to co-design regulation with industry or consider the potential for self-regulation.

**4. Regulators can perform their role efficiently:** The regulatory framework should be able to be administered by regulators in the most efficient and timely manner possible. This will facilitate investment, minimise unnecessary regulatory compliance costs and promote efficient commercial negotiations.

## 2. Land transport linkages to airports

Australia's major airports are used to transport passengers to and from Australia. They also play a critical role in assisting Australian businesses and consumers to take part in global trade and commerce.

Airports provide the critical infrastructure link that connects suppliers, air-freight services and ground transport services to ensure the efficient movement of high-value and/or time-sensitive goods. It is therefore vital that the Commission's inquiry identifies any unnecessary constraints on the provision of efficient land transport linkages to airport infrastructure.

Improving the performance of land transport linkages to airports will require:

- effective strategic planning and decisions about land use around airports
- efficient planning approval processes for new investment.

Australia's 21 leased federal airports sit on Commonwealth land. Yet the planning and approval processes for the areas surrounding these airports is subject to state, territory and local government control.

More effective long-term strategic planning therefore requires consistent and effective coordination between federal, state and local government. For instance, the incremental urban encroachment around Australia's major airports threatens to constrain access and the efficient operation of airports and, if unaddressed, will only worsen as passenger numbers continue to rapidly increase in future decades.

Evidence-based advice provided by Infrastructure Australia and the infrastructure agencies in the states and territories should continue to play an essential role in identifying the land transport projects near airports that have the highest net economic and social benefits.

To demonstrate the benefits that can be attained through effective long-term planning, Infrastructure Australia research has found that the protection and early acquisition of just

seven corridors identified as national priorities on the Infrastructure Priority List (such as the Western Sydney Airport Rail Line) could save Australian taxpayers close to \$11 billion in land purchase and construction costs.<sup>11</sup>

As outlined in the Business Council's Competitive Project Approvals report (released November 2016), planning reform should include all jurisdictions moving to a best practice model for assessing and approving major investments, characterised by a more strategic and timely approach to planning decisions.

### 3. Regulatory constraints on airport operations

Sydney Airport is Australia's busiest airport and most critical international gateway. The efficient operation of Sydney Airport is important for productivity and for growing Sydney's visitor economy.

To demonstrate the benefits of improving operational efficiency at Sydney Airport, a 2018 study (released earlier this year) by Deloitte found that an additional daily A380 service from China would, on an annual basis, contribute \$470 million to the NSW economy and generate an estimated 5200 Full-Time Equivalent jobs.<sup>12</sup>

Sydney Airport's operations are subject to a range of regulatory constraints that are designed to minimise the noise impacts on neighbouring properties. In its most recent Airport Monitoring Report (released in April 2018), the ACCC highlighted the need for policy-makers to ensure that the restrictions that apply to Sydney Airport remain fit for purpose:

*Such constraints on nationally important infrastructure can impose significant costs on users and the broader economy. While there may be social policy reasons for these constraints on Sydney Airport, they should be regularly reviewed given advances in noise reduction technologies.*

The rigid application of the regulations can result in major delays in take-offs and landings when there are disruptions, and even the re-routing of aircraft (near the curfew), which impose significant costs and inconvenience on passengers.

London's Heathrow Airport also has restrictions on the number of permitted flights, including overnight operations. However, the application of these restrictions has been designed to provide the airport with more flexibility. For example, Heathrow's cap on the number of flights is only applied annually, rather than over a rolling hour as occurs at Sydney Airport.

The cap on overnight flights at Heathrow is also subject to a 'Quota Count' system, which means that aircraft are distinguished based on their actual individual noise performance. This means that older and noisier aircraft take up more of the annual cap than newer and quieter aircraft. This system incentivises the use of newer and quieter aircraft and is designed to better achieve the underlying policy goal of reducing aircraft noise.

There would be significant benefits to passengers from the Commission identifying opportunities for greater flexibility in the way the operating restrictions are enforced at Sydney Airport. Such changes could yield significant increases in productivity and prevent disruptions for passengers, while still preserving the benefits of the operating restrictions for residents that live near Sydney Airport.

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<sup>11</sup> Infrastructure Australia, *Corridor Protection: Planning and investing for the long term*, July 2017.

<sup>12</sup> Deloitte Access Economics, *The Economic Contribution of Sydney Airport*, April 2018, p. 12.

Under the inquiry's terms of reference, an evaluation of Sydney Airport's operating constraints is warranted under the reference that the Commission "should focus on the provision of passenger and freight transport services at, and surrounding, the main passenger airports operating in Australia's major cities".

It is also recommended that the Commission quantify the economic effect of the current operational constraints that apply to Sydney Airport and the potential benefits of reform. For instance, understanding the opportunity cost of the Regional Ring Fence arrangements would enable policy-makers and members of the public to better understand the economic costs and benefits of those regulations.

The Business Council's recommendations are set out below.

**1. Remove the prescribed list of allowable aircraft that can operate during curfew hours.**

The list of prescribed allowable aircraft is set out in the *Sydney Airport Curfew Act 1995*. The prescribed list should be replaced with a principles-based approach, or an objective noise measure, which would better achieve the policy intent of the operational constraint.

**2. Remove the flight cap on actual flight movements and apply it to allocated slots (scheduled flights) only.**

Measured over a rolling hour, commencing every 15 minutes, the flight cap means no more than 80 runway movements occur in any hour. Currently, there are essentially two caps: one for allocated slots, and one on actual movements or flights. Applying only one cap on allocated slots (scheduled flights) would allow the airport and airlines to recover better from delays.

**3. Remove the 15-minute rolling hour of the slot management regime, with the hourly cap (currently set at 80 flights) ideally averaged over a longer period, say a day, a week or a month.**

The 15-minute reset period is designed to space out the noise pollution and to ensure the flight cap is not breached. This is very rigid and greatly impacts the airport's efficiency and the ability to accommodate and recover from disruptions.

**4. Allow 'weather related events' to be included as grounds for curfew dispensation.**

Adverse weather conditions, whether foreseen or not, can occur over relatively short periods, at highly localised geographic locations, and have significant flow-on impacts (for hundreds of passengers). This mean dispensation is needed to allow flight movements in the curfew to minimise passenger disruption and dislocation – often at great cost to both passengers and/ or airlines.

The new Western Sydney Airport will cater for increasing demand for aviation services driven by strong population growth and growth in the wholesale trade sector, which is a major user of air transport services. The Commission should make an explicit recommendation that a curfew not be imposed at Western Sydney Airport.

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