



PRODUCTIVITY COMMISSION INTO THE ECONOMIC REGULATION OF AIRPORTS – KING ISLAND COUNCIL

EXECUTIVE SUMMARY

In a move towards a user pays model for its airport, Council proposed increases to its overall fees and charges. These were designed to stem the current financial losses and enable the airport to work towards operational cost neutrality.

Calculation of the fees were made with the passenger movement information available from the Bureau of Infrastructure, Transport & Regional Economics (BITRE), recorded landings over the last three financial years, and through utilisation of the in-house aviation experience available to Council. There has been significant push back from the servicing airlines and as a result Rex have permanently withdrawn 30% of their flights from the key destination of Tullamarine.

At this time Council have requested assistance at State level to resolve the ongoing issue of commercial negotiations with Rex.

INTRODUCTION

King Island is a part of the state of Tasmania located in the western entrance of Bass Strait mid-way between Tasmania and Victoria. Ownership of the King Island Airport (the Airport) was handed over from the Commonwealth Government to King Island Council (Council) in 1993 and from that point forward Council have owned and operated the airport.

As the only gateway to the Island for visitors and residents alike, the airport is arguably the single most critical piece of infrastructure on the Island. Located approximately 10km north east of the main township of Currie, it is serviced by three Regular Public Transport (RPT) airlines being King Island Air, Regional Express (Rex) and Sharp Airlines with flights arriving and departing to Victoria (Tullamarine, Moorabbin and Essendon) and Launceston via Wynyard in Tasmania.

In addition to the RPT movements there are open and closed charter operations, vital medevac services and regular freight movements, as well as frequent general aviation usage of the Airport.

There is one chip sealed runway designated 10/28. It is 1585m long x 30m wide and with its classification of PCN 11/F/A/580/U it can accommodate up to Saab 340 sized aircraft. The central 18m of 10/28 was resealed in 2011 and investigations are currently under way to determine the scope and timing of the next pavement works.

There is a secondary gravel surface runway designated 17/35 which is 1105m long by 30m. This runway is only ever selected for use by smaller aircraft when cross winds prevent operations on 10/28.

Refurbishment and expansion of the airport terminal was funded in part by a State Government grant in 2015.

The airport currently has a staff complement of 2.5 FTE positions.

MARKET POWER

As the only commercial airport on King Island, Council appreciates that its' Airport could be perceived as a monopolistic opportunity. However, Council suggest that, as the impact on its residents of losing these services is significantly greater than the impact on an airline of losing one route in a network, the balance of power in this situation sits squarely with the airline.

When Council recently attempted to increase fees in order to mitigate the financial burden of the Airport on its community, Rex (the only airline servicing the key port of Tullamarine) immediately announced withdrawal of 30% of its air services. This reduced schedule was introduced almost immediately (from 14 August) despite Council's proposed fee increase not due to come in to effective until 1 October 2018.

Direct impacts of this last minute schedule change have already been felt by tourism operators on the Island, with one business reporting lost revenue of almost \$150,000 in the month that the changes came into effect. Operators have also passed on comments from potential visitors which indicate the tone of recent media releases from Rex has damaged the reputation of King Island and Tasmania as potential destinations.

This level of impact on a community the size of King Island is significant and the threat of such will hamper Council's decisions in considering how to best manage its assets for the good of the whole community.

FEES AND CHARGES.

In preparing its budgets for the last three financial years Council has considered the introduction of increased fees and charges to mitigate the financial losses experienced.

Table 1 Operating Airport Profit (loss) last 3 FY's

Financial Year	Operating Profit / (Loss)
15/16	(\$280k)
16/17	(\$350k)
17/18	(\$470k)

Improvements in operational compliance and managing increased throughput at the airport has contributed to increased operational expenditure each year. Despite significant increases in passenger throughput and aircraft landings at the airport (refer Attachment 1), operational revenue has not increased at the same rate, leading to a growing deficit.

During 2016 and 2017 Council proposed fee increases at the Airport to address these financial losses. In each case, significant lobbying by airlines and/or their supporters on the Island resulted in the proposals being rescinded by Council before coming into effect.

In preparation of the FY19 Airport budget, Council reviewed its operational expenditure and attributed each line to its specific area of operation, e.g. passenger terminal, runway and apron areas. Fees and charges were then calculated based on usage numbers in the 2017 calendar

year, including passenger numbers and aircraft landings by type of airline, with the objective being to recover most, but not all, of the associated expenditure.

Attachment 2 details the current and proposed fees and charges at the King Island Airport, as agreed by Council at its ordinary meeting on 26 June 2018. The following table shows the existing and proposed Council Airport fees for regular public transport (RPT) operations.

Table 2 Existing vs New fees

FEE VALIDITY DATES:	TYPE OF FEES (ex GST)	
	\$ per tonne of maximum take-off weight (MTOW)	Per passenger / movement
Existing:	\$20.97	-
Proposed: (from 1 October 2018)	\$25.00	\$6.82

All airlines known to service King Island on a regular basis were contacted directly in advance of Council's decision to advise them of the potential increase in fees and charges. Full financials for FY18 were also shared to transparently demonstrate Council's position. Once Council confirmed their decision at their ordinary meeting on 26 June, airlines were given a grace period of three months before the revised fees would come into effect.

AN AIRPORT 'GIFT'

In one of their media releases Rex refer to the fact the airport was 'gifted' to Council by the Federal Government. In hindsight it is arguable that many of the perceived issues generally associated with Local Government ownership of airports (inefficiencies and lack of aeronautical commercial negotiating skills as examples from the Issues Paper) could be attributed to the handover of ownership process undertaken back in the early 1990's.

Ownership of the airport brought a need for skills that most Councils – particularly smaller and remote Councils like King Islands' – simply did not have. Given airport management, compliance and design services were previously provided by the Department of Civil Aviation (DCA) there was nationally an immediate and massive shortfall of experienced aviation people available.

Capital city airports got the cream and remote island ports such as King Island continue to either appoint good non-aviation people and attempt to train them up (i.e. they learn on the job) or do the best they can recruiting on the limited remuneration they can offer. Either option usually requires a degree of reliance on external consultants driving the operational costs of the airport higher.

As Council continues its' own search for a new Airport Manager its noted that Emerald Airport is also currently in market, offering \$170k p.a. While it is anticipated that this value would bring an experienced airport manager to the table, Council could never justify that type of salary under both the existing Council salary relativities and the turnover of the airport.

Council recognises that with a greater understanding of aviation and stronger partnerships with the airlines the recent commercial negotiations would have played out differently. However, Council suggests this is a common issue across many of the smaller regional airports we interact with and therefore may be worthy of attention by Government to prevent similar situations in the future.

MANAGEMENT STRATEGY

Given the lack of formal guidance provided with the Federal Government assignment of the airport infrastructure, Council has created its own management strategies for operating the Airport. These strategies have changed over time driven by the economic ups and downs the island has experienced and by changes to the local government regulatory frame work. The latter is important as it is changes in that framework regarding arrangements for valuing Council owned assets and as such differing depreciation values, which is one point that Rex holds in contention.

Council has been encouraged by its Audit Panel to manage the Airport as a standalone business unit, moving towards operational cost neutrality through a user pays approach. Council believes this is the most equitable model for running the Airport as it does not require ratepayers that rarely use the airport to contribute to the upkeep of that asset. Council is reviewing its contractual arrangements with its non-aeronautical stakeholders and building new freight facilities for lease to broaden the revenue base and ease reliance on aeronautical revenues. Continuing review of operational practices also seeks to reduce expenditure where possible.

The proposed increased RPT fees were part of the adopted user pays approach. Since these were announced various airlines have rightly identified that the Airport provides flow-on economic benefits to the community and have suggested this should be considered when assessing the current financial losses experienced at the airport.

Council clearly understands that the higher the airport fees the more chance there is of losing price sensitive travellers to other destinations. It is also acutely aware of the impact on cost of living for residents of the island, not just through the cost of passenger flights, but through absorbing those passenger and airfreight price increases into the cost of goods and services on the Island. As such every effort has been made to try and achieve an appropriate and sustainable price point.

OPPORTUNITIES

King Island has a growing tourism sector but remains in stiff competition with Flinders Is and mainland Tasmania for inbound Tasmanian tourism, and with other domestic destinations such as Kangaroo Island.

The island receives no direct financial support from Tourism Tasmania (TT) and yet has tremendous potential as a destination particularly from the golf sector. Council believes that with greater demand generated through collaborative destination marketing (Council, TT, airline partners, etc) passenger numbers can be driven up possibly allowing for reduced fees across a larger passenger base.

Without responsible fiscal management of the Airport, the island will be poorly positioned to sustainably cater for increased aircraft movements and passenger numbers.