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QANTAS SUBMISSION
NATIONAL ACCESS REGIME INQUIRY

This Submission responds to the invitation by the Productivity Commission for submissions concerning its inquiry into the National Access Regime.

The primary interest of Qantas in relation to this inquiry is the regulation of Australian airports. As the Productivity Commission will be aware, Qantas is the major user of services provided by Australian airports. Many services provided by Australian airports are subject to the National Access Regime under Part IIIA of the *Trade Practices Act 1974* ('**TPA**'), as affected by section 192 of the *Airports Act 1996* ('**Airports Act**').

As Qantas' interest in this inquiry is principally industry based, the comments in this Submission are confined to observations about the application of the National Access Regime to airport services. In making this Submission, Qantas is also conscious that the Productivity Commission is conducting simultaneous Inquiries in respect of:

- the *Prices Surveillance Act 1983* (which regulates the prices of various airport services); and
- Price Regulation of Airport Services.

Many of the observations made by Qantas in this Submission span all three Inquiries.

The Productivity Commission's Issues Paper is broad ranging. It poses both high level questions (for example, whether the National Access Regime should be confined to vertically integrated natural monopolies) as well as more detailed questions concerning the language and operation of Part IIIA. This Submission concentrates primarily on the high level questions in the context of the airport industry and discusses:

- the natural monopoly and bottleneck (or essential facility) characteristics of airports;
- the nature of the commercial problems that arise from airports as essential facilities;
- the types of regulatory responses that are required to address those problems; and
- improvements that might be made to the National Access Regime as it applies to airports.

The Submission concludes that both access and pricing problems exist at airports, and that these problems are interlinked. In addition, the Submission explains why access problems are not confined to vertically integrated natural monopolies.

Qantas would be pleased to expand on any of the points raised in this Submission and provide additional information and data, if requested by the Productivity Commission.

Natural Monopoly and Bottleneck (or Essential Facility) Characteristics of Airports

It is widely accepted that airports:

- are natural monopolies (they are characterised by large economies of scale and scope relative to the size of the market such that it would uneconomic (if it were politically feasible) to develop an alternative facility);
- represent bottlenecks or essential facilities (in the sense that they supply services that are essential inputs for the provision of aviation services); and
- are nationally significant infrastructure assets.

Natural Monopoly Characteristics

In its inquiry into the aeronautical and non-aeronautical charges of the Federal Airports Corporation (Report No. 48, 1993), the Prices Surveillance Authority commented:

> *'Airport service markets are largely non-contestable: provision of airport services tends to be characterised by very large sunk costs and high barriers to entry. In addition, there appear to be economies of scale in the provision of airport services and significant economies of utilization over*

a range of levels of airport activity, which ensure natural monopoly status. Airports, like other utilities, exhibit joint and common production cost characteristics in the production of multiple services. Airports generally can be considered to be local monopolies in the provision of aeronautical services. Finally, the characteristics of airports has led to regulation of airport charges in several countries, including the United Kingdom.' (pp. 47-48).

In the same report, the Prices Surveillance Authority considered the extent of competition between airports. It concluded:

'*... the major airports in Australia are not particularly good substitutes for each other. Apart from a few areas where there are effective alternative airports in close proximity, such as the New South Wales north coast, most destination regions offer only one airport. In the capital cities, only the major airports are capable of handling large jet aircraft used by RPT [Regular Passenger Transport] airlines.*' (p. 51).

These conclusions have been reaffirmed more recently by other bodies. In its draft guide to section 192 of the *Airports Act*, the ACCC commented:

'*The combination of economies of scale and significant entry and exit costs means that most larger airports, including most if not all core regulated airports, could not be economically duplicated.*' (p. vii).

In considering an appeal by Sydney Airports Corporation Ltd ('**SACL**') against declaration of various services pursuant to section 44H of the TPA, the Australian Competition Tribunal commented:

'*The Tribunal heard that most major commercial airports around the world exhibit strong natural monopoly or bottleneck characteristics. Once the basic infrastructure (runways, taxiways, control tower) is in place, the owner of the facility faces sharply falling costs of servicing increments of demand (economies of scale). By contrast, a new entrant would have to replicate this basic infrastructure which is inherently capital intensive.*'

'*Such airports typically provide a bundle of services, (for example, international and domestic passenger and freight services). In addition, many airports also benefit from economies of scale and scope generated by strong network effects associated with the geographic location and the absence of viable transport modes. Passengers typically travel to destinations, not airports, and airlines will prefer to locate at one airport so that they may gain commercial benefits from interconnecting with other services and airlines.*'

'*SIA [Sydney International Airport] exhibits very strong bottleneck characteristics:*

- *not only is it Sydney's only international airport, it is Australia's major international airport, handling some 50% of international air freight leaving and entering Australia;*
- *it handles the largest portion of total international passenger traffic entering and leaving Australia;*
- *it is a national and regional interconnector with domestic passengers travelling overseas, with the two domestic carriers (Qantas and Ansett) having invested very large sums in their passenger handling facilities.*'

The Tribunal identified a '*market controlled by SACL, for the provision of the complete suite of physical assets necessary to service international airlines flying into and out of the Sydney region - these assets exhibit very strong monopolistic (or bottleneck) characteristics because of pervasive economies of scale and scope and barriers to entry derived both from high sunk costs and the market size and location*'.

It is apparent from the foregoing that the natural monopoly and bottleneck characteristics of major Australian airports have been well recognised by a variety of economic regulatory bodies.

Countervailing Power

In the Interim Report issued in respect of the Prices Surveillance Inquiry, the Productivity Commission notes the submissions made by some Australian airports that major airlines have countervailing power in respect of the use of airport services. On this basis, a number of airports suggest that there is no monopoly problem that needs to be addressed by regulation.

This assertion by airports is incorrect and is contradicted by the behaviour of Australian airports.

Countervailing power is the term used to describe the commercial or bargaining power of a purchaser of goods or services which is sufficient to offset any market power possessed by the seller.

However, countervailing power does not arise merely as a result of a person being a large purchaser of goods or services relative to the market. Countervailing power can only arise if the buyer has choices available to it. For example, the buyer may have sufficient scale to facilitate a new entrant into the market for the supply of the goods or services the buyer is seeking to purchase. The prospect of new entry may act as a constraint on the seller. Alternatively, the buyer may have sufficient scale to contemplate new entry itself, and again the threat of new entry acts as a constraint on the seller.

However, if a buyer has no choices other than to purchase goods or services from a particular seller, no countervailing power will arise, no matter how large the buyer is relative to the market.

Provided customers want to fly, airlines have no choice but to use the services of the airport available in the relevant city. From a demand perspective, air transportation to a capital city is not substitutable for an alternate capital city. No airline, is in a position to bypass or otherwise facilitate new entry into the provision of airport services in Australia. Qantas has no choice but to use the services offered by airports.

The significant monopoly power held by Australian airports is well illustrated by the current position of Sydney Airport. It is recognised that, due to Government policy, Sydney Airport is slot constrained, or close to constraint, at peak periods of use. Furthermore, Sydney Airport has recently applied to the ACCC to substantially increase aeronautical charges levied on airline users (to more than double current charges).

Despite the Government imposed congestion problem and Sydney Airport's desire to dramatically increase its prices, there is no prospect of airlines being able to bypass Sydney Airport, or replicate an airport facility to service Sydney. The reasons that such bypass or new entry are not viable are many and complex, but include:

- the construction of an airport requires the acquisition of a large amount of land and it is virtually impossible for the required quantity of land to be acquired by private interests in reasonable proximity to capital cities; and
- there are substantial political and regulatory approvals required to construct and operate an airport, which effectively prevent the construction of an airport by private interests without full government endorsement and backing.

It is apparent from the history of the proposed second airport to service the Sydney basin during the past 40 years that such approvals would be difficult to obtain. Accordingly, Sydney Airport is able to exercise complete monopoly power and no airline has any countervailing power in response.

It should be noted that airlines may have a degree of countervailing power in respect of services that do not need to be supplied from the airport location. For example, catering preparation facilities do not need to be (and are not in practice) located at the airport.

However, there are a large number of services required by airlines that must be located at the airport, either from physical or economic necessity. Many of these services are described in the ACCC's draft guide to Section 192 of the *Airports Act* (October 1998) as satisfying section 192(5) of the Airports Act. These are:

- airside facilities (runways, taxiways, aprons etc);
- certain passenger processing areas (check-in desks, gate lounges, customs etc);
- refuelling facilities and sites for providing refuelling services;
- sites for providing ground handling services and ground handling equipment storage facilities;
- sites for light/emergency maintenance facilities; and
- landside vehicle facilities.

(Although the draft guide provides a useful checklist, Qantas does not endorse all of the conclusions in the ACCC's draft guide.)

In fact, the services which must be located at the airport extend beyond the above services and include:

- services such as land and buildings for:

  - airline office space;
  - facilities for staff eg staff, lunch and changing rooms;
  - storage areas (including wheelchair storage); and
  - customer service and baggage services areas; and
- land and buildings utilised by airlines to provide a range of expected services to air travellers such as:
  - commercial and transit lounges;
  - premium class check-in services; and
  - 'seamless' transfer areas required to transfer passengers airside between international and domestic terminals.

It might be suggested that the enhanced facilities referred to in the 2nd bullet point above are not essential, and that airports do not therefore possess monopoly power in the supply of the required land and buildings. Qantas submits that airports do possess monopoly power in respect of these services because:

- there is a strong demand/expectation from air travellers for these services;
- these services can only practically and economically be provided at the airport location; and
- downstream competition between airlines will continue to see these services developed and enhanced further.

In order for Australia to continue to develop an internationally competitive air transport industry, it is essential that airlines develop these enhanced services at an efficient cost. The airports possess the monopoly power to determine whether, to what extent and at what price these enhanced services will be available to air passengers. It is unrealistic to suggest that airlines possess countervailing power in respect of these services.

The absence of countervailing power possessed by major airlines or other substantial users of airport services is also evidenced by the conduct of major airports during the past 2-3 years. Examples are set out below with further examples provided in the confidential appendix attached to this Submission.

- As noted above, Sydney Airport is currently seeking to increase aeronautical charges by more than 100%.

- In Qantas' experience, almost all airports provide services on the basis that the airport does not enter into formal written agreements under which the airport promises any specific level or quality of service provision. Accordingly, there is no commercial incentive or pressure for the airport to act efficiently or with quality in the supply of its services. Qantas and other airlines have sought to enter into service level agreements with a number of airports but, due to the monopoly position of the airports, Qantas has not been able to do so. It is clearly not in the airports' interests to enter into agreements with airlines under which they will be penalised for failure to meet agreed service levels. Airlines have no countervailing power with which to force the issue. It is probably one of the few industries in the world where customers pay millions of dollars in fees but do not have a comprehensive written agreement which clearly sets out the services which will be provided in return for those fees and the standard to which the services will be provided.

- Following privatisation, Brisbane and Perth airports introduced a fuel throughput levy payable by the major oil companies utilising a pipeline across the airport – the levy was immediately passed-on to the airlines. The pipeline and all associated infrastructure is owned, operated and maintained by the oil companies. The only service provided by the airports is a licence to run the pipeline across airport land, for which the fuel companies already pay a fixed licence fee. As observed by the ACCC, the fuel throughput levy was unrelated to any cost increases at the airport. If a fuel throughput levy equivalent to the Brisbane levy of 0.4 cents per litre was introduced at all major airports across Australia, the total cost to the oil companies – and immediately passed-on to the airlines would be approximately $20 million per annum, with Qantas' share being approximately $8 million.

- Brisbane, Perth and Canberra airports have introduced and Melbourne airport has proposed new charges payable by taxis accessing the airport terminals. Effectively, these new charges, which are unrelated to new investment, will place the airports in breach of the CPI-X price cap administered by the ACCC and should therefore result in a reduction in other aeronautical charges. The airports assert that these taxi charges are not included under the CPI-X price cap. The ACCC disagrees. However, the ACCC has no powers under the *Prices Surveillance Act* to enforce the price cap.

- Many airports have sought to substantially increase aeronautical charges, to recover amounts claimed to be 'necessary new investment'. The ACCC has rejected many of the increases but in the absence of prices surveillance by the ACCC under the *Prices Surveillance Act*, airports are likely to have introduced all of their proposed price increases (and presumably additional increases).

It should be observed that the above conduct occurred during a period in which:

- the major airports were subject to price and access regulation (although Sydney Airport does not have a CPI-X price cap and section 192 of the Airports Act does not apply to it); and
- the airports were aware that a review of the regulatory framework would take place in relation to the privatised airports.

Qantas believes strongly that airports (other than Sydney Airport – which is a good example of an airport which has not been under significant regulatory pressure) have not fully exercised their monopoly power during the past few years, both as a result of existing regulation and the pending regulatory review. However, even in this environment, increases in charges to airlines have occurred. Qantas believes that any lessening of the regulatory framework applying to airports will result in substantial increases in charges to airlines and their customers. Airlines will be unable commercially to prevent this occurring.

Bottleneck Characteristics

The bottleneck characteristics of Australian airports are also readily apparent. The primary economic and commercial activity of airports is to provide landing, take off, terminal and related services to airlines and their customers using the airport. To compete in the provision of aviation services, it is essential to obtain access to airports and airport services.

The wide range of airport services which are required for the supply of aviation services are discussed above. All of the services used by airlines (or their contractors) at airports represent bottleneck or essential services in the sense that any airline offering aviation services requires those services and inputs.

National Significance

In its report into International Air Services (Report No. 2, 1998), the Productivity Commission noted:

> '*The terms of access to airport infrastructure are vital to the efficiency and competitiveness of air services, both domestic and international.*' (p.199).
>
> '*Access to the services of essential facilities can be an important precursor to encouraging competition in related markets, and the economically efficient use of resources. ... the benefits of greater competition among airport service providers include lower costs and higher quality services to airlines and their passengers, and improved international competitiveness of Australian airports. This will enhance Australia as a tourist destination and a place for airlines to do business ...*' (p. 201).

The Productivity Commission also noted that the sale of Melbourne, Brisbane, Perth and Adelaide airports (which accounted for 44% of passenger and 42% of freight movements in 1996) realised $3.4 billion.

It is apparent that the major Australian airports (comprising at least the core regulated airports under the *Airports Act*) are nationally significant facilities.

<u>Problems Which Emerge from Airports as Essential Facilities</u>

The Issues Paper has a tendency to characterise problems which emerge from natural monopolies as either 'pricing issues' or 'access issues'. In other words, the natural monopoly either prices its services too high from an efficiency perspective, or forecloses market opportunity by denying access. In practice, the problems that can arise are often more complex, and pricing and access issues are often interlinked.

There appears to be little debate that airports give rise to monopoly pricing problems. However, the Issues Paper raises the question whether there is an access problem at airports. The question appears to be underpinned by two assumptions:

- in general terms, airports are vertically integrated; and
- the primary services sought by airlines from airports are landing and basic terminal services.

These assumptions are inaccurate or incomplete. As explained below, it is overly simplistic to characterise airports as businesses which are not vertically integrated. Furthermore, as discussed above, the range of services required by airlines at airports is far broader than landing and basic terminal services. Aviation is a far more complicated industry. There are a wide range of services required by airlines in order to conduct an aviation business. Furthermore, the range of services demanded by air travellers continues to expand – for example, new expanded lounges, premium check-in and arrivals lounges.

In Qantas' experience, access problems do arise at airports. These problems take one of two forms: either access is denied or frustrated or access is provided on unreasonable commercial terms (both price and non-price).

It should be stressed that the privatisation of Australian airports, and the establishment of the access regulatory regime, are relatively recent events. Qantas believes that airlines and airports have not yet had sufficient time to establish a commercial approach (supported by the regulatory framework) in which to negotiate access and resolve access disputes. Accordingly, to date there is little experience of utilising the regulatory framework to resolve access disputes. Qantas nevertheless firmly believes that there is a need for a clear regulatory framework, to underpin commercial negotiations and minimise the airports' abuse of their monopoly positions.

Denial of Access

Qantas has experienced substantial difficulty in negotiating access to a range of services at airports. The confidential appendix to this Submission provides examples of the range of services to which Qantas is seeking to negotiate access at airports, but to date has been unsuccessful (the appendix also provides examples of services which have been provided on monopolistic or unreasonable terms and conditions).

Qantas believes that there are a number of reasons why airports may deny or frustrate access to users of the airport.

1. Contrary to many assumptions, the airport may hold a degree of vertical integration in an upstream or downstream market, or be contemplating vertical integration.

   Vertical integration is an expression used to describe the commercial or economic integration of a firm into two vertically dependent markets. By vertically dependent we mean that the markets are functionally separate, but a good or service produced in one of the markets is required as an input in the other. In the conduct of their business, airports have a number of choices available to them. They may:

   - be a mere holder of land, leasing and licensing land to others;
   - be primarily a development and construction business, constructing buildings and other infrastructure which will be leased or licensed to others; or
   - be involved in business undertakings on the airport, for example, managing car parks, ground handling and other services provided at the airport to either consumers or other business users.

   The airport operator is free to make choices about the manner in which it will conduct its business. Furthermore, those choices may alter over time.

   Even where the airport operator does not conduct a downstream business itself, it may be economically integrated with the downstream business. For example, the airport operator may decide to grant an exclusive lease of a car park to a car park operator. Through its pricing structure, the airport operator may be able to extract all economic profits from the conduct of the single car park. Effectively, the airport operator is economically integrated with the operation of the car park. Furthermore, it may have no incentive to encourage development of additional car parks. It may also decide to deny airlines or other persons the right to conduct their own car parks (for example the valet car parks currently conducted by airlines).

2. The airport may deny access to a specific service to an airport user in order to gain a commercial advantage in other areas of its business. The airport may use the threat of access denial in order

to resolve a dispute with the airport user, or achieve a commercial outcome (such as increased prices) in respect of another airport service.

3. If the airport service is suffering a degree of congestion, the airport may simply find it easier to deny access rather than establish mechanisms to deal with congestion and scheduling problems. In other words, the airport would prefer a 'quiet life'.

In all of the above examples, airports have the ability and potential to damage competition in upstream and downstream markets. This may be a direct objective of the airport (if seeking to integrate vertically, whether through ownership or contractually), it may be an indirect objective (when seeking to obtain a collateral benefit) or may not be an objective at all (if pursuing a 'quiet life'). Whichever, Qantas believes that denial (or material delay) of access by airport operators is a real issue and has the potential to undermine competition in upstream and downstream markets. If, as a matter of policy, the National Access Regime is seeking to address competition problems which can emerge from significant essential facilities, those problems can and do arise at airports regardless of the degree of vertical integration. Qantas submits that a static analysis of vertical integration within the airport industry is not a relevant basis for applying or removing access regulation.

Provision of Access on Commercial Terms

Airports also refuse to provide access on reasonable and commercial terms and conditions (price and non-price).

In relation to price, there are many services and facilities used by airlines that are likely to be covered by the access regime, but which are not covered by *Prices Surveillance Act* regulation. The latter has a number of peculiar exclusions, including:

- aircraft refuelling;
- maintenance sites and buildings;
- freight equipment and storage sites;
- freight facility sites and buildings;
- ground support equipment sites;
- check-in counters and related facilities; and
- public and staff car parks.

Most of the above services would fall within the scope of section 192 of the *Airports Act*. Although these services are subject to price monitoring by the ACCC, this form of regulation has proved ineffective. For example, in relation to fuel throughput, the ACCC recommended the introduction of a cap on aircraft refuelling services in December 1998 but there would appear to be no political impetus for this to occur.

Prices Surveillance Act regulation also excludes any service which, on the date the airport lease was granted, was the subject of a contract, lease, licence or authority given under the common seal of the FAC. In these and other areas, including those referred to on pages 3 and 4 of this Submission, Qantas is subject to the monopoly pricing power of the airport. Examples of monopoly pricing are set out above and in the confidential appendix to this Submission.

In relation to non-price terms and conditions, Qantas' experience is that almost all airports provide services on the basis that the airport does not enter into written agreements under which the airport promises a specific level or quality of service provision and they are not willing to negotiate service level agreements. Accordingly, as discussed above, there is no commercial incentive or pressure for the airport to act efficiently or with quality in the supply of its services. This issue is illustrated by the general conditions of use which the airports endeavour to unilaterally impose in respect of the provision of aeronautical services. Such conditions of use generally:

- do not specify the services and facilities to be provided in return for the aeronautical charges;
- do not include any performance standard obligations on the airport;
- contain unreasonable price adjustment clauses; and
- contain exclusions of liability on the part of the airport, including liability for negligence, delays or failure to supply any of the services.

Examples of unreasonable terms and conditions imposed in relation to other services are set out in the confidential appendix.

The failure to agree to specific service levels and the imposition of unreasonable terms and conditions are characteristic of monopolies, and result from the use of monopoly power. None of this conduct would be sustainable in the absence of monopoly power. Furthermore, these problems are unable to be addressed merely through price regulation.

Downstream Competition and Efficiency

The consequences of these access problems are significant from an efficiency and public interest perspective. Airports play an important role in Australia's overall transportation system. They are necessary for air transport services, involving both the transportation of persons and goods. Accordingly, the efficiency and quality of airport services will impact directly on the efficiency and quality of Australia's transportation system and the markets which rely on that transportation system.

As monopolies, the primary concern of airports is profit maximisation rather than the efficiency of Australia's transportation system. This has been stated publicly by Sydney Airport in its application to the ACCC to increase aeronautical charges. Furthermore, the fact is apparent from the priorities set by airports in recent years in new development. For example, the redevelopment of the International Terminal at Sydney Airport (known as the SA2000 Project) based a higher priority on increasing retail shopping space compared with the expansion of aeronautical services (terminal gates and passenger seating). The problems associated with the SA2000 Project are set out in detail in the submission of the Board of Airline Representatives of Australia (**'BARA'**) to the ACCC.

Conclusion

In Qantas' view, the problems that arise from the monopoly power of airports can only be addressed through a regulatory framework which addresses both pricing and access issues, and which recognises the interlinked nature of the problems. Qantas would not support any lessening of the existing regime.

Appropriate Regulatory Responses to the Essential Facility Problems

The Issues Paper questions whether Part IIIA is an appropriate regulatory response to the pricing and access issues that arise in a variety of industries. In particular, the Issues Paper questions whether the pricing and access issues:

- can be addressed by market forces and Part IV of the TPA (the competitive conduct provisions);
- can be addressed by price regulation alone (without the need for a specific access regime),

and also questions whether improvements can be made to the operation of Part IIIA.

Market Forces and Part IV of the TPA

Qantas does not believe that the pricing and access issues that arise at airports can be addressed solely by market forces and Part IV of the TPA.

As explained earlier, most Australian airports have strong monopoly power and airlines do not possess countervailing power. Part IV of the TPA does not address monopoly power problems in themselves. Essentially, Part IV of the TPA prohibits various forms of conduct that have the purpose or effect of expanding or increasing market power. However, the mere use of market power, without the purpose or effect of expanding that market power, is not prohibited. Accordingly, a monopolist is entitled to increase its prices and reduce the quality or level of its services without contravening Part IV of the TPA.

More specifically, it is only unlawful for a firm with market power to deny access (refuse to supply a service or impose onerous terms on the provision of the service) if its **purpose** is to deter or harm competition in a market. As explained above, Qantas has experienced a range of circumstances in which an airport may refuse to supply a service, but its purpose is not directly to harm competition; rather, competitive damage is a consequence or effect of the airport's conduct given its monopoly position.

The Issues Paper questions whether Part IV of the TPA could be amended to address access problems. For example, the Paper questions whether the test under section 46 of the TPA could be amended from a 'purpose' test to an 'effects' test. In Qantas' view, amending section 46 of the TPA to address access issues raises more problems than it solves.

Section 46 applies to a broad range of firms which have 'substantial market power'. In general, significant access issues only arise in a much smaller range of firms: those that exhibit natural monopoly and

bottleneck characteristics. Accordingly, it would be undesirable to amend a competition provision which has generalised application in order to deal with a problem that exists in only a narrower category of firms.

In addition, section 46 is only enforceable in the Federal Court of Australia. Access issues involve complex and interrelated commercial and economic issues. As a general observation, the Federal Court is not well equipped to make determinations and assessments on a number of the issues arising from an access dispute, particularly pricing. This was noted in the Hilmer Report and was the primary reason for the formulation of Part IIIA.

Price Regulation

The Issues Paper questions whether, in the context of a non-vertically integrated essential facility, access issues can be addressed solely by price regulation.

As discussed earlier, the assumption underlying this question appears to be that non-vertically integrated firms always have an incentive to provide access. Qantas submits that in the context of airports, this assumption is incorrect, as:

- airports currently exhibit degrees of vertical integration;
- airports may increase their vertical integration over time; and
- even in the absence of vertical integration, there are a number of circumstances in which airports may seek to deny access.

Accordingly, Qantas submits that access problems do arise at airports.

That being the case, price regulation alone is unable to address the access problem that arises for the following reasons:

1. Price regulation does not deliver access. For example, if an airport does not wish to address congestion issues (and prefers a 'quiet life'), or alternatively is denying access to obtain a collateral benefit, price regulation will not further encourage or require the airport to provide access.

2. Price regulation often cannot address the non-price terms and conditions on which access is provided. For example, service standards, onerous terms and conditions or, where land or facilities are to be provided, the location of the land or facilities within the airport. Qantas recognises that a desirable aim of price regulation is to take account of non-price terms and conditions, including the quality of delivered services. Indeed, the current *Prices Surveillance Act* regulation of airports endeavours to take account of service quality levels. However, that regulation cannot impose contractual non-price terms and conditions between the airport and users of airport services. This is an inherent weakness in price regulation. (It is also unclear exactly how the quality of service issues are to be taken into account by the ACCC – certainly the ACCC has no power to force airports to reduce prices in the event of a quality reduction.)

3. The effectiveness of price regulation is to some extent dependent on the form of regulation, and the services covered by the regulation. For example, the current price regulation of airports is undertaken by way of a price cap over a bundle of airport services. Within the price cap, airports are free to alter prices charged for individual services. Accordingly, there is potential for airports to discriminate between users of services or to structure prices inefficiently across different user groups. This problem can only be addressed through an access regime that allows individual negotiation and arbitration of price for specific services.

Nevertheless, Qantas does believe that price regulation should exist beside access regulation. This is because general price regulation will set the pricing regime for services provided for all, or a significant portion, of the airport. Complementary access legislation allows arbitration in respect of access or terms and conditions (including pricing) of access to specific services at the airport.

Improving the Access Regime for Airports

The National Access Regime is relatively new. Even more recent has been the privatisation of most Australian airports, and the enactment of section 192 of the *Airports Act*. To date, there has been very little airport activity under the National Access Regime. The activity has been confined to:

- the preparation of draft access undertakings by Melbourne and Perth airports, on which airlines provided comments to the ACCC – the undertakings were not accepted by the ACCC in the form lodged; and
- the ACCC considered whether the use of an access road at Melbourne Airport by a car rental company to drop off and pick up passengers was an airport service within the meaning of section 192.

Accordingly, there is very little direct evidence about the effectiveness of the current National Access Regime as it applies to airports. This may be a direct result of the fact the airports took the existence of the regime, and the ability of airport users to utilise the regime, into account in their commercial negotiations.

In these circumstances, Qantas submits that it would be unwise to make substantial alterations to the National Access Regime. The commercial relationship between airports and airport users is continuing to develop in a post-privatisation environment. As stated above, Qantas believes that the existence of the Access Regime provides an important counterbalance to the monopoly power possessed by airports and enables airlines to enter into realistic commercial discussions with airports. To date, there is no evidence that the National Access Regime has imposed unnecessary costs on airports or is acting as a disincentive to investment.

Nevertheless, Qantas submits that a number of small amendments to the National Access Regime, as it applies to airports, would be desirable in the areas of:

- declaration criteria; and
- access undertakings.

Declaration Criteria

Qantas submits that the declaration criteria contained in Part IIIA of the TPA are appropriate in addressing the economic problems of essential facilities. At this time, Qantas does not believe there is any evidence that the declaration criteria are inappropriate.

However, it is also apparent that the declaration criteria applies to many services provided by airports in that:

- the service is used for the purposes of participation in upstream or downstream markets and access will therefore promote competition in upstream or downstream markets;
- the service must be provided at the airport location and it is not economic to duplicate most Australian airports; and
- the airport facility has national significance.

While the application of the declaration criteria is relatively straightforward to a large range of airport services, the procedural requirements under Part IIIA to demonstrate the criteria in each access application is burdensome and time consuming. The decision by the Australian Competition Tribunal in March 2000 to declare specific services at Sydney International Airport was made approximately 32 months after an application for access to the services was first made to the National Competition Council.

In Qantas' view, it is both unnecessary and administratively inefficient to demonstrate the applicability of the declaration criteria each time an access application is made in respect of an airport. It is for that reason that the Federal Government enacted section 192 of the *Airports Act*. As the Productivity Commission is aware, section 192 deems each airport service to be a declared service for the purposes of Part IIIA.

Section 192 does not completely remove inefficiency from the administrative process, but it does improve it greatly. To determine whether a particular airport service is declared, it is still necessary to determine whether the service falls within the definition of 'airport service' in section 192(5). This definition removes the 'national significance' criterion, as it is apparent that this criterion is satisfied in respect of the regulated airports. The definition also replaces the 'promote competition' criteria with the following criteria:

> *'Is the service necessary for the purposes of operating and/or maintaining civil aviation services at the airport'.*

The definition essentially maintains the 'uneconomic to duplicate' criteria.

Although the enactment of section 192 is a logical and practical step in the administration of airport access, Qantas believes that a number of further improvements can be made to the section.

1. The 'necessary for civil aviation services' criteria is a useful replacement for the 'promote competition' criteria. It is apparent that if the service is used in providing civil aviation services, access to the service will promote competition in the civil aviation market. However, difficulties arise with the use of the word 'necessary'. There are many services used at the airport which it could be argued are not physically necessary for the provision of civil aviation services but which are commercially or competitively necessary. If those services were not provided, the civil aviation industry would be substantially diminished in terms of the quality of services offered.

   Qantas submits that the word 'necessary' should be replaced by the word 'used'. In other words, provided the service is used for the purposes of civil aviation services, it should come within the access regime (subject to satisfying the uneconomic to duplicate criteria). This amendment more accurately reflects the aims of the 'promote competition' criteria. The access regime, in the context of the civil aviation industry, should be directed towards the enhancement and quality of civil aviation services provided by competing airlines.

2. Section 192 ought to apply to all core regulated airports immediately, and not merely on their privatisation. The most significant omission from section 192 is Sydney Airport. As a result, Sydney Airport has been acting in a materially monopolistic fashion in the lead-up to its privatisation.

   Qantas believes that the application of the access regime, and particularly the application of section 192 to Sydney Airport, should not be dependent on privatisation. In Qantas' view there is no policy justification for subjecting Sydney Airport to Part IIIA, but not section 192.

Access Undertakings

Qantas believes that the role of access undertakings in the National Access Regime is desirable. In the context of airports, it enables the airport operator to put forward the basis on which airport users are able to negotiate and agree access terms and conditions.

Qantas is aware that some airports have criticised the provisions relating to access undertakings, and the ACCC's interpretation of those provisions. Two main criticisms appear to be made:

1. that airport operators are unable to lodge access undertakings once section 192 has become effective (and airport services as defined in section 192(5) are declared); and
2. that the ACCC has adopted an overly interventionist or heavy handed approach to the acceptance of access undertakings.

In relation to the first criticism, Qantas is aware that this question is relevant to many industries, not just airports. Furthermore, Qantas accepts that it may be desirable from a policy perspective to enable essential facility operators to offer access undertakings even after a service has been declared. Clearly, the advantage of access undertakings is that they may provide a general framework under which access can be provided to all access seekers and resolve congestion and scheduling issues in a fair manner between access seekers. Accordingly, declaration (or the application of section 192) should not be a bar to offering access undertakings – provided they are in terms acceptable to the principal users of the services.

In relation to the second criticism, Qantas believes the criticism is unjustified. The draft determinations of the ACCC in respect of both Melbourne and Perth Airports' access undertakings are available for review by the Productivity Commission. The Melbourne Airport access undertaking was rejected by the ACCC for a number of reasons including:

- the terms of the undertaking were vague, which meant that it would be difficult for the Federal Court to enforce it;
- the undertaking provided little guidance to the determination of prices, stating that maximum prices would merely be negotiated between Melbourne Airport and users to reflect 'a level of charges that recognises the value of access to the user for its particular business'; and
- the undertaking contained little indication of service standards or non-price terms and conditions, which meant that negotiation would be difficult.

Similar concerns arose in respect of the Perth Airport access undertaking.

It appeared to Qantas that the airports commenced the process of preparing access undertakings only shortly before section 192 commenced operation. Accordingly, their time frame for discussing and negotiating the access undertakings with both the ACCC and users was very limited. This was unfortunate, and in Qantas' view led to a predictable outcome. If the National Access Regime was amended to allow airports to offer access undertakings at any time, this problem may be overcome.

Qantas believes that the ACCC's approach to the draft undertakings was correct. Undertakings can provide a beneficial framework within which the monopolist can negotiate commercial arrangements with facility users. However, they also have the effect of overriding or replacing statutory rights under the National Access Regime. Accordingly, they should only be accepted by the ACCC where it is clear that the rights of users are protected to the same extent as the statutory rights. The primary focus of the undertaking should be on producing principles and procedures of access more directly relevant to the airport industry, but without taking away rights.

Conclusion

Airports are natural monopolies and airlines do not possess countervailing power in respect of the use of airport services. Airports:

- represent bottlenecks or essential facilities (in the sense that they supply services that are essential inputs for the provision of aviation services); and
- are nationally significant infrastructure assets.

In Qantas' experience, access problems do arise at airports. These problems take one of two forms: either access is denied or frustrated or access is provided on unreasonable commercial terms (both price and non-price). There are a number of reasons why an airport may deny or frustrate access including to gain a commercial advantage in other areas of its business or because the airport holds a degree of vertical integration or is contemplating vertical integration. Airports therefore have the ability and potential to damage competition in upstream and downstream markets.

The consequences of these access problems are significant from an efficiency and public interest perspective. The efficiency and quality of airport services will impact directly on the efficiency and quality of Australia's transportation system and the markets which rely on that transportation system.

The problems that arise from the monopoly power of airports can only be addressed through a regulatory framework which addresses both pricing and access issues, and which recognises the interlinked nature of the problems. Qantas would not support any lessening of the existing regime for airports regulation. However Qantas believes some amendments to the National Access Regime, as it applies to airports, would be desirable including broadening the definition of 'airport service' under section 192 of the *Airports Act*, declaring Sydney Airport under section 192 and allowing airports to offer access undertakings under Part IIIA of the TPA at any time.