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Productivity Commission

PRODUCTIVITY COMMISSION

INQUIRY INTO ECONOMIC REGULATION OF AIRPORT SERVICES

DR W. CRAIK, Presiding Commissioner
MR J. SUTTON, Associate Commissioner

TRANSCRIPT OF PROCEEDINGS

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DR CRAIK: Good morning and welcome to the public hearings of the Productivity Commission public inquiry into the economic regulation of airport services. These hearings follow the release of the draft report in early August this year. My name is Wendy Craik and I'm the presiding commissioner in this inquiry and I'm joined by my associate commissioner, John Sutton.

The purpose of this round of hearings is to facilitate public scrutiny of the commission's work and to get comment and feedback on the draft report. Following these hearings today and tomorrow, we will then be working towards completing a final report for the government in December this year, having considered all the evidence presented at the hearings and in submissions as well as other informal discussions. Participants in the inquiry will automatically receive a copy of the final report once released by government, which may be up to 25 parliamentary sitting days after completion.

We like to conduct all hearings in a reasonably informal manner, but I remind participants that a full transcript is being taken. For this reason comments from the floor cannot be taken, but at the end of the proceedings for the day I'll provide an opportunity for any persons wishing to do so to make a brief presentation. Participants are not required to take an oath but should be truthful in their remarks. Participants are welcome to comment on the issues raised in other submissions. Transcripts will be made available to participants and will be available from the commission's web site following the hearings. Submissions are also available on the web site. Is there any media here today? Okay.

To comply with the requirement of the Occupational Health and Safety legislation and commonsense, you're advised that in the unlikely event of a fire or an emergency requiring the evacuation of this building you should follow the green exit signs to the nearest stairwell. Lifts are not to be used. Which means you got out that door and turn left and there's a green exit sign there. Please follow the instructions of floor wardens at all times. If you believe you would be unable to walk down the stairs, it is important you advise the wardens who will make alternative arrangements. Unless otherwise advised, the assembly point for today is the Suncorp Plaza at 447 Collins Street which is between William and Queen Streets.

So first up we have Virgin Australia and could I ask you to state your names and positions for the record and then invite you to make a brief opening statement. Thank you.

MR DONOHUE (VA): Good morning, commissioners. My name is Sean Donohue. I'm the group executive of operations for Virgin Australia. Appearing with me today is Leigh Balderson, manager of airports planning and pricing at Virgin Australia and Simon Snow, from Gilbert and Tobin, who is helping us out with the submission. As the commission is aware, Virgin Australia has lodged

written submissions setting out its comments in relation to the issues raised in the commission's issues paper and draft report. My objective today is to provide the commission with a summary of Virgin Australia's position in relation to the economic regulation of airport services.

Virgin Australia's position is quite simple: major airports in Australia are natural monopolies and there are no effective substitutes for their services. Monopolists without some form of constraint will act to increase prices above efficient levels, reduce the quality of the services they offer or both. Virgin Australia does not see any reason why major airports would act any differently from other monopolists. Under the current regime Virgin Australia does not consider there are any effective constraints on the monopoly powers of major airports. The regime is wholly ineffective in this regard.

There is an argument there are constraints on airports such as the threat of re-regulation, airlines having countervailing power or non-aeronautical revenue. We don't believe these factors constrain airports at all. Virgin Australia also does not consider the current price monitoring regime and the declaration provisions to be effective. We have had first-hand experience with the declaration process. It is ineffective due to the time, cost and inherent uncertainty associated with it. In the absence of an effective constraint on their monopoly power it is our view that major airports will continue to increase their charges above efficient levels and set terms and conditions for the use of their infrastructure that would not prevail in a competitive market.

Virgin Australia believes its passengers do not have any real sense of the prices that they are indirectly paying for airport use. Charges have been increasing steadily and with the significant investment program being planned by major airports over the next 10 years and without any effective constraints on these airports, this trend will continue. The effect of this will be that air fares will increase and since a large number of passengers that fly are price sensitive, fewer people will be able to take advantage of air travel.

It is important to Virgin Australia that its passengers understand the drivers for increases in fares. In the past when fuel prices have risen significantly, Virgin Australia has been forced to increase its fares through the imposition of fuel surcharges and we communicated the reasons for these increases to our passengers. We are now at a point where Virgin Australia is giving considerable thought to how it can make airport charges more transparent to the travelling public so that they can see how much they're paying for airports and how those amounts increase over time. In its draft report the commission emphasised that one of the key goals of the monitoring regime is for airlines and airports to negotiate access terms and conditions commercially. While Virgin Australia certainly considers that the commercial negotiations have many advantages when compared to a price control

environment, they should not be seen as an end to themselves.

In relation to negotiations with airports, Virgin Australia's experience is that negotiations are extremely protracted and suffer from a lack of transparency. Airports will, on occasion, adopt an inflexible approach to negotiations and increasingly, airports simply impose prices significantly above efficient costs. Our experience is that airports are prone to manipulate financial inputs and pricing models to achieve pre-determined returns. This is not in the interest of the airline or its passengers. Ideally we would like to see airlines and airports negotiating in the same way that they would in a competitive market. However, without an effective constraint on airports' market power, this simply will not happen.

The charges now comprise a very large proportion of air fares. At the same time the quality of the services at a number of airports has continued to fall despite rising revenues. Airports often seek to justify their high rates of return on the basis that it is appropriate for the high level of risk they face. However, recent experience with the global financial crisis was instructive. When demand for air travel dropped, it was the airlines that responded by discounting air fares to stimulate demand. Airports, on the other hand, maintained their charges at the same levels and benefited from steady passenger numbers. This clearly shows that airports claimed level of risks are significantly inflated and as a consequence their rates of return have therefore been excessive in this respect alone.

Airport charges are a very significant part of Virgin Australia's cost base. As such aeronautical charges make up a significant proportion of our fares as set out in the confidential written material provided to the commission. Virgin Australia does not agree with the finding in the draft report that they are a low proportion of air fares. Increases in airport charges have a significant impact on Virgin Australia's operation and Virgin Australia's fares are higher than they would be without these increases. Increased airport charges cannot therefore be dismissed as merely rent transfers between airports and airlines.

Going forward Virgin Australia believes that the commission should recommend a regulatory regime that will prevent airports from raising charges significantly above efficient levels, while also retaining maximum flexibility to allow airports and airlines to negotiate and agree on efficient and competitive terms and conditions for the use of the airports' facilities. Virgin Australia considers that a negotiate-arbitrate model of the sort detailed in its submissions would meet this criteria. Such a model should allow parties to have disputes resolved by an independent expert arbitrator.

Given the issues involved, Virgin Australia considers that the ACCC is best positioned to perform this role due to general experience in conducting arbitrations and specialised experience in relation to aeronautical services. In order to facilitate

commercial negotiations, the ACCC should issue pricing and costing guidelines as detailed in Virgin Australia's original submission. Further, parties will be most likely to negotiate commercially where there is transparency of information. For this reason the price monitoring regime should be retained and improved. Given clear pricing and costing guidelines and transparent cost information, there is no reason to fear that airports and airlines will automatically resort to arbitration in preference to commercial negotiation. Arbitration is costly and there is little to be gained from the process if there is reasonable certainty as to the outcome. It is worth remembering that a number of airport services have been declared to date without any party yet resorting to arbitration and other industries have had similar experiences with a negotiate-arbitrate model.

A show cause mechanism was considered following the last review by the Productivity Commission and failed to attract any support from any section of the industry. As set out in our submission we do not believe that the proposed show cause mechanism would in any way be effective to constrain airports from abusing their monopoly power.

In conclusion, Virgin Australia's position is simple: airports are monopolies, this is undisputed. Australia is not in the same position as the US and Europe where I know from experience that cities are invariably served by competing primary and secondary airports. In Australia there are no effective substitutes to the major airports. The current regime does not facilitate commercial outcomes due to the inherent imbalance in negotiating power between airports and airlines. As a result, airports' returns are well above that commensurate with the regulatory and commercial risks involved and there are no incentives to reduce costs or otherwise improve productivity. These increased charges have had and will continue to have a negative impact on the travelling public through increased fares and reduced investment by airlines.

As mentioned earlier, we do not believe that the passengers fully understand how much airports are charging and we are seriously looking at how we can increase the transparency of these charges to those who ultimately bear the costs. In a competitive market parties negotiate terms and conditions commercially. It is important to note that dealing with airports is only one aspect of our business. There are multiple other facets of running an airline where we engage in successful commercial negotiations on a regular basis. As such, there should be no concern on the part of the commission that a negotiate-arbitrate regime would detract from commercial negotiation. All of the experience to date with declared airport services shows that parties have strong incentives to negotiate commercially.

The commission itself acknowledges that the current regime needs a credible threat. For the reasons we have outlined above, and in our written submissions, the show cause mechanism will not provide the solution to the problem. As such we

urge the commission to reconsider the benefits of the negotiate-arbitrate model to allow airlines and airports to negotiate the same way they would in competitive market. We would be glad to take any questions that the commissioners have.

DR CRAIK: Thank you. Thanks very much for the comments. So effectively are you suggesting that what's needed is deemed declaration airports so that there's a negotiate-arbitrate position? Is that what you're actually seeking, re-regulation in fact. Is that what you're after because it's - - -

MR SNOW (VA): We wouldn't see it as re-regulation and it's certainly not going back to a regulation, as it was previously. Deemed declaration is one way to introduce obviously an negotiate-arbitrate model. We've set out in our submissions what we think the key features are. As to how the best way to achieve that is, we're open to discussions about the best way to achieve that. One way certainly would be to have deemed declaration, but it's not necessarily the only way.

DR CRAIK: So what other ways might be better?

MR SNOW (VA): You could simply introduce separate legislation that might introduce a negotiate-arbitrate model for airport services as defined. I mean, there are a number of different ways you could go about doing it. Certainly, under the current legislation, such as the Competition and Consumer Act, the easy shorthand way to get there and have the ACCC as the arbitrator would be to deem them declared but it's not necessarily the only way.

DR CRAIK: Okay. But effectively, I suppose, it's no longer light-handed regulation, is it? I suppose it's what would be normally called heavy-handed regulation.

MR SNOW (VA): No, I don't think we would agree with that. We would see it has light-handed regulation because it's not something which actually regulates the prices which an airport can charge and it puts forward as the primary way in which charges are determined as commercial negotiation. In fact, from experience, when declarations have occurred there has been very little, if any, resort to regulation or to the arbiter, it's all been done through commercial negotiation. So we wouldn't see it as heavy-handed regulation at all.

DR CRAIK: Okay. Why didn't you pursue seeking redeclaration of Sydney Airport airside services after the declaration expired at the end of 2010 if you found it such an effective mechanism?

MS BALDERSON (VA): The reason for that was mainly that to do that we would have to go through the whole declaration process again and after our first experience with the declaration process which, as Sean has outlined, it was costly, it's time

consuming, it has inherent uncertainty and since the declaration there have also been some changes to the statutory test which, in our view, may even make it more difficult to get certain airport services declared, so that's why that decision has been made.

DR CRAIK: Okay. The new timing processes and things for declaration would have made the timing shorter, wouldn't it?

MS BALDERSON (VA): Not necessarily because it goes through, as we experienced with the declaration that we were involved - there are so many different processes and avenues of appeal, and that one went all the way to seek leave to appeal to the High Court. All of that is still a time-consuming process.

MR SNOW (VA): I think there are five separate decision-makers potentially involved and although there are some time limits, in each case those time frames - there's abilities to stop the clock, if you like, and do other things so it doesn't give you any guarantee and the time limits only apply to the first two or three decision-makers, not to later decision-makers as well. So whilst it might be an improvement from a timing perspective, maybe it wouldn't take four to five years, you would still be looking at a number of years.

DR CRAIK: I'm interested on your comments on our show cause mechanism. Our view was that would apply to individual airports and a possible outcome at the end of a price VHA inquiry is a recommendation for declaration or for deemed declaration or for price capping or for price setting or whatever so that there would be a range of options, depending on what the recommendation was at the end of a show cause which would be brought into play if a single airport went through that whole process and to the satisfaction of the ACCC demonstrated abuse of market power. The question I think we would be interested in is why would that not be a satisfactory way to go unless you think all airports fall into the category of abusing market power.

MR SNOW (VA): There are a number of issues that Virgin Australia has with the show cause mechanism. Firstly, the real concern is it only kicks in after a number of years. It's not actually a useful feature to assist with negotiations with an airport. It's only very much after a period of persistent behaviour that is seen to be of excessive prices that the ACCC would then be able to form a view that an inquiry should be held. An inquiry would then need to be held and then there would need to be a recommendation and then it's quite uncertain as to what the outcome of that would be politically or if there was to be, for instance, a reintroduction of price capping, that's actually not something that either the airports or the airlines want. So the outcomes aren't necessarily what is wanted.

The process again is a very lengthy one. So if you take from the time that an

airport engaged in unacceptable behaviour, that wouldn't become apparent until it lodged its accounts for the price monitoring regime with the ACCC, so there is up to 12 or 15 months there. It would have to happen in more than one year, so you would have to wait another 12 months. The ACCC would then have to make a decision as to whether it had met the hurdle and we think the hurdle is actually quite a high one to meet and only relates to price, not non-price terms as well.

DR CRAIK: It relates to quality of service as well.

MR SNOW (VA): It wasn't clear in terms of the show cause. I think the inquiry can cover those things but it wasn't clear to us on the draft report that the trigger for it was more looking at excessive returns over a period.

DR CRAIK: Excessive returns taking into account quality of service.

MR SNOW (VA): Right. Obviously tricky in relation to negotiation tactics and things like that. So it's some years before the inquiry would be held and then obviously the inquiry would take some time and then there would be decision-making after that. So, again, a number of year, a very long time and not one with any certainty of outcome.

DR CRAIK: So there is a history of monitoring information that could be used from - - -

MR SNOW (VA): Potentially there is but, again, it would be something that would be, we think, a number of years before there would be any outcome.

DR CRAIK: Okay.

MR DONOHUE (VA): Regardless of whatever mechanism, what we're really trying to get to is a point that there is a level playing field. When we negotiate with airports right now, the balance of power is absolutely with the airports and, you know, coming from a perspective of working in the US airline for 25 years and the industry, if we wanted to fly into New York city, for example, we had three airports to choose from and if one airport was raising its rates and was more expensive, we had two other airports that we could go to. The same in Chicago, the same in Los Angeles, the same in San Francisco. So there was some balance of power there, there was some balance of being able to negotiate competitively and we absolutely support continued commercial negotiations.

We're not going back to asking for full regulation but there does need to be a mechanism in our opinion that it is a level playing field, that there is some competitive tension so that you can get to a commercial solution that is satisfactory to both parties. Right now it is wholly one sided in our opinion.

DR CRAIK: We understand that sometimes airlines, if they can't agree the new charges, just keep paying the old charges until they reach agreement on the new charges so that in a sense, even though airports wish to have a new charged imposed, we understand airlines will often keep paying for quite some time and the difference there gets written off. That is the sort of information that we've had in a general sense from airports which suggests that airlines aren't totally without some responsive power.

MS BALDERSON (VA): I certainly wouldn't say that that has any impact on the negotiation at all from my experience and secondly, it never gets written off. When there's an agreement it certainly comes back to the date that the airport wants the renewal back to kick in. In the number of negotiations I've done, even if we've done that, it certainly hasn't influenced the positioning of the airports, it certainly hasn't changed their inflexibility towards us and quite often then it resorts to other tactics which are just not conducive to a swift commercial outcome.

DR CRAIK: Your comment about advising passengers of the quantum of the airport charge in air fares, why haven't you just done that if it is such an issue? It seems not an unreasonable thing, to me, to do.

MR DONOHUE (VA): Having just joined Virgin in the last 10 months and going through this process it's something that I've asked the team to put on the table and it's something that we intend to do. We think transparency is - there is a lot of value to transparency. The fact that airport terminal and aeronautical fees now are our third-largest expense in the company and growing at a faster rate than most other expenses, we think customers should know that and I think you will see us aggressively move into that space.

DR CRAIK: Fuel surcharges have been really transparent.

MR DONOHUE (VA): Absolutely.

DR CRAIK: It seem to me there is no reason why the others wouldn't be.

MR DONOHUE (VA): Same analogy.

DR CRAIK: Although, I suppose as a passenger it's a bit irritating to see 46 charges down the bottom of the ticket. Just one more question, airlines claim that airport charges are a very high cost impost on them and unreasonable but if you read all the airlines' annual reports and the speeches that CEOs make in the public arena when they're talking about issues affecting airlines, airport charges, to our knowledge, never come up, never are mentioned, other issues seem to be much more important and yet that's not the impression we get from the submissions.

MR DONOHUE (VA): I think you'll see that changing with Virgin moving forward based upon this whole transparency issue and again, we've got to be careful that we obviously support transparency but we don't want to go overboard and sound like we're whingeing to our customers. We have a business to run, it's our responsibility to run that financially as strong as possible. But to the analogy we made in my remarks and that you just discussed, similar to fuel prices we do see there is an opportunity to educate the public more on this issue.

DR CRAIK: Just before I had over to John, one other question. Did you see the new chairman of the ACCC's comments on airports the other day about monopolies and regulation.

MS BALDERSON (VA): Yes, we did.

DR CRAIK: Do you have a view?

MS BALDERSON (VA): I think we'd say we support the ACCC's comments. Having been involved in this process a few times, it's interesting to see - and we've been advocating the same model for quite a while - that the commission, and we're pleased to see the commission, has come to similar view to airlines.

DR CRAIK: Thanks. John.

MR SUTTON: You have strong views about the shortcomings of the current regime in Australia. Is that a uniform problem across all the airports or really do you have in mind particular airports where the problem is acute in your view.

MS BALDERSON (VA): We experience problems across the majority of airports, but where it's most concerning to us, as we've outlined in our written submissions, is what we've called tier 1 and tier 2 airports and we've defined those in our written submissions, they're our biggest concerns.

MR SUTTON: But even in tier 1, in the five monitored airports, do you say the problem is the same across the five? It's just identical. You've got these very serious problems with all of those five airports?

MS BALDERSON (VA): We experience problems in negotiations across all the airports that we negotiate with.

MR SUTTON: A view that you aired quite a bit today and I've read it elsewhere from you is that you have a very firm view that prices are above or exceed efficient levels at least the monitored airports. Why do you come to that conclusion and what are you basing your views on? I'd very much be interested in that kind of analytical

material, if you do have it.

MS BALDERSON (VA): We are certainly basing our views on - as you would be aware, in the negotiation process there is financial modelling that we do receive, particularly from the tier 1 - not always from all airports, but from the tier 1 airports. So it is based on the parameters that the airports are using to explain their cost increases. I think we've given some materials on this in our written submission but if there are any specifics you are interested in, it's something we're happy to provide you extra material on if it's useful to the commission.

MR SUTTON: Yes. The commission, in our draft report, spent a whole chapter trying to grapple with this rather complex issue and we see there are lots of shades of grey around this area and it's very hard to be definitive. You have a very firm view, so I think it would very much assist us. I'm definitely interested in - if you can furnish material to prove the case.

MR DONOHUE (VA): We will absolutely provide you - - -

MS BALDERSON (VA): We would certainly be pleased to do that.

MR SUTTON: You are asserting a very strong position on this. That is important material.

MS BALDERSON (VA): We would be pleased to do that for you.

DR CRAIK: Do you have particular views about airport investment? Is it too little, too much, about right? If there's gold plating - do you think gold plating goes on with investment and would more information in negotiations help? Can you give examples of gold plating?

MR DONOHUE (VA): I will let Leigh comment. I would not say I have seen gold plating, especially given my experience in the US and what I've seen in Europe. I do worry about those specifically, for example, the cost of the second runway in Brisbane at nearly one and a half billion dollars you could build a new airport for the cost of what that second runway is costing. I'm not saying it's a gold-plated runway, but when you have situations like that, I'm not sure there's an airport in the world that has ever been built that has cost more than one and a half billion dollars and this is a runway that is costing that amount of money. So it's those type of issues that are worrisome.

DR CRAIK: Do you say it's an unreasonable amount or it's gold plated or what do you say?

MR DONOHUE (VA): A nearly one and a half billion cost for a second runway is

absolutely unreasonable.

DR CRAIK: Is it too long, too big, too what?

MR DONOHUE (VA): Again, I think it's reflective of the situation in Brisbane and not a lot of opportunity, not a lot of alternatives, but that type of cost, pre-funding of the runway in terms of the cost it would impose on airlines, it's issues like that that we wholly disagree with.

DR CRAIK: So how do you think the runway should be paid for, if not pre-funding?

MR DONOHUE (VA): I look at other infrastructure projects in the country, be it a tunnel or a toll road and the users pay for that after it's open. Users don't pay for it on a pre-funding basis, to the best of my knowledge. That seems to be a pretty effective model, in our opinion.

DR CRAIK: But there's been quite a history, hasn't there, of airport charges being imposed so new investment could occur at airports, a pre-funding model.

MS BALDERSON (VA): In the time that I've been in this role, it is certainly a position Virgin has taken, is that we don't support pre-funding.

DR CRAIK: There's no doubt in the modelling, some of the financing aspects are put into costs and we certainly support assisting with the financing aspect of it until the asset is available for use, and I think we're outlined that proposal as our suggested methodology in our written submissions.

MS BALDERSON (VA): Okay.

DR CRAIK: So is there a difference between over-investment for the purposes of Virgin Airlines, as opposed to the airport as a whole? Is that part of the problem, that airports have to invest for the airport as a whole for a whole range of airlines, not just Virgin, compared with what Virgin actually wants to see? Is that part of the problem?

MR DONOHUE (VA): Again, I'll let Leigh comment. If you look at Sydney Airport, for example, when the improvements to the airport were made to allow the operation of the A380, we wound up paying for a piece of that. We didn't get any benefit from it, but we wound up paying for a piece of it. I don't have an issue with that in particular, because that's pretty typical, I think, in airports throughout the world. So we understand that for major projects, there are examples where we get, at best, an indirect benefit, and, Leigh, you can add on. Examples like that, I think, again, we can work through on a commercial basis. I go back, though, to the

Brisbane example. Clearly there is benefit to improve the operational efficiency of Brisbane Airport. The cost-benefit return on that investment just doesn't make sense to us.

DR CRAIK: Thanks.

MR SUTTON: Just on the show cause proposition that we advance, you make the comment that this was floated in 2006 and there was no interest by anybody in the 2006 approach, or words to that effect. Let me put to you that in fact the government was quite interested in moving forward with a show cause mechanism, but it coincided with that moment when the GFC hit and really I believe that was a key reason why it was put on the shelf at that point in time. So at least the government thought that it had legs at that time and hopefully they might think it's got legs again, but I just wanted to make that observation. Comment on it if you wish, whether you agree or disagree.

DR CRAIK: It was also quite a different show cause from - - -

MR SUTTON: It was. The mechanism was different, yes.

DR CRAIK: - - - the one we're proposing.

MR SUTTON: Let me move on. We are inviting participants in one of our information requests to provide suggestions to assist the monitoring process, because you make observations that some of the current judgments of the ACCC are incomplete and they don't have adequate information on which to take issues forward. We invite people, well-placed stakeholders like your company, to make suggestions about what additional financial information, additional material that they might use, so I'd hope you would pick up that information request and make suggestions about additional material.

MS BALDERSON (VA): We certainly did make suggestions in our written submissions in that regard.

MR SNOW (VA): Yes. We have commented on that exact issue in our response to the draft report, which I think should be going up on your web site shortly. So that does have comments in that regard, but if there's anything further that you would like to add, we certainly will do so.

MR SUTTON: That's currently a confidential submission and - - -

MR SNOW (VA): Correct, and the public version, we understand, should be with you very soon.

MR SUTTON: Thank you.

DR CRAIK: Do you think the passenger surveys are reliable? Do you think they're useful, reliable surveys?

MS BALDERSON (VA): I guess what the passenger comments on, I think it is a little bit unreliable in the sense that the passenger doesn't necessarily always associate things with the airport. It can often associate it with falling within the experience with an airline, so I'm not sure that we would say they're always very reliable.

DR CRAIK: Does the passenger actually care, do you think, whether it's the airline or the airport? It's just whether they get a good service, isn't it, through the whole process?

MS BALDERSON (VA): True. Yes, certainly.

MR DONOHUE (VA): To Leigh's point, it's our view, based upon the research we do with customers, that if there is an issue during the process of check-in or security or whatever event through the airport, they view it as a Virgin Australia experience. They don't view it as Sydney Airport or Melbourne Airport. That's what all the data shows us. From the time they buy the ticket until they get home, in totality they see that as a Virgin Australia experience.

DR CRAIK: Do you have a view about using service level agreements to replace airline surveys?

MR DONOHUE (VA): We absolutely support SLAs. We have them throughout our business. As long as there's accountability on both sides, then, in my opinion and from what I've seen in Virgin, they work quite well. Again, if you have an SLA where - I keep going back to a level playing field - there is not a level playing field and one party bears all the accountability, then they are obviously less effective.

DR CRAIK: Would you support, though, using the performance rate of reaching the KPIs and service level agreements, publishing those as a substitute for airline surveys, I guess is what we're saying.

MS BALDERSON (VA): I certainly think that we would be happy to have that discussion. I think we would obviously like input into service levels and the KPIs that are published.

DR CRAIK: It wouldn't be the content we'd be publishing, so much as the actual achievement.

MS BALDERSON (VA): The achievement, yes. So we would happily have that discussion. The only other comment we would have is, in addition to if we had set KPIs, we would still want the flexibility to be able to negotiate specific service levels for specific airports.

DR CRAIK: No. We were saying the ones that were negotiated between the airline and the airport, not some predetermined thing.

MS BALDERSON (VA): I think that's something that would be really good that the industry talked about and reviewed, as opposed to having a definitive opinion one way or the other, but we would certainly be happy to look at it.

DR CRAIK: Thanks.

MR SUTTON: What do you think of the suggestion we've floated about additions to the pricing principles and/or key parties get together and try to nut out a voluntary code of conduct?

MS BALDERSON (VA): I think, in our view, adding it to the pricing principles I don't think will benefit - and I'm not sure if a voluntary code of conduct is of benefit. It's been our view that we think the ACCC, who has a lot of experience in this area, would be ideal to support issuing guidelines, but we would be certainly more than happy, if there was an industry forum to have a discussion on it, to participate.

MR SUTTON: On your key proposition about negotiate and arbitrate, you say that you would see the ACCC as being the arbitrator in that context. What do you think of something less than that position, such as the parties agree on the head of the Law Council or some esteemed private arbitrator being used. Of course the problem tends to be not when agreements are on foot because they tend to have dispute resolution mechanisms in them, it's the protracted negotiations around the new agreement. You have a preferred position of a fully-blown negotiated arbitrated model with the ACCC. What do you think of the lesser proposition that I've just advanced?

MS BALDERSON (VA): We support negotiated arbitration or any credible thing that's going to bring the balance of power and, as we've said, level the playing field. The reason the ACCC was selected is because quite often the modelling and detail that sits behind the discussions between airports and airlines is quite complex and the ACCC has experience in those types of modelling. It's a little bit unusual in that sense. It's not comparable to your traditional commercial agreement or, for example, in the construction industry where there's set arbitrators that are quite familiar with the industry and the issues at hand, but we certainly would be open to having a look at potential options; accounting firms are one. If you can find one that doesn't act for an airport or an airline or is impartial, then certainly we would support a different form of arbitration or arbitrator.

MR SUTTON: I'm sure the Chinese walls would fix that issue up.

DR CRAIK: One of the things we've been asking people who have been appearing at the hearing is the possibility of publishing the monitoring report with the airport's responses; they get a copy of the draft about their airport from the ACCC as they're preparing the monitoring report and publishing the airport's responses with the actual monitoring report itself. What would be your view of that?

MS BALDERSON (VA): I don't think we would have any issue with that occurring.

MR SNOW (VA): There could be scope for users to have comments as well perhaps.

DR CRAIK: One of the issues that's been raised by the airports in relation to our show cause proposal - a couple of the issues, I'd be interested in your feedback on. The airports are keen to see that as a confidential process. Do you have views about it being either public or confidential? I know even though you don't support the show cause, I'd be interested in your views about that.

MR DONOHUE (VA): Transparency. Again, we don't recommend it but if it happens, the more transparency the better.

DR CRAIK: Yes, I might have anticipated that. The other issue I'd be interested in your view in - and we raised it in our report and the airports have certainly raised it as well - is whether there's a problem with having the ACCC actually produce the monitoring report, make the show cause statement and then possibly recommending a VIIA inquiry and then the possibility of them actually conducting the inquiry. So having the ACCC, the same party, right through that whole chain now, do you have views about the appropriateness of that, should some other agency end up actually doing the inquiry or have some other role in part of that?

MR SNOW (VA): I don't think we see an issue with that. I don't think we have an issue with the identity of the ACCC. It's more the other aspects of the show cause that we have issues with.

DR CRAIK: You have a fundamental problem with the show cause, I understand.

MR SUTTON: The dual till, we do ask parties if they think that the non-aero revenues help constrain aero revenues and we have had an interesting variety of responses to that question from the airports. It appeals to my curiosity anyway to hear what Virgin has got to say about that.

MR SNOW (VA): This is an issue that was raised in the 2001 report I think and was examined in between and then the Productivity Commission itself found in 2006 it wasn't an effective constraint. It's also been examined by the Australian Competition Tribunal in the Full Federal Court in decisions as well. As we've set out in our submissions, although as a matter of economic theory it is a constraint at particular level, the level at which it kicks in as a potential constraint is where aeronautical charges, because of the relativities between the different revenues and how they're charged, it kicks in as a constraint when aeronautical charges increase by a factor of about 20. So in terms of would it be a constraint, yes, if aeronautical charges increased massively, at some point it would kick in then, but is it an effective constraint at any vaguely reasonable level of aeronautical charges, no.

DR CRAIK: Can I just ask one final question: while airside services at Sydney Airport were declared - did you actually have any other negotiations with Sydney Airport in relation to airside services while it was declared, other than the original - - -

MS BALDERSON (VA): Obviously that was the original issue - - -

DR CRAIK: Yes, the original one.

MS BALDERSON (VA): - - - which was actually resolved, but no, due to the time frame of the outcome of that - - -

DR CRAIK: That resolved it.

MS BALDERSON (VA): Correct.

MR SNOW (VA): And there are long-term agreements.

MS BALDERSON (VA): And they're long-term agreements so there's been reason to revisit that particular discussion since then.

DR CRAIK: Okay, thanks. Thank you very much for your comments. Thanks for your information and we look forward to having the submission publicly available.

MS BALDERSON (VA): No problem.

MR DONOHUE (VA): Thank you.

DR CRAIK: The next appearance is from Tim Anderson from Airport Link. Could you state your name and position for the record please and if you'd like to make a brief opening statement, we'd be happy to hear from you. Thank you.

MR ANDERSON (ALC): Thank you. My name is Tim Anderson. I'm the chief executive of Airport Link Co. As you know, our organisation works with the New South Wales government to provide rail connections between Sydney Airport and Sydney City and to another 301 stations in the Greater Sydney area and in this way we combine to provide more than 80,000 train connections through the airport link tunnel each year which assists in rail access for five million people going to and from the airport and another three and a half million people going to Mascot and Green Square.

I'm hopeful that my second submission of 21 September and my appearance today will assist the commission by shedding light on the matter of ground transport mode share and specifically for rail at Sydney Airport. I was interested because the draft report records the mode share of Sydney Airport Link as both 9 per cent and 11 per cent and that includes some of the statements on page XL, such as:

The rail service to the airport carries only 11 per cent of airport users.

On page 14, a pie graph indicated usage was 11 per cent; on page 163, a table records the rail mode share as 9 per cent, again on page 167 at 9 per cent and then on page 267 at 11 per cent. So I just thought with that in mind, it would be worthwhile and in the best interests of finalising the report if I could provide the commission with further insight.

DR CRAIK: Very helpful, thank you.

MR ANDERSON (ALC): Our calculation for the mode share for the last financial year was actually 13.78 per cent. In other words, during 2010-11 we experienced 4,945,000 people passing through our train arrangements at Sydney Airport domestic and Sydney Airport international stations. I know that in the same period, Sydney Airport recorded 35,000,885 passengers, so the ratio being 13.78 per cent. More recently, the commission may be interested to know that our mode share is consistently exceeding 14 per cent and our last recorded result for August 2011 was 14.27 per cent. I also record for your consideration that on three occasions this calendar year, our mode share at the Sydney Airport international terminal has exceeded 15 per cent of all people going through there on the train.

So when the draft report did report the figures at 9 per cent, that was 35 per cent below true-life results, and when at 11 per cent it was 20 per cent below. So I think it's just interesting to record that the discrepancy in my mind was too large so I made the second submission in that having a recorded mode share of 9 per cent it

actually underestimates real-life passengers by 1,715,000 people actually using the service.

It's slightly better when the report referred to 11 per cent mode share. That was 3,947,000 estimated passengers but it's still almost exactly one million to the number actually underestimating what we're actually achieving. So I do ask perhaps if the commission could consider my second submission today and perhaps, if you approve, record a mode share of 14 per cent in the final document. But I thought of more interest to the commission would be the projected and more recent modal trend. In my letter - and I have the line graph here if you are interested. I just pointed out in the letter that the report referred to the market share in this green box here whereas the ongoing trend is significantly above it and it's also quite solid and continuous. We hope that that trend, and we see no abating of the trend actually and are rather confident that a mode share in the order of 17 to 18 per cent of all passengers going through Sydney Airport could be on the train by 2015-16 and certainly much higher if we can achieve some further fare reform.

I should say as well that in the early years of Airport Link, just after the Olympics, the train was often ridiculed as the ghost train and so forth for some years, I'm sure you know, and it's been difficult to shrug off that tag and some of that mud still sticks actually. So I'm also hopeful that my submission of advising that five million people year and the market share might in some way start to change that perception. It's on that point that I also did feel that the expression of "low usage" to refer to Airport Link which occurred in the document is perhaps not the most accurate wording.

For instance, I again do point out that around five million people used rail to get to or from Sydney Airport last year. It's a lot of people. It's more than the entire population of Sydney or Melbourne and, as an example, I also record that around 15,000 people each day travel to or from Sydney Airport by train. Just last Friday we experienced, as a true-life example, 12,516 passengers going through our domestic train station and 6430 at our international station. So there were actually 18,946 people catching the train to or from Sydney Airport last Friday. So I do ask that the final report consider that it's not low usage.

In comparative terms we fill up - I mention in my letter - around 95 A320 aircraft each day and on an annual basis one could say that there is 27,900 A320s that we fill up from all those people coming in off the trains. So I do consider that the rail is well supporting Sydney airport's existing flight activities and, as I mentioned, perhaps we can achieve 18 per cent in the coming years and certainly I'm hopeful that that may be as many as one in five passengers using the airport going by train.

However, although I disagreed with the draft report's terminology of low usage to describe the airport line, I would agree that rail use to Sydney Airport remains

underutilised. I draw this conclusion because since our new management of Airport Link in 2008 we've revised and improved our marketing and our services and you, I think, would be aware, the company was in administration for something like six or seven years, a very long period of time, before it went under new ownership and since it's been under new ownership our patronage in just two years at the airport has increased by 25 per cent. So that says to me that we're carrying a lot of people but it also says to me that we can certainly do a lot more. So that's why I was more interested in providing the recommendation if the commission could consider adopting the term "remains under utilised" instead of "low patronage" in the final report.

But I also accept that pricing of tickets on the line has a part to play in utilising the infrastructure more fully and I do accept that fare reform could further rapidly increase rail mode share to the airport and our experiences with fare reform at Mascot and Green Square station over the last year or so have been very significant in increasing patronage and more recently, since the draft report came out, I've been on the public record saying that we would be prepared to participate in any fare reform for airport link in Sydney.

But beyond pricing I hold the view that the airport link is like all businesses and takes time to grow and expand and is expanding well and that's what's occurring and it's steady growth to a high and proper mode share continues. So that is all I'd like to say today and I'm hoping my comments in my second submission provide further insight.

DR CRAIK: Thanks very much, Tim, and that's for revising the report with such forensic analysis. Can I just point out that the data we put related to 2006 and it was from Sydney Airport's Grand Transport Plan and we know it's a bit out of date but it was the only data that covered all mode shares at one time and the 9 per cent referred to passengers and meeters and greeters and the 11 per cent referred to all users for 2006. So there was method in our madness but - - -

MR ANDERSON (ALC): I can appreciate that. I did recognise that. I just thought since then things have virtually moved on so it would be interesting to provide - - -

DR CRAIK: Yes.

MR ANDERSON (ALC): I think the complexity during administration it seems to me - I wasn't there - the company was loath to provide information at that time so the whole world has been in a little bit of a fog about patronage on the airport link. It's not a criticism, it's just to help the final report.

DR CRAIK: No, it's very helpful the information that you've given us. There has been a significant increase now that that access charge has come off Green Square

and, is it, Mascot or - - -

MR ANDERSON (ALC): Yes, that's correct.

DR CRAIK: Have you had any projections done as to what the actual increase might be if the access fee was taken off the airport station?

MR ANDERSON (ALC): Look, it's been very interesting our experiences. On 7 March of this year we did have fare reform which virtually halved the ticket pricing at Mascot and Green Square and the increases - I did actually bring along a graph because I thought you would ask me, if you're interested. The volumes have virtually increased by 6000 people at day or nearly 80 per cent. I think that if we had fare reform at the airport station, of the five million that we do, my feeling that it would be in the order of about 30 per cent. So I think that we could increase patronage by at least one and half million people.

DR CRAIK: Have you got any studies done on that since that one or is your conclusion based on - - -

MR ANDERSON (ALC): That is my conclusion based on having my fingers actually right on it but also more recently I saw in the - Sydney Airport is always interested in the matter and has also had various consultants holding similar views. But I think quite conservatively I'd have to say, if we've had 80 per cent increase off airport, I would think that perhaps in the order of 30 per cent.

DR CRAIK: Okay.

MR ANDERSON (ALC): So it is a lot and I think that's in the order of, as I say, one and a half or even two million, which all relates to getting people back off the road networks and so forth.

DR CRAIK: The Department of Infrastructure and Transport said that the Airport and East Hills line - "Sydney Airport is saying that the airport and East Hills line has operated at capacity between 8 and 9 o'clock in the morning for the last three years," and if the excess fee was dropped, the additional travellers would have to be outside that 8.00 to 9.00 peak to actually get a ride on the train as I understand what is being said here.

MR ANDERSON (ALC): Yes.

DR CRAIK: Is that correct? So that there wouldn't be any more capacity in that 8 to 9 am period of the day. Is that right?

MR ANDERSON (ALC): It is. That's one of the challenges that we're looking at

at the moment, that if we did have further fare reform - and even I have to say with our ongoing growth - between 8.00 and 9.00 in the morning and 5.00 to 6.00 at night is the peak times for us. During those hours we have eight train services each way and I have recently been in discussions with RailCorp in Sydney to increase that to the order of 10 or 11. So I'm hopeful that with the new trains and so forth going slowly on in Sydney that we'll be able to increase services. That's the answer to it, so increasing an extra two or three trains per hour, bearing in mind that each train carries about 1200 people. So all of a sudden you're quite significantly increasing the capacity. So it needs to be balanced but this certainly can be done.

DR CRAIK: That's good.

MR ANDERSON (ALC): I should say that everyone is still getting on the train during those hours, no-one is missing it. It does get a little bit chaotic but - - -

DR CRAIK: Cosy, by the sounds of it.

MR ANDERSON (ALC): Cosy, that's probably the word.

DR CRAIK: How are your discussions with the New South Wales government on removing that access?

MR ANDERSON (ALC): It's more a matter of not necessarily removing but looking at options to change the concession that - - -

DR CRAIK: Someone else paying it or something.

MR ANDERSON (ALC): The concession is based on - it's a profit-share concession with various thresholds. When they are reached the government takes virtually the lion's share of the gross profit. So in my mind an opportunity would exist to amend or refine those arrangements. They're going quite well, just general discussions, and I'm hopeful that progress will be made on that matter into next year.

MR SUTTON: Just in pressing my memory, your company controls the four stations. Is that right?

MR ANDERSON (ALC): Yes.

MR SUTTON: The two airport ones, Mascot and Green Square.

MR ANDERSON (ALC): Correct.

MR SUTTON: So when the state government came along and made that change in respect to Mascot and Green Square that represented a windfall essentially for your

company.

MR ANDERSON (ALC): It does and - - -

MR SUTTON: It did.

MR ANDERSON (ALC): It did, and it was recently reported in the Financial Review along those lines. But nevertheless because there is a mechanism where the government captures the gross profit, there is a certain extent of the uplift gets recycled back into the government, so it's not all just one way. I have to say, though, and I was reported at the time, that it was advantageous and I didn't quite expect - - -

MR SUTTON: The revenues from the increased patronage were somehow shared between your company and the government.

MR ANDERSON (ALC): In due course, yes, after 2014.

MR SUTTON: I personally am a user of your service in the sense that I get on and off at Wollli Creek quite frequently and I have noticed with my own observation the increased patronage or what I detect as increased patronage. An interesting situation, when I boarded the train at Wollli Creek on Tuesday at 11 o'clock in the morning - I went to Wollli Creek, it was a ghost station and the train I got on was a ghost train. There was nobody on the whole train. But when we got to international and to Mascot, pleasantly from my point of view - I'm interested in good public policy - a lot of people were getting on. It was really quite remarkable the number of people getting on at international and I got off at the domestic. So that was good.

However, I can't help but feel there is some sort of logistical problem here when the train that has come from Glenfield or Campbelltown or wherever it's come from is empty, it gets to your two key stations at the airport and obviously it picks up a lot of passengers there and it takes them through Central, I suppose. Do you seek the - I mean, it must be difficult for state rail to have a train that's essentially empty and then takes people three or four stations.

MR ANDERSON (ALC): It's hard to know what went on beyond the line, of course, between, say, Campbelltown and - - -

MR SUTTON: The odd person got on and off, I guess.

MR ANDERSON (ALC): Yes. I have to say in my mind it's encouraging, so long as there is plenty of capacity by the time it gets to Wollli Creek.

MR SUTTON: Think of the broad public policy issues involved.

MR ANDERSON (ALC): Look, it is a complex issue of rostering and scheduling in RailCorp. They do a great job. RailCorp has their faults but I'm one of their supporters actually, and it's a complex issue but it's very well serviced the airport line. It's one of the best serviced lines in Sydney and they provide rolling stock through that line 19 hours a day, every day of the year on average every nine minutes, 82,000 trains and there's just a lot of capacity. So in a sense I have to say I'm not entirely understanding your observation. I think you're meaning that it's probably a waste before it gets to Wolli Creek.

MR SUTTON: It's a ghost train. It must be difficult for State Rail to contemplate that idea but maybe that when there's a football event or something, the train remains empty until it hits the station where the - or the entertainment event. Maybe that's par for the course.

MR ANDERSON (ALC): What I will say, one of the good things that they have done in the last year or so, if you're aware, is that they have put in the Revesby Turnback. So in days gone back the trains had to go right out to the end of the line, Macarthur, Campbelltown, so I can soften your concern by saying that a lot of those trains are not going as far, not to the end of the line and back, so they're not wasting capacity during the day.

MR SUTTON: One other quick personal observation. Paying the \$15 from Wolli Creek to go about one and a half kilometres. It just doesn't seem natural but anyway, that's part of what hopefully will be tackled at some stage. I want to ask you about - we've got very serious concerns and that's part of our terms of reference, the whole question of congestion around Sydney Airport - well, all the key airports but particularly Sydney - and we do see rail as part of a solution. Your communication, cooperation et cetera with Sydney Airport, how would you rate that as an issue?

MR ANDERSON (ALC): Look, I have to say it's not an issue. I have a very close relationship with Sydney Airport, the previous chief executive and there's been a bit of a turnover of people there in more recent months so I'm renewing my acquaintances with the new management. But, no, they're very supportive of what we do. I don't have any problems with that. Not putting words into their mouth but they know that the future of Sydney Airport in so many ways is tied up with us in the rail connection. To put through millions and millions and to get to the end of our concession they're predicting 78 million people going through the airport, which is an additional 35 million from present, and I think logic also says that enormous amounts of those people need to go through the rail.

So they're very supportive of what we do. They're critical of the pricing mechanisms and I'm working through that. I think a lot of this goes back to the pricing structures and your \$15 from Wolli Creek and so forth. It needs to be better. It goes back to the structures established in the 1990s and I do feel that the time is

now right to - 12 years on, out of administration, patronage going well, that perhaps the time is to review the arrangements.

MR SUTTON: One last thing. The increased patronage that is happening on the line, do you have any knowledge as to whether that is just the natural growth that is happening at the airport, in terms of passenger numbers are growing and you're just picking up your share, or do you think proportionately the mode share, as it were, is altering in favour of the rail. Do you have any sense about that?

MR ANDERSON (ALC): It's very clear to me that mode share is increasing way above what the airport is experiencing and off the top of my head if I look at August 2011 I think that domestic volumes at Sydney Airport were down maybe 1.5 per cent, whereas ours were up about 8.5 per cent. At the same period internationally we were up about 15 per cent and they were up about 1 or 2 per cent. So we are experiencing a big lift in mode share and particularly that graph that I put in my second submission indicates that. I think that the company as it has been has been to blame and if you have been a regular user, I'm hopeful in the last couple of years you have seen a very significant increase in the marketing of the company increasing ticket sale capacity. We run five ticket windows virtually 19 hours a day. A couple of years ago it was two, people were lining up for 10 minutes, just walking off. All that has been changed which has given us this great uplift.

Last financial year had an extra 518,000 more people than the year before and there was three or four or five hundred thousand the year before that. So we have had a million more people going through in the last couple of year. I think it's this combination of better marketing, better service and just a revitalisation. It is certainly getting an uplift in mode share.

DR CRAIK: If there was 75 million passengers at Sydney Airport and even if your mode share stays at about 20 per cent or something, that's about 17 million, according to my calculations, can the train handle that?

MR ANDERSON (ALC): I'm quite confident that it can. It's all about volume, of course, and rolling stock. I lived in Japan for a number of years in the 1990s and if you have had that experience you go down to any of their major lines and they're virtually coming every two minutes, there's not even a timetable there. So it has to be a balance of just getting more rolling stock onto the line. At the moment it's an average of nine minutes. As the volumes increase, I'm hopeful that we could bring that back into three or four minutes in, say, 10 years' time. Our contractual arrangements with the government also necessitate that that would have to be the case.

DR CRAIK: Are you doing anything to encourage the providers of the rolling stock to have baggage-friendly rolling stock?

MR ANDERSON (ALC): It's difficult because it is unusual, it's all linked into the broader network. Not really but I tell you what I really am encouraged about with the new rolling stock is the enlargement in the new trains of the lobby area.

DR CRAIK: The standing-up area?

MR ANDERSON (ALC): Yes, the standing-up area. That's really advantageous for us. I'm a little bit not exactly - I know the train has been criticised for many years about the luggage. My view is that because we're only 12 or 13 minutes from Central that people want to stay next to their bags and not necessarily put it somewhere and walk to the back of the train for a seat so that's why I'm more encouraged with the larger lobbies in the train. But the new trains, there's only three of them of in Sydney - - -

DR CRAIK: Maybe they don't go to find a seat because it is difficult to lever your bag down, having done it.

MR ANDERSON (ALC): Maybe that's part of it. It has got its faults. But what I can say is that the - and you may have seen some of the ongoing controversy but nevertheless there are some new trains coming onto the Sydney network, there's three at the moment and they've been used on the airport line and it creates this great morale lift and I think it will be terrific when they all start to wash through in the next couple of years.

DR CRAIK: Okay. Thanks, Tim, very much for that. That's very helpful and thanks for all the information.

MR ANDERSON (ALC): Good.

DR CRAIK: We're running a bit ahead of time now so we might have morning tea early and we'll try and start again at 10.30, assuming people are here. Thank you.

DR CRAIK: Well, thank you very much for agreeing to change your position in the schedule, that helps us out quite a bit, thank you. So if you could state your name and positions for the record please, both of you, and then if you'd like to make a few brief opening remarks, we'd be very happy to hear from you, thank you.

MR SHARP (Q): Rob Sharp, head of global airport infrastructure and services for Qantas Airways.

MR CARDEN (Q): Jim Carden, I'm head of government and public affairs for Qantas Airways.

MR SHARP (Q): Chair, thank you very much for the opportunity for Qantas to have the opportunity to have a few words in response to the draft productivity report. The natural monopoly that the airports in Australia do enjoy is actually penalising the travelling public. We believe that there's no disincentive for major airports to not charge excessive rates for aviation facilities. What that has led to is an increase in cost to the travelling public and to airlines.

The current light-handed approach to regulation, which has had much debate, we believe has been ineffective in preventing that use of market power. If you just look past aeronautical pricing, we see examples where excessive leases are charged for airport offices, lounges, maintenance facilities, check-in counters, service desks, staff carparking; a lot of the ancillary services that are actually fundamental to running an operation. These are typically benchmarked in excess of what we would believe to be commercial rates. What that does is it drives significant cost into the operation, which impacts on the consumer.

I think there's a historic point in time here where we've had a number of reviews into the airport pricing regime and we're at a point where there's about a \$10 billion pipeline of capital coming down the Australian domestic airport arena. There's a significant amount of productivity that's attached to driving and delivering such a large chunk of infrastructure. If we're to extract that productivity we believe we need a change in the way that the light-handed regime is actually operating.

The commission's review talked about a voluntary code to help with pricing principles and negotiations. We don't believe that that's going to be sufficiently robust to actually change behaviour. We still highly recommend consideration for a mandatory code of conduct. Unfortunately reasonable and commercial outcomes that are negotiated are the exception. Basically it takes many years for us to reach agreement, and we see that as really being an example of the advantage that airports have, competitive advantage, that you don't see in other industries. What that means is that to actually drive more reasonable outcomes that are consumer focused, we do need to see some sort of regulatory action.

The codes of conduct are basically an avenue that we see that would support negotiations, and potentially if there was a dispute, provide a reference point for resolving disputes in an efficient manner. The current framework we don't believe strikes the appropriate balance between providing incentives for airports to invest, and we're as keen as everyone to see the appropriate investment occur at the right time. But also, it needs to be balanced with mechanisms to prevent excessive pricing.

We don't agree with the Productivity Commission's view that airport operations actually engage in commercial-focused negotiation. Yes, we have negotiations, but we believe the pendulum has actually swung too far in the favour of airports. The light-handed framework does enable airports to generate returns that we believe are in excess of what a commercially negotiated outcome would deliver. The end result: higher expense for consumers and airlines. We detailed multiple examples of this pricing behaviour in our original submission, and we would emphasise that the submission that we put in went to exceptional lengths to try and articulate the behaviours that are occurring.

We've, I suppose, repeatedly been forced to enter into agreements after protracted years of negotiations by virtue of the market power that exists. In other words, it takes considerable amount of time to actually get to a point where you agree; are you actually agreeing to something that's commercial? We're also disappointed that the draft recommendation is against an airport-specific arbitration regime through deemed declaration. The Qantas Group supports the ACCC's recommendation. We see that as having considerable merit and believe that such a step change would actually bring a balance back into negotiations.

The Productivity Commission did express some concern as to whether the airline community and Qantas would abuse that power. The reality is that that type of arbitration involves considerable resource, considerable staff and time and effort, and I think there's a significant disincentive for us to be running off to an arbitrator. What it does do, however, is provide a mechanism that could potentially refer back to codes of conduct and deliver an efficient outcome.

The commission also raised questions as to why Part IIIA declaration hasn't been utilised on a regular basis, the reality being that it does not actually provide an effective constraint to the airports. It's highly time consuming and if we're looking at commercial outcomes in commercial time frames it doesn't actually deliver on that. So if we're talking \$10 billion coming down over the next 10 to 12 years, three to four years of dispute resolution and progressing that, you're already halfway through the process. So delivering on the productivity benefits that come from that would be questionable.

We have a common goal with airports: to increase passenger volumes and

grow services. There's clearly a success there over the last 12 years or so. There's been infrastructure that's been built. We see passenger volumes up. There's new business models that have been entered into the market such as low-cost carriers. The passenger numbers have actually sustained that growth. However, there does remain a lack of accountability over the quality of the services that are provided. The recommendation towards an opt-out of service monitoring, we believe, has a lot of merit. The service level agreements that have been negotiated with airports are comprehensive, to actually focus on customer and airlines and the efficient operation of an airport. If those are robust and you can achieve robust service level agreements, I believe there's a lot of value in that. However, we are seeing a range of service level agreements in place, often they're very high with no teeth. Some don't have service level agreements at all and others are at the other end of the spectrum, where they are actually reasonably robust documents. But as a general comment, I think there's merit in heading down that path.

Those comments also apply to regional airports and particularly given the significance of airports for various businesses in Australia in tourism, mining in particular. They are playing a very significant support role in delivering services to those capital cities or between capital cities and those regional ports. The issue that we see is that there are basically no principles that are applying there and we believe some sort of pricing principles or a cut-down version of codes of conduct or some basic rules would make sense, such as a focus on basic principles around capital planning, the pricing that's applicable, basic building block models, the planning being on a long-term basis.

There are significant expenditures coming down in regional ports over the next five years and there's nothing to underpin those negotiations. What we believe that will do is actually help facilitate some common ground in those negotiations, which don't exist at the moment. So fundamentally transparency of costs, consultation and scope around the development plans would be significant value adds in the regional space.

So, in summary, the light-handed approach to regulation, we believe, has been ineffective and that market power has been exercised. We endorse the ACCC's deemed declaration approach as being reasonable, supported by binding codes of conduct to facilitate the negotiations, with some reference in there for regional pricing negotiations. Why are we taking that position? Fundamentally there's a very large amount of capital that's going to come into the industry that's needed for the airlines and the airports. Productivity, however, is absolutely fundamental. We believe that without some regulatory change here, there's a real risk to achieving that productivity gain. Thank you very much.

DR CRAIK: Thanks very much, Rob. Are you guys going to put in a submission?

MR SHARP (Q): Yes.

DR CRAIK: Good. When can we expect it?

MR SHARP (Q): We'll send it through. I'm not sure where it's at. It's actually completed. It should be on its way.

DR CRAIK: We look forward to receiving it. Clearly you would prefer a deemed declaration plus a mandatory code of conduct. What would you see as being envisaged in a mandatory code of conduct? What sort of things in a mandatory code of conduct are you actually envisaging?

MR SHARP (Q): The basis of commercial negotiations at the moment is effectively using the ACCC building block model, and that is used as a reference point around which negotiations occur. What we see across the country is a differing approach to how principles are actually interpreted and applied. So we spend probably 50 per cent of our time debating nuances around WACC, aero/non-aero splits, all the various make-ups, the basics, if you like, of the negotiation. We believe there would be a lot of efficiency gains through having more granularity around some elements of that model.

When we say mandatory, we're not saying we need a very comprehensive re-regulated defined building block model. We're not heading down that path. Really at the moment there's very little there. Some enhancements to that, we believe, would add significant value to the efficiency of the process. So rather than taking two or three years to negotiate, we believe those time frames would come back quite substantially.

DR CRAIK: If it's a mandatory code of conduct, I think I'm right in saying that the ACCC needs to be involved, so there would be some, I suppose, specification or boundaries on some of those parameters and the ACCC presumably would be signing off on such a mandatory code of conduct. With deemed declaration of airports, specified ranges of values for parameters, you're getting pretty close to price setting, aren't you?

MR SHARP (Q): Price setting is, I think, an approach where you've actually got a lot of rigour and very defined elements to it, so it becomes quite specific, almost formula based. We certainly see that in a lot of the overseas airports. London Heathrow is an example which gets a lot of airing. We're not envisaging going down that path. Is there a risk in heading down that path? We're certainly not wanting to go down that path. We see that as actually being detrimental. Commercial negotiations are important, but do extract value for both organisations.

The question though is one of efficiency and the question, I suppose, for the

Productivity Commission is, is some movement possible. The risk is that you're flagging, does it go the whole way back down to pricing. No-one in the industry is wanting that. The question is what is the pathway to actually get to that. We believe if the code of conduct is struck at the right level, then it has two benefits: one is that it's more principle-orientated, not down into the detail of a specific formula, and secondly if there is a dispute, there's a reference point for the arbitrator and we believe that would actually add quite significant value.

DR CRAIK: If they're getting a code of conduct that kind of specifies a range of values you can have for a WACC and things like that, that's getting pretty specific, isn't it?

MR SHARP (Q): If you're getting into that sort of definition, I'd agree, and that would be something that the industry would need to discuss and debate and what we're looking at is a move, not a defined model. So it really comes down to the mechanism of how you would define those rules.

DR CRAIK: So does that mean that you find all airports difficult to negotiate with or - - -

MR SHARP (Q): The answer is yes, the reason being that often there's a lack of transparency and it takes quite a bit of time to actually understand what the actual drivers are. To be having a negotiation and you've had an open book, you'd be basically saying what are the key business drivers for both parties and how do you actually come up with an equitable outcome? It often takes quite extensive time and effort to get to a point where we have enough information to actually understand what the commercial deal is. That's the inefficiency in the process. Do we get there? Regularly we get close to it, but it takes a very extended period of time.

DR CRAIK: But given the nature and sometimes the terms and value, I suppose, of the agreements, is that surprising it takes so much time?

MR SHARP (Q): I think it's surprising that it's so consistent across the industry, and that's the point that we're raising.

DR CRAIK: So which airports would you want deemed to be declared? Every airport in Australia or - - -

MR SHARP (Q): Every airport in Australia?

DR CRAIK: - - - every airport that Qantas flies to?

MR SHARP (Q): I think, for me, the key value is actually around the codes of conduct. That actually provides the basis for commercial discussions. It provides a

reference point. Deemed declaration is still deemed last resort, from our perspective. As I said, lots of time and effort and you end up with relationships potentially being tarnished because you're actually putting the gloves on with an arbitrator. It's not something you would rush into. So, as a consequence, the main value driver is actually having that reference point where you can have the negotiations. If I take examples in the regional airports, often we have no visibility of the underlying capital plans, a price is just put on the table, "This is the price you're going to be charged." How do you actually, from a commercial perspective, get some visibility as to whether that's a sensible price? If you're talking an organisation that has market power - and we're a large organisation as well - you need to have a partnering relationship for that to be successful. At the moment we're not seeing the basis of that being in place.

DR CRAIK: You say airport charges and their potential effect on the cost of air fares and things like that and cost to consumers. I guess one of the things that struck us a bit is even though airlines seem to complain about airports charges their annual reports don't mention them as a problem or an issue. We've been following the speeches of your MD and they don't get an airing; a lot of other things get an airing but airport charges don't. They're not shown in the price of an airline ticket. So how much of an issue - - -

MR SHARP (Q): Yes, look, in terms of comments that we've made publicly - now, there's actually been quite considerable commentary. If I speak on behalf of Bruce Buchanan, Hobart Airport and Darwin in particular, there was a lot of press, there's a lot of public comment. 18 months ago, two years ago, Alan Joyce publicly spoke about Brisbane Airport and Sydney Airport. We had significant concerns. That actually fostered some discussions and deeper relationships, but there was quite a period of public commentary. David Epstein, our head of government corporate affairs, just last year spoke at an airport forum and publicly named a number of regional airports where we were seeing a number of issues. So there are a number of forums where we do articulate that, and typically in the press.

In terms of air fares - and it's an interesting one, because typically we need to package all our costs together in the price of a ticket, so it becomes problematic on how you actually unbundle that and how you actually disclose that to the public. I think it is somewhat unknown to the consumer, because those charges are very much hidden and rolled into the price. There's a number of other items in there that are coming along such as the carbon tax. So there's something the industry will need to have a look at, because there are a number of these charges layering in. One of the issues we face is that it is those layering in of charges that actually forces fares past price points in the market, which actually has quite a significant impact on demand. So we're quite concerned about it. How do you actually communicate that is actually - it is problematic, but it is something that we probably do need as an industry to be considering.

DR CRAIK: You say you support the ACCC's proposal, which is deemed declaration, so that really requires a decision as to well, which airports would be deemed to be declared. I suppose what we were proposing in a show cause process, and I would be interested in your commentary on this, is that if an individual airport was causing difficulty or was abusing market power, and presumably in that way causing difficulty for airlines, then there would be a process that we followed through. As a result of that process, and if that was substantiated after a Part VIIA price inquiry then the ACCC could recommend one of a number of remedies if it wanted to, to the government, of which declaration is one; price setting might be another.

You seem to have a blanket proposal, and I'm not really sure of the boundaries of your deemed declaration proposal in terms of numbers of airports, but ours was a selective one for airport by airport. So I guess we'd be interested in your commentary on our show cause.

MR SHARP (Q): So in the original submission we were still promoting this concept, and we were targeting tier 1 and tier 2 airports; that's unchanged. In terms of your question around show cause, a couple of issues that from a practical perspective emerge. One is that if it's based on the monitoring that occurs, there's been a number of questions around the robustness of that monitoring and the statistical basis of it.

If you're basing show cause on something that there's a question mark over, there's a fair bit of work needed, I believe, to actually have something that the industry as a whole is going to be comfortable with. If contracts are for five, seven years, the basis of the pricing is set for quite an extended period. The show cause suggestion you had was basically along the lines that over time you would see trends emerging. It's a long time between drinks if you have contract periods. So you're talking 10 years before you even potentially have your second round of pricing; very difficult to see trends coming out of that. So from a pricing perspective we had some questions as to whether it would really achieve the objective.

The other question we had on it was if you're actually focusing on productivity, the types of items that are covered in there at the moment are more around service delivery as opposed to productivity. So the actual issues of the day that we've been flagging in our submission are largely not covered in those surveys. So the question we had was well, if you're not actually really tracking that as drivers, how are you actually going to pick the trends and then take action? So we really couldn't see a commercial benefit emerging out of it. If it was going to go down that path we'd certainly be happy to work with the commissions or the committees that are put in place to develop it, but there would be a fair bit of work, I think, to get it to a stage where it would have any teeth. What I mean by that is ultimately it has got to change

behaviour, and we have a real question mark over whether it would achieve that objective.

DR CRAIK: Okay, thanks. John?

MR SUTTON: On the issue about the transparency of charges, Virgin this morning, when they were here sitting where you are, stated on the public record that they are seriously looking at how they can demonstrate airport charges on the ticket or in the process of purchasing a ticket. They say that, so - I mean we all believe in transparency, and that clearly seems to be a useful suggestion. You weren't here on the time, it's on the public record, there's nothing secretive about it, but it does seem to be a useful suggestion, which if the airlines can do that it can't but help, I guess; just a comment.

You say that in the process of negotiating, frequently these processes take a hell of a long time, it's a lopsided negotiating process and often you eventually sign up; you're not too happy about it but you sign up. I wrote here: does that mean Qantas signs under duress, does it mean something less than that? Can you in fact flesh out why you end up signing, because one of the very strong arguments of the airports is that the airlines sign up. They wouldn't sign it if they had such a dramatic beef - why would they sign the thing? Can you flesh out for the public record why it is that a big corporation like Qantas signs something that you find to be unsatisfactory?

MR SHARP (Q): Yes, it's all about degrees, isn't it? I think if duress was involved we would take action under Part IIIA. You'd run the gauntlet. We've stepped up to that on one or two occasions and in the end decided that the effort and time and cost, which is in the millions, is not worth the effort, hence our recommendations. In a commercial negotiation often the term "win-win" is used. If there's a lose-lose does that mean it's just another way of saying we've got a win-win? Airports would rightly say that we agree on the program, the capital that's required

Often the debate centres around timing of capital and also on the pricing. With the pricing there are some points of principle. Pre-funding is one that pops up occasionally. Brisbane Airport with the new parallel runway is probably the major one at the moment, because it really puts a spotlight on it just because of the sheer amount of time that the preparation works are there; but notwithstanding, those debates do occur. We're a large organisation, so we have areas of expertise that are embodied in the organisation, so we have people who are Treasury experts, we have people who are experts on building block models. They bring their expertise in. End of the day when we're signing off, a lot of those areas are not comfortable with the detail, if you like, that's behind the pricing proposals.

So yes, a commercial agreement is signed. And why? Because capacity is

needed to support growth. If we can't grow that obviously hurts our profitability. If there's product implications - so terminal might be getting run down or constrained. From Qantas Airlines' perspective, product differentiation is very important. So that's starting to be impacted; it actually impacts on our ability to deliver. So therefore you get to a point where the pain is such that you say, Yes, it's worth the dollars and I'll sign off." However, does that mean that those dollars are actually the appropriate commercial dollars, and we're raising a question mark over that. The detailed submission gave lots of examples of why we think that arises.

I suppose more recently during the GFC deals were done, but we certainly felt that the risk all sat with the airlines principally. Our yields were substantially hit. We were needing to fill aircraft seats. But for each passenger we were still paying full price to the airports. Yes, we're doing that because we're capital intensive and we need to fill those planes, but it does actually act as a significant risk mitigator to the airports. We saw no reflection of that in pricing. So those types of issues get under the skin. It's probably not to a point where you would say there's duress, but it is those commercial trade-offs.

The question is - that just sounds all like normal commercial negotiations - and I can see you're nodding - so the question is how much of that is an excess price. Our economists modelled that. We had various debates over, you know, how far that's occurring. I suppose the point we're raising is that there's enough examples where we believe that that is impacting on productivity and the costs and flows through to the consumers.

MR SUTTON: On the issue of the pricing principles and, you know, the idea that we float off additions to the pricing principles and/or the parties come together and apply themselves to a voluntary code. We're open to the idea that there could be principles, there could be issues that could be put down on paper as a guide to the industry that would cut down the amount of time, would make the negotiating process a more efficient one, we're open to that idea, and you spoke very much of that, as opposed to, you know, getting right into the heart of pricing issues.

I do ask that in the submission that's coming, if you could apply yourself to concrete examples, because the pricing principles - there has been some embellishment over time and we have been able to add in some items that have helped the industry. But we need to find out what these - I mean, notionally it sounds good, but what are they that can make the negotiating process - you know, we don't want people arguing about reinvention of the wheel. If we can pinpoint what they are, so I very much would ask you to do that in a targeted way.

MR SHARP (Q): We'll certainly do that, and our submission basically says we're quite willing to work with the commission or a committee to frame that. I'm sure there'd be cross-industry representation there. More than happy to send through

examples. It'll be basically extracts from the very detailed report we originally put in. Flagged about eight areas of concern in terms of that aspect.

DR CRAIK: One of the things you raise, Rob, is this mandatory code of conduct. Who would actually decide what was in it? I mean, at the end of the day the ACCC would sign off because it's a mandatory one I assume, but who would actually - I mean, do you really think it's likely that airports and airlines would be likely to reach anything approaching an agreement on a code of conduct?

MR SHARP (Q): That's an interesting question. I'd like to think so, if there was a recommendation that there was value in going down that path. I think if you were getting down to a comprehensive model with all the t's crossed and the i's dotted and mechanics, probably not, because everyone would have a view. If it's around principles or things that would make life easier in negotiations, I think there would be mutual interest. Examples in the modern world are things like aeronautical splits. Assets are now used for multiple things: retail, carparking, passenger flows.

We have areas that we use for Qantas-specific activities with sales desks, actually delineating how you allocate costs across those, and it might sound a pretty basic comment, but there's a lot of dollars associated with that. Some sort of guidance around how you go about those because we see multiple approaches and they're quite large variations in the way those sorts of outcomes are applied. At the moment it's really sitting around a table individually and having quite extensive debates around those. In that particular example some guidelines around, you know, what are the drivers of those and how you might allocate costs would be of benefit to everyone, I would have thought.

DR CRAIK: Thanks. John?

MR SUTTON: Service level agreements, we float the idea of where parties are prepared to sign on and, you know, critical mass can be established, et cetera, that we think that might be a good way to proceed in lieu of surveys, et cetera. You seem to be on all fours with that. You support that?

MR SHARP (Q): Yes, we support that. We put a lot of value on service level agreements and we've been trying to drive an agenda for a good couple of years. Service level agreements have been around in various forms, but often, from our perspective, they have been fairly high level and not really focusing on all the business drivers. When I say business drivers, I'm talking productivity, operational efficiency, not just the consumer product element of it. We've had some success in some airports, but in others we're still getting quite a bit of resistance to comprehensive service level agreements. I certainly endorse this, I believe it's of significant value, and if agreement can be reached with an airport I'd certainly support them being able to opt out of the surveys.

MR SUTTON: How important is the publication of the detail? I mean, airports, many of them have said to us, "Well, they're commercial-in-confidence documents. We could only report anything at a very high level or in a very broad fashion," et cetera. I suppose cynically you could say, you know, that's an attempt to sort of on the one hand see off surveys, and then publish something that's pretty meaningless or so broad that it doesn't tell anyone much. How important is public exposure as opposed to the parties agreeing between themselves?

MR SHARP (Q): I suppose the question is where is the value-add that comes from a service level agreement, and it's actually in the regular reporting and communication between the two parties as to where issues are emerging so that you can actually have dialogue around those and address them. You will always have varying, competing demands on capital and constraints and points in time where things arise, so service levels will vary over time. One of the challenges in doing detailed reporting is how you communicate all those nuances around those competing demands, and that's always one of the challenges with the high-level surveys. If you don't actually have that in the public arena - - -

MR SUTTON: Does it matter?

MR SHARP (Q): Does it matter? From my perspective, no. On the flip side, if you're looking from a consumer perspective, because obviously we're wearing an airline hat, there may well be some customer-orientated service levels that could be put out into the public arena. But, you know, you'd basically look at a subset that would be relevant. For example, service levels on how long an aircraft can stay on a gate and turn around is not going to be of any relevance to the public, it's really around the operational efficiency of the airport asset and the aircraft; or access to parking areas for ground-handling equipment.

There's a lot of service level aspects that drive our operational efficiency that in the public arena probably really doesn't generate the discussion. The concern I have got is that given there's multiple stakeholders - and, yes, we might have a service level, but how do you actually ensure that there's enough service level agreements in place - I suppose key players - that you get the desired outcome. Certainly we're not privy to the mechanism that you're thinking of to achieve that, but as a general concept we see a lot of value in service level agreements.

DR CRAIK: Brisbane Airport says they've offered to have service level agreements with airlines but nobody has taken them on, nobody wants them.

MR SHARP (Q): The debate in Brisbane is around what's controllable and what's not, and often there are complexities around that. So if someone is late on to a gate, how do you actually measure that service? They might be late on to a gate because

of taxiway congestion or airspace congestion, it may be outside of the airport's control. How do you actually handle those? We believe that there are mechanisms to take those into account. We have recently entered into discussions with Brisbane Airport on the next five-year pricing deal, and there is agreement that service level agreement is on the agenda to be discussed. We're drafting some proposals, and that's where that's at the moment. I'm comfortable that the dialogue is occurring, but it's early days.

DR CRAIK: Okay. Can I raise the issue of regional airports with you. You raised it in your comments to us. It's a bit hard to think that some small regional airports run by local government authority exercise market power over Qantas. I mean, that stretches the imagination a bit. Often you're the only player flying in there. We haven't had many submissions I agree from regional airports, it's not the major focus of our inquiry, but we have had some, and they really just say, "Well, airlines generally just refuse to pay or say they'll withdraw the service," and because the local council or whoever it is is keen to keep the airline coming to service their local constituents they subsidise you guys, basically I think is the bottom line. Is the difficulty in reaching agreements that you think are reasonable and they think are reasonable, is that a function of the sophistication of the regional airport management?

MR SHARP (Q): It is. As I said earlier, the challenge that we face is if you're looking for a price for a given asset - we're quite happy for the airports to receive a fair return on the assets. Transparency is the biggest issue we face in that we don't know what the asset bases are, whether they've valued them; often the assets were given across to the councils by the government and they're now at a stage where major redevelopments are required, and what we're finding is that the skill set is largely lacking there. So particularly in intra WA where the mining boom is driving sizeable increases in size of aircraft, the airports are really struggling with not only the runway capabilities but certainly the terminals.

So when you're looking at long-term planning, there's some thinking around it but really I suppose the mechanisms and the expertise are somewhat limited. What that means though is when you come to pricing they typically fall back on CPI and a generic return on assets, and outside of that there's very little put on the table. So the challenge we have is, although we're paying a fair price, often we see major increases in passenger volume, no capital expenditure and the price goes up by CPI. So quite clearly it's not following what we would consider normal commercial pricing principles.

DR CRAIK: The comment yesterday made the Airports Association in relation to the possible application of the existing pricing principles to regional airports was that it would very likely see a rise in the cost to airlines, not a decrease in the cost to airlines.

MR SHARP (Q): Yes, and the key driver for that is, what value do you put on the assets. So a lot of the regional ports, notwithstanding the fact that they receive the runways and the land, are wanting to put a commercial value on it. So they then say, "Well, the price needs to go up." So there's an argument around, "Is that an appropriate mechanism for the pricing?" You mentioned that we can pull out of regional ports. There are - - -

DR CRAIK: Or at least threaten to anyway.

MR SHARP (Q): Yes, and there's a lot of examples. There's some flights between Kalgoorlie and Adelaide which are always marginal. Certainly there's some subsidies there to initiate services, the idea being that you can grow the volume to a point where the flight becomes of I suppose a sufficient level that it maintains the service. By and large though our key customers - the BHPs, the Rio Tintos, the large mining companies - have major operations there. We're largely flying in workforces that have to arrive on that day, they're literally going straight onto shifts. We have no ability to pull flights. The bulk of our flights are actually geared to servicing those customers.

It's not dissimilar in the large airports. Business people want to fly from downtown to downtown. It's not as though we can suddenly shift our planes to another airport. The customers don't want to go there, they want to go downtown. You fly where the customers need to go. In these small regional towns, particularly where the mining industry is being supported, there is no ability for us to suddenly just pull aircraft, because the ramifications for those key customers is so huge.

So then it just comes down to, is it a fair and equitable return that the local councils are receiving. Our view is that in some instances we just don't know because we just don't get the transparency; in others it's quite clear that we're not; in others they're pushing the envelope in terms of revaluing assets and charging off revalued assets, which is a principle we don't agree with. So it's almost going back to the line-in-the-sand discussion at the last Productivity Commission.

DR CRAIK: Have you ever thought of approaching someone like the regional airports association or someone to actually see if you can get some more sophistication in the - - -

MR SHARP (Q): Yes, look, I think our recommendation is along those lines. It's actually getting the relevant parties together to look at how you actually drive some sophistication. We are aware some of the larger airports are actually talking to some of the regionals as well about providing some expertise. So I think there's a recognition that there's an issue there. We're also aware that there's some consulting companies that are touting their services, which are to actually help fill that gap.

Typically it's a basic building block model. We think it's a good initiative. However, they are typically revaluing assets, which is what is driving those price increases.

DR CRAIK: Thanks. John?

MR SUTTON: Rob, I just want to pick up on the P word that you used a fair bit today, productivity; something we all believe in. I take it your case is that current regulatory arrangements are impinging upon or at least going forward with this \$10 billion to be spent, et cetera, that somehow the currently regulatory arrangements are holding back productivity or cutting across it or something to that effect. I want to invite you to, at least in your submission - and if you can develop it now that would be good, but I want to invite you to drill down a bit on that. It's fine to say it, but I think we need some specifics about how and why you say that's the case.

MR SHARP (Q): Okay, we'll articulate some examples in the submission. At a macro level there's two drivers of productivity: one is obviously the dollars, which we've been talking to to date; the other is efficient use of current assets, and how do you actually drive efficient operations in an airport. A \$10 billion price tag is very, very large. It has an impact potentially on demand. The sorts of price increases that will drive are about 7 per cent CAGR every year for the next 10 years. So we're seeing potential price hikes of 40 to 45 per cent; not insignificant.

Putting the pricing issue aside, productivity is a very key one for us. So if you look at what drives productivity for airline: efficient access around runways, taxiways. We're seeing airspace management becoming quite congested right around Australia. There's a large flow-on benefit if you can get efficient movement on and off runways. That is a very, very key constraint to the industry. Where you actually spend that \$10 billion makes a huge difference in terms of the operational flow-on efficiencies that can emerge. Fuel prices are high. For every minute that you're taxiing or you're waiting to get on to a runway, you're talking millions of dollars of operational costs.

On-time performance is another one. There's a lot of press around airline on-time performance. There's an industry issue, in that even if we as an airline community all got to a certain point where we were 100 per cent delivering there are fundamental infrastructure and constraints around airspace management that are actually needing quite a bit of focus over the next little while, and Airservices has kicked off reviews - one being the AIS program with Brisbane, Melbourne and Perth, and that's around runway capacity and how can you do things more efficiently benchmarking against Gatwick - which is the most efficient airport in the world. Lots of lessons to be learned. How do you actually bring that into the capital pipeline efficiently?

The question we've got is that if that pipeline of capital is going right across the

domestic arena, it's not just an individual airport you're negotiating with, it's actually the trade-off of investment across the whole domestic airport and that's the productivity dilemma that we're facing. Have we got the right mechanisms in place to foster the right price outcome but also to allow the discussions to occur in an efficient time frame.

What worries me is that we'll be sitting here in three years' time with here and now operational issues and we'll still be debating the nuances to actually get to an agreement. In the meantime, we've got two or three years of productivity gains that have been lost. So there's a two-pronged focus for us there.

DR CRAIK: Can we just ask you about Brisbane's second runway and your views on it. Do you believe that the proposed price tag is excessive, arrangement for funding are inappropriate?

MR SHARP (Q): It's a complex piece of infrastructure. The complexity is driven by two things; one is that you're basically building on a plateau of mud, so it's very, very expensive and it drives a very, very long time frame for the initial tranche of capital. So of the 1.3 billion, about 500 million of it is for sand and reclamation works which sit there for five-odd years. So half a billion dollars sitting there for five years with no benefit at that point is one of the challenges.

The pricing regime doesn't adequately address that and this is probably the first piece of infrastructure of this nature and size that's come up, so it's generating a lot of debate in the industry. There's been considerable work done at various reviews over 10, 15 years on is it needed, when it is needed? There's been working groups on the specification and I think, by and large, there's a deep understanding in the industry as to the nature, size and cost drivers.

The 1.3 billion does have some very large contingency amounts built into it and at the moment, that will just flow straight into the pricing. From my perspective, there would need to be mechanisms to reset pricing to balance the risk, if you like, of the construction costs, given the nature of this particular runway. So in terms of the price tag, they're probably the key issues.

In terms of the actual recovery mechanism which dovetails into funding, the cash flow equity, if you like, in the first five years is something around a third; Brisbane Airport equity, there's about a third that has been asked of the airline community, pre-funding, around 300 million, and then there's another third which is basically debt funding. So Brisbane Airport would view that as being a balanced outcome. Two points of principle for the airline community: one is pre-funding. As a concept, we typically don't agree with it. We're paying for an asset before we use it. Often the capacity that's delivered is often very long term in its nature, so as a consequence, what happens is you're effectively paying for future users. So when

they come in down the track, they pay exactly the same price, and none of that is actually addressed in the pricing model.

So the point of contention for us is twofold; one is how you handle that pre-funding. Our personal view is that there's two solutions potentially; one is that you look at some sort of mechanism where you have economic depreciation indexed where the return is still there on the asset but the asset is actually written off in a way that actually matches the economic use of that capacity. The gas pipeline industry up in Queensland is an industry that actually uses a similar model. We certainly think that moving forward, that as a principle is something that we'll be raising with most airports, given the capacity issue.

This particular piece of infrastructure is just large and it really does highlight this particular pricing issue. What's the inference to that? The inference is that the cash flow early on is lower and so therefore there's a question over the triple B rating and whether they can maintain that. My personal view is that that is an equity debt position for the airports. That is a risk appetite question for them and at the moment, that risk has all been largely passed to the airline community. So as a consequence, for Qantas, being a large incumbent, we end up bearing a very large portion, a disproportional cost of that future capacity by effectively paying it early. The pre-funding just exacerbates that. So the nexus that's been reached is really around how do you actually fund that and what's the equitable pricing and that's the discussion that is being had.

DR CRAIK: As we understand it, in England when T5 was being built, the regulator actually decided there would be pre-funding by airlines over a staged period.

MR SHARP (Q): Yes, they did.

DR CRAIK: Do you have a view about that? That might be a consequence of regulation - - -

MR SUTTON: Yes, T5 took about five or six years to build, so it was a fairly lengthy process. The interesting thing, there's also a question of timing that comes in. In London Heathrow, the underlying demand had built up quite substantially and so it was at a point where the passenger volumes and the revenue that was coming through made it much more economically feasible to do that. The question we've raised with Brisbane Airport is actually one around timing, not whether you need it, it's, "When is the appropriate time?" For us, that comes down to an economic question because there is an underlying demand there. So if you just forecast aircraft movements, you'd say, "Yes, let's build it," but ultimately there's got to be an economic review done to say, "What does that do on demand? At what point is there sufficient underlying demand to actually trigger the optimal time?" so there's a

debate around.

At London Heathrow, because there's been huge environmental discussion and the debate dragged on for about 10 years, the airport was almost at breaking point. The underlying demand was large, so therefore it makes it economically easier to digest that type of regime. Interestingly enough, the International Airline Association also comments on pre-funding and they're aren't necessarily saying you don't ever do it, but there was a number of criteria that they set out that the airline community would typically want if you were going to have pre-funding. It's around things like guaranteed access, it's around I suppose a long price agreement that's commensurate with the life of the asset. It's those types of items. At the moment in Brisbane, there's a five-year pricing deal for a 50-year asset.

If you look at some other industries, ports, for example, where coal exports have been building port capacity, they pre-fund, but they do it on the basis that they get access to a certain portion of the capacity. That is the quid pro quo for the pre-funding. But if you're passing the risk over, you're not doing long-term pricing, the pricing is inequitable, you're not ticking too many of the boxes in terms of getting agreement on pre-funding.

DR CRAIK: Okay, thanks.

MR SUTTON: Just a quick one on the length of negotiations, given that negotiations are so long, why isn't part of the answer to that to lock in long-term agreements? I mean, if you're going to spend two years nutting the thing out and it's very painful, why not lock in long-term agreements?

MR SHARP (Q): There are examples. Canberra Airport, I was personally involved in negotiating that for quite some years. It was a seven-year negotiation from when it first started and we have a very long-term arrangement there. Now, that works quite well because it was a major redevelopment of the entire terminal and it was basically a pricing deal that was back to back on that, so it gave them financing security and surety; it gave everyone some surety around price paths. Most of the debate was around the risk sharing because it's such a long-term arrangement, but a very long-term agreement was reached.

Adelaide Airport is another one, five or six years ago; it's a little bit older now. That was a 15-year pricing deal. They're pretty much the examples that are there. Otherwise there's pretty much a five-year cycle that every other airport wants to run with and typically stays with. It does get discussed at various points but ultimately it still ends up pretty much focused on the five years.

MR SUTTON: Just one last quick matter from me on a different kind of matter. Landside access, land transport access issues to the big airport, so it was something

we're required to look at in our terms of reference, are you in the loop on that? Are you being consulted? What concerns have you got? I know Qantas have got a lot of issues on its plate and I'm sure it probably doesn't rate that high, but for us, it's a key issue at some of the big airports. Is there anything you want to say on that?

MR SHARP (Q): If I come back to that productivity discussion that we were just having, if people can't get to the airport, you've got a major problem. Airports generate a lot of things. They generate jobs, there's tourism, there's flow-on benefits to the economy, they're an economic engine - often referred to - and the question is, at what point is the road infrastructure really there specifically to support their assets and their business partners et cetera versus a community asset that needs to actually provide access for the community to get to that particular area?

There were some interesting observations made in your draft report around a couple of airports that kicked the tin. Canberra Airport had to contribute a little bit to actually get some exits off main freeways. Brisbane has spent a lot of money on roads internally and actually contributed some land to facilitate, so there are some examples where it's blurred a little bit. Our view is quite strongly that the economic benefits flow quite significantly from airports. Typically if you were building somewhere, there would be builder contributions or development contributions to local councils. We believe the airports, given the sheer size, pay large amounts of revenue already to the councils and generate a very significant economic benefit to the state. So as a consequence, those road infrastructures leading to the airport are state responsibility.

Are we involved in that? We've been lobbying in Canberra for some time about improved coordination of planning between local councils, state, federal and the airports. We constantly see development activities encroaching into airspace, getting closer and closer to airports. There are some significant issues around that. That's been our primary interest to date. But from our perspective, we have raised these issues with state level in particular; the Sydney rail system is one. There's been some really interesting developments where recently they took some charges off Mascot railway station and tripled the number of people coming through. So there's definitely productivity issues, pricepoint issues, planning issues.

DR CRAIK: Rob, one question: yesterday we had some people discussing the issue of noise and aircraft and it was particularly in relation to Sydney Airport. We were told that these new so-called quieter aircraft aren't really quieter at all; they might be one or two decibels quieter. Maybe being an airline person - and it wasn't from the airlines that we got this yesterday - can you enlighten us as to how much quieter they are?

MR SHARP (Q): Yes. There's specific statistics on those. New aircraft are designed for noise reduction, principally driven by environmental legislation in

Europe, in the EU and the US. There's largely two manufacturers so therefore they target that. London Heathrow has had noise issues for many years and they basically keep reducing the level of noise that aircraft can make, so it fosters new aircraft coming into those airports. Off the top of my head, I haven't got the statistics, but they are very large reductions in the actual noise.

DR CRAIK: So not just one or two decibels.

MR SHARP (Q): No, you're talking 30 to 40 per cent reduction. I was responsible for bringing the Airbus into Australia and one of the interesting analyses that came out of that was the actual footprint of noise. Aircraft tend to take off much more rapidly. The actual engines have got noise acoustics now designed into them. So the actual footprint of the noise tends to stay largely over the airport as opposed to spilling more and more out over the cities.

As a resident sitting right underneath the runway, the question becomes one of, "I can still hear it, so therefore it's still noisy," and that's a debate that needs to be had in terms of efficiency because these newer aircraft also burn less fuel. Typically there's ground power now used on these aircraft so you're not generating nitrous oxides around the runways or the taxiways, which is one of the key pollutants. So there's lots of good environmental messages there. Certainly we're happy to send through some statistics straight out of the actual technical registers that the aircraft manufacturers prepare. They have quite specific testing in live environments on those.

DR CRAIK: Is it at all an issue - this is again in relation to Sydney and I think Adelaide as well - for the curfew hours? There are lists of specified aircraft that can land during those hours, but they're actual specified aircraft as opposed to a noise performance based thing. Is that a problem in terms of updating of modern aircraft or restrictions on - - -

MR SHARP (Q): Aircraft technology, just because of the sheer cost of fuel and the community concerns around this, it's going to be an ongoing development, so you will have an aircraft type but it might have a different engine on it which is more efficient and quieter. So how do you actually manage those? So there's a lot of complexity around it. The other complexity is that often the models use contour lines, so you may see a picture of an airport and you see these lines, a bit like a weather map, showing when noise comes. Because that's actually on a bit of paper, people go, "Well, actually I'm outside of that line so therefore I'm not impacted." The reality is that there's still noise there, but it's below some technical line.

DR CRAIK: Yes.

MR SHARP (Q): So from a planning perspective it gets very hard to manage

perceptions around this. My personal view is that there needs to be facts on the table. It's very emotive. There's a lot of environmental benefits and new technology that can be deployed to assist in delivering that, but because of the complexity around noise in particular, it's a very hard message to get out there. As an industry, we're working with Airservices Australia to look at how do we actually communicate that. There are industry forums already in place, that's certainly one avenue, but as the general public only hears of this on occasions with headlines, it's very hard to communicate the complexities. We certainly see some advantage from a productivity perspective and noise to head down that path and a lot of it is around communication.

DR CRAIK: Okay. Thanks very much. We look forward to your submission.

MR SHARP (Q): Yes, apologies that that hasn't arrived on your desk.

DR CRAIK: Thank you.

DR CRAIK: Now, if Eric Wilson and Keith McLaughlin are here. If you could both state your names and positions for the record, then if you'd like to make a brief opening statement, we'd be happy to hear from you.

MR WILSON: Yes. My name is Eric Wilson, representing myself. I've got no position.

MR McLAUGHLIN: Keith McLaughlin. I'm a director of a company involved in the property.

DR CRAIK: Thanks.

MR WILSON: Basically I just wanted to, if I may, run through, I guess from Keith's experience but from a bigger perspective, to back up some of the things that we put in my reply to the commission regarding road access. The McLaughlins, I guess, have lived through three different phases of Melbourne Airport. The first phase was when it was being run by the Civil Aviation Authority, the second phase by the FAC and the third under privatisation with an airport lease there, so they have had a broad range of experiences.

Under the original running of the airport by the Civil Aviation Authority, that was a regulatory-based scheme which allowed for business concessions to be made; the greatest concession a contract could be was about three years. It was surprising to hear under a fully privatised system the airlines were only typically getting a five-year deal when under the fully regulated system it was a three-year maximum. But obviously three years is only enough if you want to run a cafeteria in an airport or something like that. If you want to do more, you need more dealing power with the airport than three years. So the airport moved to be a corporatised model with the FAC and finally it was privatised.

I just want to run through some of the initial policy settings to start with. I did have some things here to show you. I might first start off by handing out a picture, if I can just hand that up. I've got another one too. This picture is an aerial photograph I've taken from Google. One is the area surrounding Sydney Airport, the other one is a picture of surrounding Melbourne Airport. There's quite a difference in the productivity of the land surrounding the airport, as you can see. I would characterise the land surrounding Melbourne Airport to be a lot of green acres. There's actually hundreds of acres of undeveloped land. There is lots of bushland as well, a state park, national park. There's a lot of farmland. But certainly you can see from that photograph - and that's what I'm going to be driving at with my presentation today - about I guess driving productivity from the land surrounding the airport which involves interfacing with that airport.

So if we start off from the policy settings originally set by the Commonwealth

over Melbourne Airport, the initial policy settings - I have some notes to hand out if you're interested or I can just run them off and we can hand them up later. It's up to you.

DR CRAIK: Why don't you give them to us later?

MR WILSON: Okay. To start off with, the Commonwealth built the airport in 1959 and decided to take advantage of state planning authorities as a policy. Instead of buying buffer zones around the airport to reduce noise, they said to the state authorities, "You guys just don't rezone and when you are going to rezone, tell us about it and then we'll make an acquisition before the rezoning happens so we can get the land at a good price." That was the Commonwealth's policy.

The other policy the Commonwealth made was - they understood that the freeway around Melbourne Airport had what they called a sterilising effect on the land that was to the east and north-east of the airport. That is where the double-lane freeway goes. You can't get through to the airport. So anything that is to the north-east of the airport would become unproductive and as a result, the Commonwealth made it their policy that they would run the freeway around the very edge of the airport and Sunbury Road also in order to minimise the sterilising effect of the freeway that was proposed in 1960.

The idea was that it would be given back to the state. As Qantas said, it was policy back then that roads of access are the providence of the state. However, in a 1962 cabinet submission, the Commonwealth minister stated that the airport freeway would be retained by the Commonwealth around the airport land. I believe that would have been because they didn't want to open the freeway up because access to the freeway into the airport would allow the land to be developed around the airport which means it couldn't be acquired, it would be rezoned. That was the policy of the day in the Menzies government.

It hasn't really changed that much. We move into the time of deregulation which was in the late 1980s. When the airport was deregulated, it became a business of the FAC. Suddenly the restrictions dropped away on the three-year contracts and that type of thing. But what happened was that the FAC got involved in opposing the rezoning of land surrounding the airport to make it more productive. In the McLaughlin case, which I obviously know the best - and I will refer to other matters soon - but in that case, the FAC said that their land should not be rezoned, it should stay for sand mining and not be rezoned for commercial use that would compete with the airport.

I've already given the commission in my submission the FAC's reasoning where they calculated the cost to them of keeping Hertz on their land, the cost to them of leasing from the McLaughlins and subleasing to Hertz and the cost of

acquiring the McLaughlin land and then leasing to Hertz that acquisition. None of the FAC's proposals was to allow the McLaughlins to compete. That was simply not an option. So as it happened, they priced the access in such a way and made the conditions so variable and indefinite that Hertz went to the airport land, not the land surrounding the airport.

So what then happened was there was a land use study in 1992 which is recognised in the 2008 master plan today and that recognised the sterilising effect that the freeway was having. The report said, "Questions of access across the Tullamarine Freeway must be resolved," and that was in 1992. That report is referenced in the 2008 airport master plan. So the question is: how do we get across the freeway so that all that land - and there's hundreds of acres of undeveloped land - can be productive?

What happened was Keith McLaughlin approach the FAC's Bob Young with that report and his file note was that they would not assist in any shape or form; the FAC's reason was, "Because we would be competition to them." So very clearly the land surrounding the airport and the freeway access, if there was better access to the freeway, it would unleash a lot of productivity with that land. The short-term goals of the airport, though - I mean, they have got big interest bills to pay, they've got money to give to their shareholders. Ultimately unleashing all the land around the airport would, I believe, increase revenues for the airport with the increased industrial use and that kind of thing, but it's a long-term gain and they have to deliver next year a profit. They have to pay their interest bills today. So it's very difficult without the full benefit of the law to be able to enforce on an airport lessee that you must open up the freeway and let competition in from competing land nearby.

In any event, the FAC itself was slightly receptive to this need and they produced a terminal and precinct study in a draft master plan in 1993 which showed at Victoria Street, which is near the McLaughlins' land, a crossing of the freeway, so a lot of business could start dealing with the freeway, they could start competing with carparking but also with freight and all the other facilities that was going to be built on the McLaughlins' land.

However, something else happened in 1995. The FAC started to invest in carparking and they built at carpark which was at the time criticised by the Public Transport Users Association. They said it will be a lock-in, that we'll lock in road transport, as in cars, and delay for many years, if not forever, the possibility of a public transport link to Melbourne Airport. That's what they were complaining about in the mid-90s.

So then comes privatisation. By law, many of the FAC staff under Part 9 of the Airports (Transitional) Act had to be transferred to the privatised airports. So you have this mentality of, "We own the whole thing," the same mentality that Keith and

Norma encountered with the FAC. It came straight into the new privatised entities through this piece of legislation.

In my submission to you, I give the calculations that were done by a man named Tim Cullinan and he calculated how much different access routes would cost and how much it would cost Hertz if they went the long way round, the seven-kilometre trip, how much would it cost if they got direct terminal access, which existed at that time.

This was the decision-maker who'd worked this out. This was the decision-maker who was working inside the Melbourne Airport lessee when it came to cutting the terminal access altogether from the McLaughlins' land. So these people knew what they were doing, they were fully aware, not only through the fact that the master plans acknowledged the issue of the freeway crossing through the 1990 studies, not only the fact that the FAC's master plan had a freeway crossing pencilled in there, but also because the guy, the decision-maker had actually done the calculations to work out how much it would cost the McLaughlins if that was cut off. But they did it anyway.

The other fellow who had said he was not interested in helping in any way shape or form, he ended up being the person who worked for the airport lessee who filed the contamination scare with VCAT against the McLaughlins' development plan. So the same kind of mindset continued on. It's only recently that the government has started to say, Well, we're going to have a bigger say in what happens on the land side part. For many years it was just laissez faire, "You can do anything you want." VicRoads, though, has been raising the issue of the landowners surrounding the airport, and I've got a letter for you to look at that.

All of this, what I'm making, I've got letters and correspondence, you can check. They made it conditional in 2003 that the approval of the airport lessees Apac Drive extension, which looks like it's starting construction now, was made contingent on solving access issues for the northern landholders. Then after that, though, in 2004 there was a limited access proposal for the surrounding land which connected Western Avenue - which was where the McLaughlins' land was connected to - allowed that to have freeway access. However, the idea of an actual overpass over the freeway to let all this land be used - the report the McLaughlins got back from their road engineer, who got it through back channels through VicRoads, was that the airport lessee "would not be doing that for some time".

Then in 2008 the Hume City Council proposed another freeway interchange, and I'll give you the map of that because it shows quite convincingly what's involved. The proposal is for a big double road to go right the way through and connect - yes, this is the E14, and on the big sheet there is a red dotted line and you can see that's the road network they wish to bring in, and the blow-up behind it shows you how it

crosses the freeway, allows access to airport, a very large arterial road which they want to build to bring industry into the airport area. That was what they were putting up in 2008.

DR CRAIK: This is the Hume City Council?

MR WILSON: Yes, that's right, that was Hume's idea in 2008. By way of comparison, the minister was getting a few complaints and he asked for a ground transport plan to be made by Melbourne Airport, and I will give the commission just an extract of that. I would like to point out what actually was proposed by the airport. I might give one more plan as well. No, I've covered that. This is the ground transport plan. There's a flow chart on the third page of the extract, in the middle of the flow chart it says that they consulted with state authorities and local councils.

But when you actually look at the road proposals on the third page you'll find that this sterilising effect is still there, because there's no proposed access for the north-east of the airport. We're really back where we were in the days of the policies of the Menzies government when they were building the airport. Keith informs me there's 500 acres of land at stake that's unproductive because of this access issue which has been officially recognised since the mid-90s.

DR CRAIK: I'm just having trouble relating this new plan to the E14 proposal.

MR WILSON: Okay, I'll just give some clarification. I should have split them up; you were right, Keith. It's here. I think it's just a matter of orientating the two maps to compare. Yes, they're different scales and different types. But what I'm keen for you to see is that - you can see in the Hume City Council map there is Melbourne Airport and you can see there is the terminal area, you can see Melrose Drive going into the terminal area of Melbourne Airport on the Hume map. Now, you can track that by Melrose Drive going into the terminal area in the airport's map. So that's sort of the idea of where we're at.

As you can see, the airport's red dotted lines are not leading to the east and the north. There is no access going across to allow people to get in from that side of the airport, and in fact their road network map, you can see the road network is quite sparse in their portrayal of it. It's still in effect sterilised by the freeway, that's having a sterilising effect, which was the Commonwealth's terminology in the 1950s. So that land is being held back.

The interesting thing about - at the top of this ground transport plan it says, Transport Network Improvements. So this is actually the projection that they have in the future. So in their transport plan there is no provision to release the potential of the surrounding land to the north-west. The sterilising effect of the freeway actually

works for the competitive advantage of the airport, because it means that you have to use their land for whatever you want to do. Do you want to spend some time - - -

DR CRAIK: No, that's fine.

MR WILSON: That's all right?

MR SUTTON: Can I just ask, this latest ground transport plan, what's the status of these two documents? The earlier one, the Hume one, has fallen away, it's on the shelf? This one is proceeding? Are these live documents?

MR WILSON: I can't tell you what the status of the Hume one is because when a council makes a thing like this it really depends on lots of approvals from different places and whether it goes ahead or not is a long process, it takes years, and they need to get the cooperation of VicRoads obviously to get into the freeway there; and it looks like that particular proposal went across some Commonwealth land, so they would need approvals from the airport.

MR SUTTON: So you don't know if that idea is - - -

MR WILSON: It might have gone by the bye. All I'm saying is that there's lots of different proposals over the years to get across the freeway, lots of them - - -

MR SUTTON: What about the Melbourne Airport ground transport plan, has that got momentum or not?

MR WILSON: That was requested by the minister in 2008 and you can't really rely on it, because as I've included on the front cover, it has got a big disclaimer on there saying that - well, you know, on page 2 it says that "Accordingly, the recommendations detailed in it are indicative only".

MR SUTTON: Okay.

MR WILSON: There were arrangements that I will give you in the documents which seem much firmer than this, where VicRoads required an access point into Western Avenue as a condition for which they would allow the airport access into the freeway with their new on-ramp - off-ramp, I should say, and on-ramp to the freeway. So things look solid and then they disappear, and that is part of the problem. If you don't have a solid road network you won't get investment around the airport, it just can't happen.

DR CRAIK: I guess we're sort of beginning to run short of time.

MR WILSON: Yes, I'm almost there.

DR CRAIK: Thanks.

MR WILSON: The final thing I guess is that the final act was that the airport lessee has a massive advantage here. When they acquired the McLaughlins' land - we now have confirmation from the Titles Office that the easement is unregistered now on their land, so the Western Avenue access is no longer attached to the land's title, and there is a note on the title now that says that their land's access is now from Sunbury Road. So the very thing that the McLaughlins were fighting for 20 years or so - and they believe they had the rights, they just didn't have the financial ability to enforce their rights they believe - the airport has done for themselves with the stroke of a pen.

Obviously there's an injustice there and all of that, but really it just shows you the tremendous advantage they have: they can do this with the stroke of a pen, where the landowner outside the airport, not a hope, because there's so many proposals that have happened, they just don't come off. This is not a pricing issue. Unless there's more teeth in the bottom layers of your pyramid, which is what I'm making in my submission, it's just impossible for people outside of the airport to compete. The airport is quite profitable, it should compete on its own two feet without the use of Commonwealth jurisdiction, without the use of Commonwealth power, it should compete as a business, and the McLaughlins found it doesn't, it has this great capacity to hit out without being accountable.

DR CRAIK: Thanks, Eric. Thanks, Keith. You've certainly had a long and incredible saga on this one. But thank you for all the documents.

MR McLAUGHLIN: This was 23 years.

DR CRAIK: Yes, I know.

MR McLAUGHLIN: 23 years. But the whole thing was they were not going to let us operate. We could have put a 600-car park building in there and would have been half the price of the airport and we're only 250 metres from the terminal.

MR WILSON: How many cars, Keith?

MR McLAUGHLIN: 600.

DR CRAIK: Is there anything you would like to recommend? I mean, this is an inquiry about economic regulation. Do you have, like, a particular recommendation for the PC on this?

MR McLAUGHLIN: The only body we finally got some help from was the AAT.

I believe that in property matters and access matters I think the AAT should be given more teeth to be able to do something.

DR CRAIK: When you say more teeth, what precisely - - -

MR McLAUGHLIN: Just because they can sort of just put this recommendation to the airport but they can't enforce this. They get the master plan and then they dropped all of these things out of the master plan, so we went back to AAT and said, "Look, all these things have been taken out," and of course they didn't know it was taken out. Then of course we had another hearing, and then they made a demand on the Melbourne Airport and the minister had approved it and he shouldn't have approved it, and so it goes on.

So unless the AAT - we believe they were the ones that helped us as much as they could, and we thought if they could have a bit more clout, because the actual president of the AAT said directly to the airport in the hearing, "You know what you've done, don't you? You've depreciated the property of McLaughlins by taking out that Quarry Road, ripping it up." The whole thing stalled there.

DR CRAIK: So what you're saying is that the AAT made a decision but it has not been enforced anywhere. Is that what you're saying?

MR WILSON: Not quite. The AAT only has powers that are defined by the act and parliament has got to give it that authority. It really only considers things in an administrative capacity, not like a court.

DR CRAIK: That's right.

MR WILSON: So that means that unless things are really spelt out in the act very, very clearly, you're really asking the AAT to stick their necks out.

DR CRAIK: Which the wont do - - -

MR WILSON: Which they don't do.

DR CRAIK: - - - beyond the powers of their act.

MR WILSON: They can't do it, especially with the airport. They stuck their neck out for Kevin Rudd and the Federal Court slugged them, you know. So it has got to be spelt out in the regulations and in the act what the required behaviours are. You know, things such as that the airport has to comply with legislation, which is one of the things I said should be put in as part of the master plan criteria, which gives people a ground to say, "Hey, what they're doing isn't lawful. We want to go to the AAT on that," but instead - - -

DR CRAIK: So you're talking about amendments to the Airports Act?

MR WILSON: Yes, indeed, and I've got that in my submission.

DR CRAIK: Yes, you have.

MR WILSON: About what I think is needed. Also I think there's something that's just wrong with the whole system, in that when you deal with the local council in a state you deal with the council and if you don't like what they say you can appeal it, and the minister only gets involved in things he wants to get involved in; but the way the Airports Act is set up is that the minister is dragged into everything practically, almost, he is really quite hands-on and he's supposed to be impartial.

He's in a terrible position, he has to have the airport lessor hat on and he has to have the I'm-the-Crown, I'm-impartial hat on at the same time. So there's commercial interests for the Commonwealth, which means budgetary problems if he does one thing, there's lots of complications for him, and I think there needs to be a separate authority, a planning authority for at least the land side of airports, so that things can happen in a way that is a lot more regular, because at the moment it's hotch-potch. There's regularity in planning in the states, but as soon as you cross the border into the Commonwealth territory you're in Indian country. That was Keith's experience.

DR CRAIK: Thanks. Well, we'll take that on board. John, do you have any questions?

MR SUTTON: There's a lot of complexity in this, but, if I understood you correctly on your point about where the major roadways access the airport, you have a view - correct me if I'm wrong - that at some stage, perhaps a fair while back, the freeway should have gone round to the western side of the airport and the benefit there would be that would open up that land to more productive purposes. Is that - - -

MR WILSON: Not quite - - -

MR McLAUGHLIN: Not quite. No. But they shouldn't isolate - use the freeway because they control the freeway.

MR SUTTON: Who is they?

MR McLAUGHLIN: APAM.

DR CRAIK: Melbourne Airport.

MR McLAUGHLIN: See, APAM, when they first came into the saddle in 1998, they were asked by, I think it was, the minister, "Would you give the land back to them that VicRoads had built the road on," and they said, "No." So they were able to veto that, and by vetoing that then they actually ripped our road up and that gave no access all the way through to Mickleham Road.

MR WILSON: So the freeway really needs crossings.

DR CRAIK: So the whole Tullamarine Freeway is controlled by Melbourne Airport, is that what you're saying?

MR McLAUGHLIN: Yes, it is.

MR WILSON: Yes, and Sunbury Road to the north of the airport.

MR McLAUGHLIN: We had the road for 30, 40 years, but they came in with bulldozers and ripped it out.

DR CRAIK: Mm.

MR WILSON: It's actually the crossing of the freeway that's the issue. Where the freeway runs is not the issue. There's an underpass that was cut off. You could go through an underpass into the terminal precinct. That access was cut off. But over the years there was another access at Victoria Street that has had many different configurations proposed over the years but it never happens, and I don't think it's in the airport's short-term commercial interest that it does happen. So getting it through the Commonwealth side of the fence is incredibly difficult.

MR McLAUGHLIN: I think that's basically all it needs. If that overpass went in that would release - on the land map there's about 500 acres from that side right up around the Mickleham Road.

MR SUTTON: Keith, you've sold the land now.

MR McLAUGHLIN: We have, yes.

MR SUTTON: You're here more in the public interest, as it were, rather than - - -

MR McLAUGHLIN: We just believe there should be - we've had 23 years with it and we thought it is a real point where there's some attention that needs to be put to it.

DR CRAIK: Okay.

MR WILSON: The Commonwealth has power to make easements over the land. Ultimately if the state said, "We want a road here and we're going to lead it to the fence of the airport," the Commonwealth can say, "Well, it doesn't conflict with the master plan, or not one that the minister is going to approve," and if the airport ultimately doesn't do it then the Commonwealth can grant an easement and make it a property right. Now, that's a really bad way to do it, I think, but ultimately that sanction is there. The problem is the departmental policy that has come down from the Menzies era where really those principles of, "We control the freeway, and we wanted to depress land values around in case we wish to acquire," that's got to go, because when you analyse what actually happened to the McLaughlins, it's actually those three departmental policies way back in the 50s that's still alive.

DR CRAIK: Carried on.

MR WILSON: Yes, carried on from the Civil Aviation to the FAC and those guys went straight into the airport leases. It's a cultural thing. That's why in the recommendations I've also said it's got to be a departmental policy here, not just a legislative change, where the department suddenly becomes focused not just on aviation but on the land surrounding the airport also.

DR CRAIK: Okay. Thank you both very much for coming in and for all the paperwork and everything you've sent in. We'll take it on board. I'm not sure the extent to which we can do anything because we've acquired bad economic regulation, but thank you.

MR McLAUGHLIN: Thank you for hearing us.

DR CRAIK: We'll now break for lunch and we'll resume at 1 o'clock.

(Luncheon adjournment)

DR CRAIK: Thank you very much. If you could start by stating your name and position for the record please, and then if you'd like to make a brief statement we'd be happy to hear from you.

MS MATHER (SACL): Thank you for the opportunity to participate in these hearings, but before I do give a brief summary of our position I would like to introduce myself and my colleagues. My name is Kerrie Mather, I'm the CEO of Sydney Airport.

MR FINLAYSON (SACL): Tim Finlayson, the CFO of Sydney Airport.

MR KAMERON (SACL): Luke Kameron, I'm responsible for regulatory affairs.

MR FANNING (SACL): Nigel Fanning, I'm the airline commercial manager for Sydney Airport Corporation.

MS MATHER (SACL): In preparing for today I reflected upon my experience as CEO of MAp Airports for the past decade, and my more recent experience as CEO of Sydney Airport. Over this period, the aviation industry has changed remarkably. From my perspective the most important change has been the increase in global competition between airports due to the growth and development of low-cost airlines, the increasing importance of the Middle East and Asia, and the strengthening of airline alliances.

Airports that were once perhaps local monopolies now clearly compete globally for the deployment of aircraft that can be deployed anywhere in the world. In fact this week we have a team from Sydney Airport that are in Berlin at a conference where delegates from almost 600 airports are competing for increased capacity from around 300 airlines. This change has taken place against a background of increased risk for airlines and airports arising from both natural and man-made disruptions, as well as ever-increasing regulations governing safety, security and environment.

At the same time, airports remain complex in their own right with extensive operational regulations, long-term investment horizons, multiple interdependent businesses and conflicting priorities between different customers that are competing with each other. The combination of technological change, increased competition and risk and business complexity requires a visionary, proactive and long-term strategy from airports. My approach has been to listen to each airline and endeavour to deliver to them through collaboration and innovation, while retaining flexibility, to respond as their needs change.

Airports can and do enable substantial benefits to the community and airlines through the efficient and innovative provision of the infrastructure and services to

airlines and other users. Enhancements to these facilities and services are far more important to the success of airlines than airport charges which typically reflect less than 5 per cent of an airline's costs. Even Sydney Airport's centralised procurement of in-flight traffic data and centralised supply of power and airconditioning save the airlines the equivalent of 3 to 4 per cent reduction in airport charges.

There's relatively little focus on areas that are more meaningful, such as the cost of delays and reduced economic activity resulting from the over-growing operational regulations and inadequate use of new technologies to improve operational practices. In fact the regulations governing Sydney Airport are more onerous than those applying to any of the other top 50 airports in the world. Also there's little focus on the direct and indirect costs of travelling to the airport, such as congestion.

I welcome the balanced and objective approach taken by the Productivity Commission in the preparation of its draft report which recognised the reduced potential for exploitation of market power arising from increased competition; the strong investment outcomes under the light hand of regulatory regime, both compared to the previous regime but also other industries; the lack of evidence from misuse of market power in rates of return, airport charges, service quality, carparking or ground access, refuting in fact all of the concerns of the ACCC; the incorporation of additional features requested by airlines in commercial agreements, and the importance of improving public transport and road access to the airports generally, but particularly to Sydney Airport.

These are the types of investment and service benefits expected from the introduction of private sector innovation and commercial behaviour. As we noted in our submission, Sydney Airport has invested almost \$2 billion, increased passenger service levels and negotiated increasingly airline specific agreements with all domestic and international airlines. In fact we've also recently negotiated individual agreements with several international airlines covering the period up to 2017. At the same time the evidence is clear that Sydney Airport has not earned excessive profits and that prices have only increased in line with investment. We've averaged around 8 per cent, well below many of our competitors and, by any measure in this environment, a reasonable WACC.

I don't believe there's any need for conjecture about why there's been no action, is because of the numbers in the ACCC reports demonstrate the good behaviour of airports. The current health and competitiveness of the Australian aviation industry would also seem to be a testament to the success of the progressive privatisation and deregulation of the airlines and airports over the past two decades. In this context it's difficult to see how any additional regulations could be justified. The purported benefit of curtailing excess of profits is demonstrably unnecessary. Set against this, additional regulation would have significant costs, including to investment,

innovation, differentiation and flexibility. Any additional regulatory risk is likely to deter investment, as your draft report recognises, due to the reduced ability to attract debt financing, investor uncertainty and the effort involved in following regulatory processes.

Market disruptions caused by events as diverse as the GFC, terrorism and weather events periodically make investment very difficult. Long-term regulatory risk at these times might make investment impossible. Perceived regulatory risk will increase from the moment any regulatory review process is publicly announced, whether that be a show cause or Part IIIA announcement. The perceived risk will be higher, to the extent that the review inquiry is recommended and conducted by an authority which has apparently already reached the conclusion that it should have an increased involvement in setting prices.

Innovation, differentiation and flexibility are all necessary for us to deliver our customers the different experiences they want in the future, and all of them are easily undermined by standard regulatory models which treat all customers as if they were identical and often commit airports to fixed five-year plans. It seems to me that the greater urgency is to reduce the impact of the existing regulations, both economic and operational. Too often the legacy of the historic cost recovery regulation is to focus airport-airline negotiations on whether the airport is permitted to recover its cost of capital rather than maximising the benefit and negotiating a price between the airport's cost and the airline's benefit. This can easily result in sub-optimal investments.

As noted in our first submission, Sydney Airport is subject to at least 18 different airport-specific Commonwealth government acts or regulations, which have grown larger over time, and our partners are subject to many more. All of these regulations result in both costs and benefits to the community. Given the changes which have taken place in the industry and the incremental way in which these regulations have accumulated, I believe there's potential benefit to the industry and the community if some of the acts and regulations were made more contemporary.

Even without changing the regulations, the damaging impact of the existing monitoring regime could be reduced if the monitoring reports were required to meet the general principles set out in the draft report for show cause process. It seems entirely reasonable for airports and other readers to expect the analytical conclusions in these reports to be robust and transparent, explicit and definitive, not reliant on any one year or specific time period, concerned with consistent patterns of returns, benchmarked against a reasonably expected band of outcomes and have regard to price, investment, quality and market conditions.

Turning to land transport, I'd like to once again call for improved public transport to the airport, and in particular cheaper rail fares and more bus services, and

for additional road capacity to meet the needs of commuter and Port Botany traffic currently using roads provided by the airport. Better public transport will benefit passengers, end the discrimination against the 17,000 staff that work at the airport and significantly reduce the amount of investment required in roads by the state government. So that ends my brief opening comments. Thank you again for the opportunity to speak, and my colleagues and I would be happy to take any questions.

DR CRAIK: Thank you, and thank you for your submissions. I guess the first question I'd like to ask you is you may be aware that the new chairman of the ACCC made a speech - I think it was last week, or the week before - about monopolies and regulation, in particular in reference to airports. Do you have any comments on that that you're aware of?

MS MATHER (SACL): I think it's very early days, in terms of his appointment. So I assume that he's actually picked up the historic ACCC position. Just coming back to Sydney Airport's track record, I think the results speak for themselves. We have earned a below-average WACC on any measure, so there has been no evidence of misuse of market pricing; and we have got extensive commercial agreements in place with all of our domestic and international airlines.

DR CRAIK: I don't think you were here, but some of your colleagues were here this morning when we had Qantas and Virgin speaking, and both of them were keen on what amounts to deemed declaration of at least tier 1 and tier 2 airports, possibly even more, and Qantas suggested a mandatory code of conduct, which would mean I guess it would have to be signed off by the ACCC, which would provide guidance on things like the range of values that various parameters could fall between.

We were trying to extract from them, you know, are there particular airports that they have difficult negotiating with, and it was very difficult. I mean, basically it was across the board essentially, all airports caused them significant problems in terms of reaching a balanced position. I just wonder if you have any response to all that. We're getting kind of one message from airports generally, and then we get a kind of very different message from some of these airlines.

MS MATHER (SACL): It's difficult for me to comment on other airports, but certainly in respect of Sydney Airport, Sydney was only privatised in 2002 and the first commercial agreements were reached in 2007, and I think we would have actually reached agreements earlier than that had we not had a Productivity Commission review actually proceeding in the background. So in a sense it was a bit of a distraction from actually trying to reach a commercial relation. Since 2007 I think what we have seen is a maturing of those commercial relationships. It's testament to the fact that we have a whole team actually dedicated to management of those commercial arrangements and the commercial relationships with airlines. With the passage of the time there has been an increasing number of those commercial

arrangements.

I think to move to a code of conduct would actually suggest a one-size-fits-all when actually with the maturity of our relationships and a regime that's obviously working, which is, you know, turning towards more tailored arrangements for individual airlines based on their need to increasingly differentiate themselves on the ground as well as in the air, we have to be able to respond to that with more tailored, commercially sensitive agreements. So a one-size-fits-all code of conduct would be inconsistent with that.

MR FANNING (SACL): The Qantas initial submission also spoke about the framework that Sydney Airport has in place. So think if you reference the comments in that, it actually talks quite positively about how Sydney Airport engages on the parameters that we use to negotiate new investments, for example. So I think if you go back to more specific examples that they have raised in their initial submissions.

DR CRAIK: It's interesting, the diametrically different approaches.

MR FINLAYSON (SACL): Can I just maybe pick up on that. I wasn't here for the first one, but I was here for the Qantas discussion. I actually took away more the fact that they had concerns around regional, which is outside the terms of reference here. That was a particular issue. There had been issues raised I think that relate to Jetstar within the Qantas group. They are a low-cost carrier, they do spend a lot of time actually talking almost - sometimes in public around any type of activity, let alone airport prices. So I just want to make sure that that was sort of put into context there. I'm not sure that they were actually issues that were raised with the Qantas group level.

Also I thought that they said that deemed declaration was probably a last resort for the approach in there. So I think there is a recognition of the commercial agreements and relationships we have got in place, and that's at my team's level, which is the commercial relationships, but also then the escalation points up to CEO and otherwise that are always there in any type of commercial relationship.

DR CRAIK: I know you're not enthused about the show cause proposal that we have. Our view is that right now the monitoring reports are published, the ACCC draws some implications from those monitoring reports and makes suggestions about abuses of market power and indications, and, you know, these kind of slightly vague words, and in the media in particular, but there has been no reaction to these reports either by the ACCC, if they suspect that there's an issue, or by the government. The intention of our show cause was really to lead to some kind of determined response to these reports.

So that if the ACCC does have real concerns about potential abuse of market

power there's a path that's to be followed. So that was a lot of the rationale for the show cause process, to make the whole possible sanction actually credible. I know you're not keen on it, but if we did pursue it - and you've raised the issue that you think it should be confidential because of the concerns in the marketplace, the regulatory use of raising funds, et cetera - is there a problem if you're a listed company though? You would have to notify the ASX anyway, so it would become public anyway?

MS MATHER (SACL): Probably. That I think would depend on the nature of the issue at the time. There are quite prescriptive arrangements around how disclosure works. But it's a very good point. I think one of the issues with the show cause is that it has the potential to add a regulatory tier to actually solve a problem which could be solved at source by solving the monitoring, which is where the issue is actually arising from. So by the time you've got a show cause, actually it's quite a long way down the path; you know, the problem has occurred and there's no turning around to actually solve what could have been solved actually at source if you actually had the right monitoring. So I think that actually if there is an issue it needs to be dealt with much earlier in the piece and it could be solved with an effective monitoring regime.

DR CRAIK: We have certainly got some recommendations for improving the monitoring process. We're also wondering whether airports and airlines would see value in when the monitoring report is actually published - the responses of airports to the ACCC in relation to the draft information that is sent to airports is published with the monitoring reports.

MS MATHER (SACL): I think actually having access to the report before it's published as well. So there is access to the facts but not the findings. It's very difficult to review the facts without seeing the findings. So having access to the complete information to have the opportunity to comment prior, I think, is important. Just coming back to the issue around the show cause, I think it actually does add significant risk, it adds potential uncertainty which potentially makes it difficult to actually raise capital. So if we think about what happened to the share price actually when the Productivity Commission review was announced - - -

DR CRAIK: I remember you told us that, yes.

MS MATHER (SACL): Yes, it was a billion dollars it actually took off the market capitalisation of the copy.

DR CRAIK: How quickly did it come back up?

MS MATHER (SACL): It hasn't come back.

DR CRAIK: At all?

MS MATHER (SACL): No. You know, things actually only go one way at the moment. In an environment where you've got a very nervous market, that sort of regulatory uncertainty, it not only affects your ability to actually raise capital in the public market, but, you know, it actually creates uncertainty in the eyes of the banks as to whether there's some underlying problem.

DR CRAIK: One other question about our show cause proposal is we have suggested the ACCC does the monitoring report, the ACCC issues the show cause, then the ACCC makes a recommendation about the VIIA inquiry. Then if the minister says yes, then the ACCC is the logical body I suppose to do the VIIA inquiry. So you've got the same organisation all the way along. We raised this as a potential issue of concern because once they have issued a show cause then maybe there's a view that it's difficult to come to an inquiry without having a pre-formed view. So do you have a view whether it should be a different organisation somewhere in the chain, and, if so, which organisation that might be? We have struggled with trying to think of any other organisation.

MS MATHER (SACL): I think it has to be - this is without suggesting in any way that we're supportive of a show cause process, because we do see it as adding uncertainty and getting in the way of commercial relationships actually directly with the airlines - I think the party has to be independent.

MR KAMERON (SACL): I think our thought was the NCC, for example, undertakes some of the other - I can't remember if it was Part IIIA, Part IVA or both.

DR CRAIK: They do IIIA anyway.

MR KAMERON (SACL): And it would seem why not undertake a Part VIIA, and if they're not currently resourced for it then surely a better solution to allowing a potential conflict of interest to persist in one organisation is to properly resource a second one that could do it. So I think that would be one option.

DR CRAIK: Thanks. That's a good idea. John?

MR SUTTON: Could you just take me through, you say that if the monitoring process was better there wouldn't need to be show cause or any other additional regulatory tools. I'm a little bit troubled with that. That, what, assumes goodwill reigns? I'm talking in general here, across the whole Australian landscape, airportwise, not picking on you in particular. But you just say that will obviate any problems in the future, is that what you say?

MS MATHER (SACL): I think what I'm suggesting - and I might get Tim to talk

about the monitoring, but I think by the time you're talking about a show cause there's so much - you know, with the passage of time it's very difficult for the parties to actually respond appropriately. So our view is that it's better to actually deal with the problem at source by actually having effective monitoring.

MR FINLAYSON (SACL): That's right. I think there has been volumes of data provided to the PC and also to the ACCC about the methodology, about how a more robust methodology can be developed which is actually bound in accordance with international standards, and also taking over a period of time as opposed to taking a snapshot in time. Even the ACCC report, it talks about one year, but it actually takes a snapshot on a certain date, so it doesn't even take a year's worth of numbers in many cases. It is an adequate methodology; we have put forward our positions on that.

We think if there is a development of the proper methodology - and this is combined with the monitoring, including SLAs in there - so we have got the ACI ASQ surveys - SLAs in place that we've got with airlines that carry more than I think 60 per cent of our passengers on an international basis. You combine those, you've got robustness in there, discipline, in terms of the monitoring regime. You actually take it out of the need for the show cause mechanism there, because up-front you've got the right data. Then if there is something later on, then it will fall under the normal regulatory process that's available now.

MR SUTTON: You say those other mechanisms, they represent a credible threat, I take it. You think they are a sufficient credible threat in the marketplace here?

MR FINLAYSON (SACL): We do. At the moment you've got that in there, no disputes have been raised under the agreements we have got in place. We have got agreements in place since 2007, for example, on the international agreements. We're coming up to a new negotiation for middle of 2012 for nearly all of the airlines. We have already put several in place over the last couple of months, so those regulations are there available. We've had the declaration before that wasn't used; again there haven't been the disputes that have been raised up under it. So I think it is a credible - - -

MR SUTTON: Mightn't that suggest - well, two options that come to me. Again talking in the broad, not just concentrating on Sydney. Either everything is pretty hunky dory in the garden - to use a nice, rough sort of language - or those mechanisms that sit there - you know, IIA and VIIA et cetera - are not really adequate for problems that do exist out there. They're the two things that come to me. Basically either things are just fine and dandy, or they're not really a credible threat.

MS MATHER (SACL): From the airport's perspective, they are a credible threat

and a stick, and I think that's borne out actually in the returns that we're generating. There's an incentive to actually promote commercial outcomes, which is driving the extensive nature of our commercial agreements, and in order to have a commercial agreement, it naturally means you're making a concession in order to get there and those concessions are actually reflected in the derived returns that we're getting.

MR SUTTON: Let me pick up on that, because I did ask Qantas before lunch about - you know, they complain, as do the other airlines, about the protracted negotiation process and I did ask them, "Well, why at the end of the day do you sign on? When you're complaining of the process and you're frequently complaining of the outcome that you say you're stuck with, why do you sign on," and their answer is to the effect that, "Well, we have to weigh up a whole range of competing considerations," and signing onto something that essentially they're saying is sub-optimal. It's not a win-win outcome, from their point of view. It's sub-optimal. That's my paraphrasing of their position.

They say that's because there's imbalance in the negotiating power and of course Qantas has presumably got more power as an airline than most others, so if you're another airline, I'm sure you would probably claim there was an imbalance in the power relationship. So airports do say of course, "Well, they voluntarily signed on. We did a fair and square deal," but the position very much of airlines is the lack of balance in the equation means that they are signing on to sub-optimal arrangements.

MS MATHER (SACL): Perhaps that was in the context of the specific examples he was giving, where there was less of a regime, as Tim said, at the regional airports, whereas - - -

DR CRAIK: No, it was actually a general comment that they've been forced to agree, because I wrote it down.

MR KAMERON (SACL): It does seem somewhat surprising that the airlines have been forced to agree to a contract where, when you look back with the benefit of hindsight four years later, the traffic forecasts in the agreement haven't been met, the cost of debt has been higher than was agreed and we made concessions on asset beta and agreed to an asset beta that is lower than, if you look at all the airports listed in the world, the average of that range. So we have made concessions. We haven't actually achieved a return that is consistent with the cost of capital inflate in our share price. So looking at the objective facts with the benefit of hindsight, I struggle to see how the parameters that were agreed were disadvantageous to them.

MS MATHER (SACL): I think in terms of Sydney, remember for terminal 2, that was actually one of our first commercial agreements and actually Qantas were the first commercial agreement that we had, so we bought the airport on 1 July and they

actually signed that commercial agreement on 14 August, so I think that actually was turned around in quite a timely way. In relation to the international, the international was agreed in July 2007, so we're not due for another negotiation until another 12 months away, so I don't think it was specifically a reference to Sydney.

MR FANNING (SACL): Yes, so the prices were set by the ACCC until 2006, so it was basically 12 to 18 months to negotiate the international agreement and that was the first agreement at the time. I think in any commercial negotiation, there's always going to be a sub-optimal outcome for both parties, because we're both making concessions and we're both conceding - - -

DR CRAIK: We did put that to them, "Isn't that what you'd expect in a normal commercial negotiation, that nobody gets quite what they want?"

MR FANNING (SACL): Correct, and I think you would probably have to test them on specific examples and maybe being less generic about the whole industry and talking about more specific examples and specific outcomes.

MS MATHER (SACL): I think the key is what the commercial agreements have actually promoted. So while certainly from an airport's perspective, we've made concessions in terms of the returns that we were seeking relative to what we might have got in a regulated scenario, what it's enabled from the airline's perspective is a whole lot of non-price elements to actually be included in the commercial agreements, so things that were actually a priority for them, so service issues, the way particular gates were configured, particular flows through the terminals. So there were a number of non-price outcomes. These things are never about price. It actually puts those issues and opportunities on the table that you mightn't otherwise get the opportunity to do in otherwise than a commercial agreement.

MR SUTTON: Some price issues they did raise very early on. You have key headline charges that get a lot of focus, but he reeled off half a dozen and I didn't - - -

DR CRAIK: I think it was check-in counters, airport lounges - - -

MR SUTTON: Yes, a whole lot of smaller areas where there are charges that they say are exorbitant, which, because they're not the main headline charges, they go through contrary to what Qantas would say are reasonable arrangements pricing-wise.

MR FINLAYSON (SACL): The airports were privatised very clearly on one basis, which is dual till, so having aeronautical separate from the commercial side of the business. The aeronautical activities are clearly defined in the regulations and everything that's in the aeronautical side is subject to this model effectively we're talking about today. Everything outside really should reflect a commercial return on

our investments, so on the equity and the debt we're putting in there. So all we're actually doing is following the regulations on that side.

MR KAMERON (SACL): I might go a little bit further. That might leave open the, "Well, you've got us over a barrel for the non-aeronautical," but Sydney Airport continues to follow a heads of agreement, as it were, for pricing principles for property-type leases with Qantas that was agreed in 1994 under the FAC. That is still being followed and hasn't been changed.

MR FANNING (SACL): Again, some of those other attributes or services that we're providing, they are very much sort of brand and service driven as well, so it's providing a business class lounge or a first class lounge specific to the needs of those passengers, who are obviously paying a very different fare as well.

DR CRAIK: Can we just go onto the issue of SLAs and monitoring and things. I think you originally proposed that you could dispense with airline monitoring if the airport's record in meeting the SLAs, performance record, was available and published. Not the content of the SLA, so much as the actual achievement of performance, and we suggested a figure - I forget what it is - something like 95 per cent of passenger traffic and 90 per cent of the airlines flying in and you've come back with an alternative, I think, of a lower percentage of airlines and a slightly lower percentage of the traffic volume to give the opportunity to get out of monitoring airlines.

I guess our concern is if the percentage of airlines is low enough, it's possible for airports to say, "We know we'll never get agreement with X, Y and Z," so we'll just include a percentage that will give us the ones that we can agree on so we can get out of being part of the airline monitoring survey. So I guess some discussion about what a reasonable percentage might be in terms of what you guys want, which is probably the minimum that you can get away with, and a monitoring regime which gives a reasonable picture of percentage achievement of SLAs in terms of the percentage of airlines and passenger traffic would be useful. Sorry, that was all a bit garbled.

MR KAMERON (SACL): Just to clarify one thing, my reading of the draft report, I think it was 100 per cent of airlines.

DR CRAIK: Yes, I think that's what we said.

MR KAMERON (SACL): That requires one airline to start flying today that didn't fly yesterday and you've reached it again.

DR CRAIK: I think we've accepted 100 per cent is probably going to be difficult, but I guess what we're trying to do is avoid having Qantas in there or avoid having

one of the really big airlines in those places.

MR KAMERON (SACL): Yes, and I don't know what the right number is either. I think it's got to be well short of 100. You would need to be allowing the flexibility for more than one or two airlines and it's going to be north of 50 per cent and I don't think we have a strong view on where that is. I wouldn't say as high as 95 per cent.

MR FINLAYSON (SACL): I may take it further. If you're putting yourself out there as an airport, and what we've said that we support actually is public viewing of the ACI and ASQ and public viewing of the SLAs. Basically, once you've got that in place and you've got robust methodology, (1) we don't think you need the airline surveys at all, but if you need some sort of hurdle, what is a significant enough amount that is public enough that therefore actually we need respond to that - and quite honestly, it's around 10 per cent. If you've got an airline that's got 10 per cent of the market, we're talking bigger than Cathay, bigger than Singapore, bigger than Emirates, three of our largest airlines coming into Sydney. You aren't talking Qantas group. You get that right and you will apply that across the whole business.

So the reality is, from a commercial perspective, we're not going to go and say, "We'll do a deal over here," so it's 50 per cent of passengers we've got SLAs on and now we don't want airline surveys because the other 50 per cent, they just have to live with it. The reality is, if you've got 50 per cent or even a material amount which is 10 per cent effectively you've got agreed SLAs between the two parties, then you have effective monitoring, I think. So commercially you will actually need to follow up with all the rest of the airlines. You can't just exclude airlines from that, that's the reality.

MR SUTTON: Can I ask you a question about service level agreements that has always troubled me and I will just get your take on it. Airlines advertise to the public because they have the public interface, they need the public custom, they're selling a thing to the public and they advertise, "We're a perfect airline in this way or that way," or whatever. The thing that somewhat I can't get over is why would any airline want published any material that says, "We've got an 83 per cent performance on this, we've got a 91 on that," anything that's out there in the public domain that says they are less than perfect just seems to me to represent a danger to their public message, their advertising. So from my point of view I can't see why they would want any of that material published but that's me and I probably don't understand the industry enough. Can you comment on that?

MR KAMERON (SACL): That's I think precisely why what we're not proposing would be we publish the details of, "Here is what the target is with Qantas, with Air New Zealand," or whoever on each metric and what is actually being achieved because we don't think that and Qantas said the same. That's not something the public need to know and Qantas doesn't want - - -

MR SUTTON: What would be the utility of what you put up otherwise?

MR KAMERON (SACL): From a regulatory perspective, I think the main thing the general public wants to know is that we actually have got agreements with our airlines and we are doing our best to meet them and actually we're achieving most all of those standards because the sort of things they're talking about is - on-time performance is something a passenger might care about but the aerobridge is out of order for 10 minutes is not something a passenger cares about unless it causes them an on-time performance issue. So what we would be talking about is, okay, the electrical system was operational 99.9 per cent of the time is the KPI, yes, we achieved it and what would be reported would be - and this is something the airlines and airports need to actually decide what is the appropriate reporting - but we've got electrical system based on an availability, there's KPIs in place with most of our airlines and we're meeting the KPIs or we're failing to.

MR SUTTON: I might go onto a couple of other things. We asked the question about whether non-aero revenues act as any kind of constraint on aero prices or charges and revenues and we got what I find to be a very interesting batch of answers from airports. How do you answer that one?

MR KAMERON (SACL): I think we answered this in the submission which you received and I imagine is coming up shortly. Sorry, I've had a mental - - -

MR SUTTON: Do non-aero charges constrain aero charges?

MR KAMERON (SACL): I think there are two things. There is a natural impact of non-aeronautical businesses in reducing aeronautical charges just by the sharing of assets. If you built an airport with no retail, with no airline lounges, the entire corridor would be aeronautical. As it is a portion of that corridor is actually treated as non-aeronautical and the overall airport charges are lower. So that happens automatically. In terms of otherwise, there are incentives offered to help grow the business and I think it's akin to Virgin this morning who, on the one hand tried to argue that air fares are basically elastic and as a result of which if our charges go up the community loses because passenger volumes go down and, at the same time, tried to argued they were inelastic and it was a small proportion and various other things.

The reality is, for some passengers they're elastic at some points in time and at other times they're more inelastic. One particular point of which they are elastic that is separable is for a new market that is being opened. So for things such as a new market being opened to help it for the first year, two, three years, you might offer incentives to build the market and what you're using is you're using your non-aeronautical revenues over that period to help build the market. In the longer

term that extra traffic results in a reduction in your aeronautical charges unless there is equivalent assets brought in. So actually the activity tends to work in the short term with the growth of the business and in the longer term with the economies of scale there is a spill-on effect. Quantifying it, I don't think it's at the 20 times current prices but I don't know what it is.

MR SUTTON: I have one more for you and that is the question around the pricing principles and/or a voluntary code of conduct and Qantas are on board for the idea that there could well be - and I invited them to give us specifics because we definitely need to deal in the world of specifics here - there could well be further principles that could minimise some of the time and the agony involved and reinventing the wheel in a lot of these negotiations. There could well be principles that could make that a more efficient process and they say they're going to send us something which they think can flesh that out. So what do you think about the concept - we floated, of course, that there could be additions to the pricing principles and/or work on a voluntary code of conduct.

MR FINLAYSON (SACL): I think the pricing principles that are in place at the moment are very helpful in terms of guiding principles and the commercial relationships between the airports and airlines are improving and maturing, I think is the word Kerrie used, because really 2007 was the first time that we had done international agreements with airlines and we're coming up to the new ones. So those relationships have matured significantly. So we already have pricing principles in place. To get to a further voluntary code of conduct actually is the same as commercial agreement of principles which I think actually then goes back to just purely again the negotiation between two commercial parties. I understand where they are coming from.

I think the extensive seven-year negotiations that Qantas referred to with Canberra are something of the past. I think you are coming up to a stage where there are precedents set now. We're a lot further down the track. Those negotiations will actually be a lot shorter and sharper across the board, barring extremely complex issues which then do need to be negotiated and will normally fall outside pricing principles anyway, I think. We've got the pricing principles in place, we've got maturing relationships, to get a voluntary code of conduct it sounds good but it actually is the same as having commercial agreements in commercial relationships.

DR CRAIK: One of the things that Qantas raised in their discussions was that there is really no measure in the monitoring reports of productivity or there is no kind of evaluation of productivity and they seem to imply that, you know, there's no way that they can feel that the money they pay in airport charges leads to improved productivity in the system. Do you have any comment here about that whether it could, should be measured, put in agreements? Maybe it is put in agreements, I don't know.

MR FINLAYSON (SACL): Again, I mean, airports are very keen on improving productivity.

DR CRAIK: For their own reasons I would have thought there was a fair - - -

MR FINLAYSON (SACL): For our own reasons, but if the airlines are growing, we're growing. We are actually linked at the hip. Any time that they're impacted, we're also impacted. The productivity is very important to us. We've brought in ground power and preconditioned air which is something that required investment that actually improved the efficiency of the operations for airlines as well. That was a win-win. There are ways that we can work together to improve productivity. We've got SLAs in place with Qantas. We've got the ACI ASQ surveys. If those SLAs, for example, need to be amended in some way, then let's have the commercial negotiation about that. That hasn't been used particularly as an issue that they cannot negotiate that with us. I'm very open to SLAs that support the airlines and support our own growth.

MS MATHER (SACL): I think having listened to Qantas's submission this morning, the couple of examples they raised on measuring productivity and promoting more productivity that I think were relevant for Sydney were in terms of airspace management and a lot of regulations that apply to that, but also the access to the airport.

DR CRAIK: Isn't airspace regulation a matter for Airservices Australia?

MS MATHER (SACL): It is. We would certainly support anything that improved a - it was one of the things that I was referring to in my opening comments about making some of the regulation around the airport more contemporary. Certainly airports overseas where noise is an issue, where there are restrictions around the operations of the airport there is a relationship between noise rather than an arbitrary cap. So as Qantas are investing, whether it's in new aircraft that are significantly reducing their noise emissions or where they're investing in airspace management technology, that there was an operational regulatory framework that supports those investments. We would certainly be very supportive of moving in that direction as well.

I think we have definitely got an aligned interest with Qantas on improving the access at Sydney Airport, both in terms of the roads, but they also gave the example of a rail access fee that applies on the commuter rail link to Sydney Airport. The rail access fee was removed off Mascot Station and I think they gave an example where the patronage had increased threefold. Certainly the consultants, before that was removed, were predicting a 17 per cent increase in patronage and they ended up with 70 per cent increase in patronage. Given that there are 17,000 people that actually

work in the terminals at Sydney Airport and where you've got rail access into both the international and domestic terminals, removing that rail access fee would actually provide a more convenient and cost-effective way for all those workers to get to the airport and provide an immediate relief in terms of road congestion. I think they were the two things they were focusing on in relation to Sydney and we would certainly be very supportive of both.

MR FANNING (SACL): Airport services is very much a joint product as well, with both airlines providing sufficient resources at the right places, it's the airport providing the right infrastructure, it's control authorities, customs, so it's very much a joint industry effort as well. Trying to get the right productivity gains obviously takes a lot of stakeholders to come together, both internally as well as externally, and some of them are non-controllable, but we are absolutely working with airlines to - - -

DR CRAIK: Some of them are non-controllable, did you say?

MR FANNING (SACL): They're government agencies, for example, or Airservices have their own regulations and restrictions. In order to reduce, say, fuel burn there's only so much each individual party can bring to the table. It takes a broader industry initiative to try and get some of those productivity gains.

DR CRAIK: Can I pick up the issue of noise management, Kerrie - and John might raise any questions on this, his place of residence. We had a discussion yesterday when a couple of people appeared before the commission and, firstly, there was the suggestion - because we suggested in our draft report that maybe it's worth considering managing this noise issue on a noise performance basis, rather than a numerical basis where the actual derivation of that is not entirely clear. If you can shed any light on the derivation of those numbers, like a cap of 80 per hour and things that would be useful to us. Does Sydney Airport have strong views about - I know you've written something in your first submission about capping the curfew and the noise restrictions. We did put some things in our draft report about that, that some of these issues might be reconsidered. Do you have anything to add on that issue?

MS MATHER (SACL): How long have you got?

DR CRAIK: At least eight minutes.

MS MATHER (SACL): Sydney has four operating restrictions that apply to it; more than any other capital city of its size in the world. Many of them were arbitrarily put in place some years ago and they're out of step with movements on this front overseas. Sydney has an 80 movement an hour cap. What's interesting, since the airport was privatised, traffic has grown 40 per cent in that time, but the

number of movements has only grown less than 1 per cent. You're getting more seats per movement because the aircraft are getting larger, and that's happening at every level in the market, from international to domestic to regionals. That's only going to continue. But I think what's interesting is that the noise has effectively reduced because the aircraft that are being used are a lot quieter.

DR CRAIK: We were told yesterday that the quietness has only improved by one or two decibels, so it's insignificant.

MR KAMERON (SACL): I know that Qantas will also look to this. We'll pull out the Airservices data that has the noise characteristics that they certify aircraft for. The other thing is, 10 decibels is a tenfold increase in noise. A three decibel reduction is actually a halving.

MR FANNING (SACL): It's a logarithmic scale. When you talk about only two decibels you're talking about only a 30 or 40 per cent reduction. It sounds quite small but it's actually - - -

DR CRAIK: It is in reality quite high.

MR FANNING (SACL): It is more real.

DR CRAIK: Okay.

MS MATHER (SACL): The trend is going to continue because at the moment we've got three airlines that are using the A380s at Sydney, and in fairly short order we'll have six. Qantas themselves have significant deliveries of the 787s, which will move - I think they're going to configure them with 300 seats, replacing 767s, which they configured with 160 to 180 seats. That trend is going to continue.

DR CRAIK: The point was made yesterday that the number of quiet aircraft as a percentage of all the movements is actually quite small, so again it doesn't - - -

MR KAMERON (SACL): Define "quiet". The number of quiet aircraft today defined by 1980 standards is 100 per cent. The number of quiet aircraft in 2030 by today's standards will probably be 80 or 90 per cent I would imagine. I know the 737s are being re-engined. The A320 is being redesigned. The 787 is in production. The A380 is in production. The A350 is almost in production. Year by year, yes, there will be some aircraft that are delivered today that will still be there in 20 years' time but there will be none of the aircraft that are flying today that were delivered 20 years ago still flying in 20 years' time.

There is some of this happening naturally. What I think the missed opportunity under the current regulations is the opportunity to do more. There is possibility of

investment by the airport, the airlines, Airservices and other parties that have either capex or operating cost, you potentially increase fuel burn or time, that further reduce noise. Under the existing regulations there is no incentive, no benefit to doing so and since you're actually incurring cost, positive disincentives to do these things. A regulatory regime such as exists in most places or many places in Europe which encouraged you to actually - "Okay, we can have two flights that have less noise, than this one flight," the community benefits, the airlines both in terms of lower noise but also in terms of more business and the airlines and the airports benefit. I struggle to see what the downside of that approach is.

DR CRAIK: Okay, that's useful. Thank you. Do you have anything, John.

MR SUTTON: Yes, I've got a few things. General aviation, does GA have a secure future at Sydney Airport?

MR FINLAYSON (SACL): I think if you look at the master plan which is the land use plan for the airport, general aviation is still there in 2029. Every five years we do a new process so that's a master planning exercise but they're there absolutely in the master plan.

MR FANNING (SACL): And delegations under the head lease as well also preserves the right to access Sydney Airport.

MR SUTTON: Good. Land transport issues. Can I suggest that the situation is pretty dire in that we know the passenger forecasts at Sydney Airport; we know the main port now is Port Botany, we know it's increasing its capacity at this very moment. I happen to live in the area so I just know how logjammed it is and looking forward it seems a pretty dire situation in which I think urgent action by a variety of authorities, a variety of stakeholders is necessary. Can I just ask for a comment on that set of problems.

MS MATHER (SACL): Consistent with the position that Qantas adopted before, I think our submissions also demonstrate that the benefits of the airport activity almost fall entirely to the broader state so there needs to be state investment in the surrounding roads. Pleasingly the government and a new infrastructure group has actually recently announced that Sydney Airport-Port Botany land transport access is their number one priority.

DR CRAIK: This is the New South Wales infrastructure?

MS MATHER (SACL): This is New South Wales.

DR CRAIK: Set up under Nick Greiner.

MS MATHER (SACL): Yes. So that's pleasing but I think the other priority is actually the rail access fee in terms of providing a more economic mode of transport for airport workers as well.

MR SUTTON: Just drawing you out further on the part about - which I think you were implicitly touching on, when there are non-aero developments on the airport which have an impact off airport, and the information request we have in there about whether in those circumstances there should be a requirement in terms of funding of that necessary infrastructure off airport. You just think it should be done on a case-by-case basis or is there any argument for a formula or a consistent approach? What do you think?

MR KAMERON (SACL): I think the first point to make is actually if you look at the Sydney Airport site and you look at the master plan and where we're putting runways and taxiways and terminals and carparks, there's actually - this is not Brisbane and Melbourne Airport with large acreage available for shopping malls. There is relatively little scope for non-aviation activities. I think, secondly, the little we do have - there is, for example, a Krispy Kreme on Airport Drive, almost all of that is sitting on Airport Drive which is already provided by the airport. So I don't see there would be any need to further subsidise a road that is actually half used by commuter traffic rather than airport traffic as it is.

I think to the extent that there is other non-aviation business that was material in any way then, yes, a case-by-case basis by might be most appropriate. But in our case it's getting fairly hypothetical. There's not that much opportunity.

DR CRAIK: Just following up John's question about general aviation, we had the Business Aviation people speak to us yesterday, I think some of you probably heard what they said and the fact that they're concerned about - there apparently is a proposal for a Virgin hangar where they currently are on Sydney Airport and they are concerned about the possibility of being moved on and I guess they are concerned about both the cost and the timing and it is going to be a very difficult interim period for them.

MR FANNING (SACL): Indeed, yes. Sydney Airport addressed their AGM only last week on the issue so we presented to the members what's entailed in the master planning process and what's already been included within the master plan and we also then discussed the implications of if Virgin do proceed with a major development plan to build a hangar where it is currently proposed, which is again consistent with the master plan. The area is not completely removed. There is still a substantial area for the existing users to continue to use that space and as part of the ongoing consultation and as part of the MDP process we will also look to continue to provide access at other parts of the airport.

Again, it comes back to what are their needs, what's the level of investment that's required and some mechanism to put a covering on that investment. So there is a lot of due courses yet to take place, so it's a little bit theoretical at the moment.

DR CRAIK: Okay.

MR SUTTON: Just one thing that just occurs to me. The major concern of the airlines - one of - around the agreements is not so much whether the agreements are on foot in that there are mostly dispute-settling mechanisms in the agreements, it's more about the period where you're haggling to try and reach an agreement. We know where the airlines are coming from, they want to have a negotiate-arbitrate model. What do you think of something less than that, such as where there is a deadlock or some issue that's proving extremely difficult to resolve, the idea of an agreed independent arbitrator or a private arbitrator or head of the Law Council or somebody who comes in by agreement to unlock the so-called deadlock? What do you think of that kind of mechanism?

MR FINLAYSON (SACL): Any airline that is flying in - we've got over 38 airlines flying in - all have conditions of use in place and commercial agreements in place. So there are mechanisms within those to actually resolve any disputes and you've always got the opportunity of (1) building the commercial relationships, and Qantas actually referred to that, is that it's extremely important through this process to have not just a regulatory approach but actually a commercial approach so that you can get innovation, you can get product differentiation.

But you've also got that opportunity to escalate that already to CEOs and I'm not aware of any issues that have actually been escalated and had to be resolved at the CEO level.

MR SUTTON: Is that while an agreement is on foot, are you talking about there?

MR FINLAYSON (SACL): On and before. I don't see any evidence of where there's been no agreements - - -

MS MATHER (SACL): They do have a regime where they continue until another agreement is actually put in place.

MR FINLAYSON (SACL): The conditions of use that's in place as well has an escalation process.

DR CRAIK: So even before you've actually got your first agreement they could go with the conditions of use?

MR FINLAYSON (SACL): Correct, and that allows for escalation as well as a

mediation process.

DR CRAIK: Okay. Anything more?

MR KAMERON (SACL): I think, to directly answer the question as well, the benefit of a dispute resolution, the process that we have, which is in the conditions of use and in the commercial agreements, is that you don't run the risk of regulatory creep that you would have if it was the ACCC doing it where every decision they make on any one airport, with any one airline, on any issue, somehow sets a precedent for every other airline, on every other airport, on every other issue, regardless of its relevance. I think that's the importance of the dispute resolution being via a mediation or, if you agree, in arbitration with a commercial-type approach that is looking at the specific issues in hand and isn't setting precedents that cut across - - -

MR SUTTON: There could be in given circumstances some value in a private arbitration about a discrete issue or something that was deadlocking the parties.

MR KAMERON (SACL): The parties are open to agree to that at any time as well, bearing in mind it's hard for us to invest if we don't have an agreement. They might have time pressures but so do we.

DR CRAIK: Okay. I think we've run out of questions but thank you very much for your submission. Thanks for coming along today.

MS MATHER (SACL): Thank you.

DR CRAIK: Okay. We'll now move on to Margaret Arblaster. Thanks for coming along. Can you state your name and position for the record, and then if you would like to make a brief opening statement we would be happy to hear from you.

MS ARBLASTER (TA): Thank you. My name is Margaret Arblaster, I'm a director of TransAv, which is my consulting entity. I've made a submission to this inquiry but on a fairly narrow aspect of it, and that was in relation to the show cause recommendation. In my submission I have expressed the view that I think that rather than strengthening the regulatory framework, I think the prospect of a show cause mechanism would weaken it for a number of reasons. Firstly, the criteria which the PC have proposed that should be met in order to invoke the show cause provision I don't think is readily ascertainable from the monitoring information. I think it's a fairly high benchmark and the data that is provided to the monitoring process would not allow the ACCC to make judgments to the standard that the PC proposes should be the case. That's both with respect to price monitoring information and also with respect to quality of service information.

The other thing is that I don't think the show cause mechanism provides an appropriate or timely remedy to specific problems. I think a show cause provision potentially leads to a public inquiry and in my view there would be an absolute minimum of 18 months from the time of the end of the financial year of a particular reporting period to the outcome of a public inquiry, and it could well be longer than that, so it's not timely. The other issue I think is you need to look at the possible recommendations that might come out of a public inquiry and whether or not they would redress any particular problems that arise.

One of the main things that is often put behind a public inquiry is if the inquiry found excessive pricing or the use of market power, it might propose direct regulation, and I think if in the event that an inquiry did reach that conclusion I don't think a recommendation for regulation through direct price controls would be a satisfactory recommendation because it conflicts with the current pricing principles anyway. The government, I don't think, or industry would want a reimposition of price controls. That particular outcome from a public inquiry would not likely be adopted.

I also think the show cause proposal introduces a lot of uncertainty because I'm not quite sure what the outcome of a public inquiry would be. There's quite a raft of recommendations that can occur. There's not many precedents in terms of Part VIIA public inquiries. There's only been about three in the last 15 years. I think we need to look at what are the possible outcomes and how effective they are. That in itself I think creates some uncertainty. I also think the process that the PC propose doesn't appear to be a transparent process which is inconsistent with other regulatory proposals. It's also a very one-sided process whereby the PC have recommended that the ACCC make a recommendation on the data and they don't take into account other

information, like complaints from the industry. They're my essential points.

DR CRAIK: Thank you for your submission. We appreciate it because it's useful to have someone who has a close familiarity with some of these things. It's useful to get commentary on what we proposed. It's very helpful to us. When you say the monitoring won't provide the information that you think would be necessary to meet show cause hurdles, in a sense does that say that monitoring as it stands now could never lead to the ACCC recommending a VIIA inquiry, leaving aside a show cause?

MS ARBLASTER (TA): If there was very gross behaviour that was identified through the monitoring regime, I suppose the ACCC could make a recommendation. I think there are circumstances where it possibly could but there's probably a lot of circumstances where there might be particular problems where the monitoring information wouldn't actually identify those.

DR CRAIK: Okay. Do you really think they're too high because we're only seeing the show cause as a preliminary step. For example, the ACCC, at least in a kind of summary chapter and in the media sometimes, have suggested there might be an abuse of market power here, or potential abuse of market power there in relation to some of their monitoring reports. If it meant the hurdles that we've set up that they could issue a show cause so it is an opportunity for the airports to come back and kind of explain - so we only see it as a preliminary step. We're not launching into a full-blown prosecution at this stage.

MS ARBLASTER (TA): I suppose it's a preliminary step. I mean, in order to take that preliminary step you've said that you've got to reach a certain level of confidence, and I can't see that necessarily being reached.

DR CRAIK: The other question you raised is this issue of the possible outcomes. I mean, I don't know, I might be reading far too much into what you say, but it seems to me what you're essentially suggesting is that - I mean, the possible outcomes now from a VIIA inquiry - you know, either price-capping or declaration, a whole range of things that exist currently, and you say they're not likely to happen regardless because of the environment in which all this is established. So does that mean that they're really - - -

MS ARBLASTER (TA): Well, the direct price-capping I think is unlikely.

DR CRAIK: But declaration is always a possibility out of - - -

MS ARBLASTER (TA): I suppose there's other direct - sorry to cut you off - other declaration processes, and it's a question of, you know, what would be the best way of invoking a declaration.

DR CRAIK: Yes. But a VIIA inquiry could recommend that that process be instituted, couldn't it? As I understand, and you know more about than I do, a VIIA inquiry is free to recommend whatever it believes as appropriate. So in that sense, while price-capping may not be acceptable as an outcome, there are a range of other outcomes that are possible out of a VIIA inquiry that might deal with - - -

MS ARBLASTER (TA): I suppose potentially it could. But you'd still have the problem that it's well and truly after the event and it's very delayed in introducing that. Say, a Part VIIA inquiry did recommend that particular airport services were declared, or a range of airport were declared with deemed access, you've still got the next step of introducing the deeming provision and there'd be a range of ways that that could be done. Previously it has been done by sort of special purpose legislation. If the deeming was to be introduced by a legislative means, I mean, there's further delays again because it takes a long time to sort of draft suitable legislation and then actually sort of pass it and implement it through the parliamentary process.

DR CRAIK: Doesn't that all apply under the current system? Isn't all that true under the current system, under the current regimes? Doesn't all that apply now? Isn't all that the fact now?

MS ARBLASTER (TA): Some of it. Well, there's the extra delay that a show cause would introduce.

DR CRAIK: Yes, the show cause will add into the system.

MS ARBLASTER (TA): I mean, the Part IIIA can be used now, and I understand BARA have just put in an application for declaration under Part IIIA, I think it was last week.

DR CRAIK: Have they?

MS ARBLASTER (TA): Yes, for the Sydney Airport JUHI facilities and the Caltex pipeline, because they had issues associated with aviation fuel supply I think at some of their airports.

DR CRAIK: I guess all I'm saying is the time durations on all the end result, on the outcomes, they all exist at present; so it would be the additional time that the show cause process would add to the process that you see as an additional problem - - -

MS ARBLASTER (TA): Yes, it would be an additional problem. Under the current arrangements, the ACCC or the government could decide to have an inquiry and all deemed declaration could occur under a PC inquiry. It depends on how they're introduced.

DR CRAIK: Okay. John, do you have any questions?

MR SUTTON: All those problems that we've just touched on with VIIA, even as it currently sits absent any show cause, it's a long process, it's unlikely to do anything far-reaching like price-setting or price-capping, or whatever.

MS ARBLASTER (TA): That's right.

MR SUTTON: Doesn't that all amount to illustrating that the so-called credible threat - VIIA is one of the sort of things that's pointed to - to suggest there is a credible threat in existence right now. But if VIIA has got a lot of problems with it, sort of in a way it helps prove a point that we're making that we somehow have got to supplement or add to the existing tools because they don't really amount to a credible threat.

MS ARBLASTER (TA): I suppose it's an issue to what extent Part VIIA is a credible threat, and, as I think we were just discussing, I don't see it as a credible threat of regulation of introducing price caps. So it wouldn't be a credible threat in that sense. Then you've also got the issue of whether the monitoring itself is still going to be a credible threat, because too the monitoring provides historical information and it's fairly limited in nature. In order to actually increase the degree of regulation there's not sufficient information that you sort of derive from the monitoring.

So for example if there were going to be prices determined going forward through some avenue or some specific situation resolved, then a lot of additional information would have to be acquired - sorry, while past monitoring information might be helpful, it wouldn't be sufficient and a fair bit of additional information would need to be acquired. So monitoring doesn't sort of readily link to introducing a strict form of regulation.

DR CRAIK: To me, it questions the whole value of monitoring, if that's the case.

MS ARBLASTER (TA): I think with monitoring you've got to ask, you know, what is the purpose of it, and depending on what you think the purpose of it is depends on the type of information that you really need to get. I mean, if it has limited value as credible threat then do you need more information, is more information going to help you? If it's going to help the airlines and their negotiations, then I think you'd probably need to ask them. I mean, is monitoring to test the pricing principles, because the information that's provided by monitoring now doesn't allow you to sort of test the pricing principles that are established. I mean, is monitoring to give the government a very general idea of, you know, how the airports' revenue and costs are going as measured by historical accounting

information and a broad indication of performance?

MR SUTTON: Margaret, just going back to that same territory. You started off by saying that the data that the ACCC has access to at the moment wouldn't allow them to make judgments about either price or quality matters sufficient - - -

MS ARBLASTER (TA): I don't think I - sorry, I'll let you finish.

MR SUTTON: Well, you correct me if I'm wrong. I took you to be suggesting that they didn't have access to sufficient information that would allow them to form a judgment about price or quality matters such that would satisfy the test we're laying down for the proposed show cause.

MS ARBLASTER (TA): I think the ACCC themselves sort of more or less indirectly said that. I mean, the ACCC themselves say that, you know, the monitoring information is indicative and they'll need to take the monitoring information in relation to other factors. So I'm not sort of saying that the ACCC can't make any judgments at all. What I was saying was that I don't think the monitoring information allows the sort of judgments that - - -

DR CRAIK: You think would be required?

MS ARBLASTER (TA): To meet the standards that you described as, you know - demonstrated, for example, is one of the words that you use.

MR SUTTON: Should we be recommending that they go and access whatever additional data they need?

MS ARBLASTER (TA): I think again it gets back to what the purpose of monitoring is. I mean, there's no point in getting additional information if the monitoring is not going to lead - well, to sort of something worthwhile.

MR SUTTON: But they are forming views now in the monitoring - supposedly forming views about price issues and quality issues. So one would hope that they do have sufficient data to do that. They've been doing it for some time.

MS ARBLASTER (TA): They qualify the views that they form. I mean, in the reports, as I've sort of indicated in my submission, they have said that it's indicative, and qualified to the extent that they - and I am not speaking on behalf of the ACCC, but, I mean, the ACCC identified that it was a possible time for an inquiry to have a look at other measures.

MR SUTTON: They have those powers, section 155 - - -

MS ARBLASTER (TA): Sorry, the PC to have an inquiry.

MR SUTTON: Doesn't the ACCC have powers - I think it's section 155 - to obtain further information.

DR CRAIK: They have never used it.

MR SUTTON: Do they do that in the course of monitoring or are they prohibited from doing that in the course of monitoring?

MS ARBLASTER (TA): I think that that's probably a question you should address to the ACCC, but, I mean, a lot of the powers of the ACCC has have to be looked at in the specific circumstances, and there's fairly high hurdles for using some of those powers and certainly with section 155 powers there are legal tests involved. I think that that's probably the questions that they should answer. You'd also have to ask - or, you know, it partly depends on what you think you're going to achieve too. I mean, there's no point in just using a power without a purpose.

DR CRAIK: I must say your history of the derivation of monitoring is actually very enlightening. That was actually quite good. So thank you for that. The other comment you made is that you don't think that the show cause process as we put it is - you know, not transparent, because particularly it doesn't invite commentary from other industry. I guess we were trying to avoid a complaints-based process and actually have it based on tangible and hopefully robust data; so it was an evidence-based process as opposed to a complaints-based process, which the last show cause ended up being for a while. Certainly third parties would have an opportunity during a VIIA inquiry to have an input into the thing. But we were trying to keep it to an evidence-based process rather than a complaints-based process, in the show cause part of the exercise.

MS ARBLASTER (TA): I suppose if it's one way, you may not have an inquiry when the circumstances - well, without getting a balanced view - may warrant it. I mean, if you're going on the numbers and the numbers are limited, then you're asking sort of one particular party for their views and they express particular views, but you haven't got the other side of the coin, and based on their views of the numbers you sort of say the show cause is not warranted. That's what I sort of see as a potential defect.

DR CRAIK: As a problem. This might be an unfair question, and feel free not to answer it if you don't want, but the new chairman of the ACCC made points about airports are monopolies and therefore should be regulated. Do you have a view about that?

MS ARBLASTER (TA): I'd prefer not to comment, thank you.

DR CRAIK: Okay. I thought you might. Do you have anything else, John?

MR SUTTON: No.

DR CRAIK: Thanks very much, Margaret. Your comments were actually really helpful to us.

MS ARBLASTER (TA): Thank you.

DR CRAIK: Thanks for coming along.

DR CRAIK: Now we have Mildura Airport. Thanks for coming. Could you state your name and your position, please - - -

MR BURKE (MA): Yes, William John - Bill - Burke, and I'm chief executive of the Mildura Airport company.

DR CRAIK: If you'd like to make a brief opening statement, we'd be happy to hear from you.

MR BURKE (MA): I have made a written submission and tendered some confidential material, and, quite honestly, I think that's the substance of what I've got to say. I'd be happy to expand on any of that for the commission. I've got some fairly strong views and my board has quite strong views on the way dealings are done in the regional forum between airlines and airports, and, quite frankly, I think some of the assertions that have been made by some airlines in some forums, including this, are quite, in my view, somewhat mischievously incorrect.

DR CRAIK: If you wish to respond to those, feel free. We invite you to respond to those.

MR BURKE (MA): Look, there have been some assertions made that regional airports, and airports in general in fact, are gouging moneys out of airlines and creating situations of inequity and difficulty with the airlines in their operations into some of those regional ports. Frankly, I'll say very categorically, quite the reverse applies. Regional airports are invariably run by councils and people relatively inexperienced, unconnected, lacking the communication networks that exist in the bigger cities, and, frankly, it's open slather for those airlines that deal across the nation with multiple airports, have knowledge of dealings with their experience - good, bad or indifferent - and have the ability to be able to apply pressure to local communities for the continuation or not of a service based on the success they achieve in negotiating a fee for the service of the airport.

Airports in regional communities, they're critical infrastructure, there's just no doubt about that at all. They're the same as road stations, call it what you will, but nevertheless what the airlines fail to acknowledge and respect is the fact that there's a cost of operation of an airport; they're regulated, they're controlled, and the compliance requirements with the Civil Aviation Safety Authority and with the Office of Transport Security. The compliance requirements are quite stringent and they come with a cost. I'd suggest that in some areas and in some operations the true costs of operation are not known. Some of those costs are generally absorbed within the community, the council and not necessarily passed on directly to the aviation users of the airport.

In the case of Mildura the council about three years ago - I think they took a

good direction - they decided to excise the airport from the council operation and set it up under a company and operate it completely independently and transparently with a bunch of, hopefully, expert people to operate it, and under their model it has been running very well. But what it does highlight is the true cost of operation of an airport like Mildura. It's a critical airport. Its services are wide-reaching and far beyond just the local community. It services three states of the nation, and, you know, quite a substantial population beyond the local population.

The need to retain services, the need to have appropriate services into Mildura is paramount. But we are faced constantly with pressure from airlines - and I won't nominate who, but airlines in general - to keep costs down, to negotiate preferential arrangements, to generally come to the party in terms of cooperation or run that risk of losing the services. How far we can go and how far other airports can go is a vexed question, because really I think it's a negotiating ploy, I think it's something that the airlines use to finesse their bottom line, but I don't really believe that what any airport in a regional sense can offer to an airline is going to make the difference between retaining or losing the service that they're operating.

DR CRAIK: Do you call their bluff?

MR BURKE (MA): Yes.

DR CRAIK: Have you ever had any withdraw?

MR BURKE (MA): Yes, we had Sharp Airlines withdraw from the Mildura to Adelaide run, and the reasons that they stated were the costs of operating into Mildura and the pending likely cost of passenger security, which will be coming forward on 1 July when the Q400s that Qantas operate are routed into the system, at which time we will become a fully screened airport.

We have a policy that we will not negotiate on a head tax with anyone. That head tax applies to all airlines across the board. We will have entry and we will have differential arrangements for increases in services, increases in seat numbers, those sorts of performance based things but the base level of head tax is the same. Security is applied against those people who - at the moment it's only Virgin - require security and so they cover the full cost of that. It's not passed onto any of the other airlines. But at a point in the future that will change.

DR CRAIK: Are you familiar with the pricing principles that apply to the major airports?

MR BURKE (MA): Not really, no.

DR CRAIK: We raised the question in our draft report whether there was any merit

in those pricing principles applying to regional airports and when we discussed this yesterday with the Airports Association they suggested if those pricing principles applied that in fact the prices at airports would actually go up because the true costs would be affected.

MR BURKE (MA): I suspect that would probably be correct without really knowing what the principles are. We at Mildura, I can say factually, do not fully recover the costs of day-to-day operations against the airlines.

MR SUTTON: Notwithstanding that you've made it a stand-alone business, do I take you - it's a stand-alone business.

MR BURKE (MA): It is.

MR SUTTON: It's meant to operate on its own wares, you're a loss-making enterprise.

MR BURKE (MA): No, we can't be a loss-making enterprise because we're faced with solvency provisions of the Corporations Act but - - -

MR SUTTON: Can you just clarify.

MR BURKE (MA): We make enough out of our head taxes to cover our day-to-day operations and there is a very, very small margin for uncertainty beyond that. So really the charge against the airlines is doing nothing more than cover the cost of labour and equipment and operations to maintain the operation at the airport.

MR SUTTON: When you talk of the head tax and you say that's not negotiable, what is it and how does it come about?

MR BURKE (MA): The head tax should be, in my opinion - I think a lot of work needs to be done in this area - an amount of money that reflects some level of return on the asset or such amount as to cover the cost of operation of the airport and, as I say, leave some small margin in the kitty. In our case the amount that we charge is something that is a product of the past and just what the basis of that was I couldn't tell you. But what I do know is that it's within the ballpark of many of the regions around Australia.

DR CRAIK: So what do you do when you need to invest in major maintenance, major development at the airport if you - - -

MR BURKE (MA): Capital works rely on grants, federal, state grants. Major repairs clearly have to come out of our revenue.

DR CRAIK: So any new development you pretty much have to get a grant for, is that - - -

MR BURKE (MA): Pretty much, yes. In the last couple of years we've spent some 10 million on apron works which was money that came partly out of council, partly out of the airport and partly out of state government and without that work having been done, we would not be operating Q400 and up to 737 aircraft into the airport.

DR CRAIK: Is there anything you would like us to recommend? What would you like us to recommend?

MR BURKE (MA): I think it is a difficult area because it's very much a commercial area. I don't think regulation is going to help. I think the commission needs to understand that regional airports are not the bad people they have been portrayed to be. In fact, quite frankly, the boot is on the other foot. Regional airports are constantly running a fine line between trying to satisfy the demands, if you like, of the airlines but satisfy the needs of the community in keeping those services there. But the problem that most regional airports would have is that they just don't have the capital and the money to be able to subsidise the airline services.

DR CRAIK: Qantas today suggested one of the fundamental problems with regional airports is their valuation of the asset base.

MR BURKE (MA): I did a little number before I came down here and we're doing about .8 per cent on the asset value at the moment return so you would put the money in a bank rather than an invest it at an airport at those sort of levels.

DR CRAIK: Do you think there is any role for someone like the Regional Airports Association to assist local airport, regional airports in negotiating with airlines?

MR BURKE (MA): Simple answer, no, because I think the Regional Aviation Association has a foot in two camps. They represent airports as well as airlines and how do you work that?

DR CRAIK: What about that AAA?

MR BURKE (MA): AAA tends to - I may get into trouble with John on this but the AAA I think represents a bigger end of town rather than a smaller end and I'm not quite sure that they are as focused on the regional interests as they are perhaps on the larger end of town.

MR SUTTON: It will be interesting to watch the dynamics of the afternoon tea between you two. Security charges in recent years with additional security requirements. What kind of challenge is that posing to the operation of your airport?

MR BURKE (MA): It's a huge challenge. We have been quite steadfast in applying the security charges only to those airlines that have received a benefit. In one case it was the jet operation of Virgin and in another case it was for one service a day, it was the Q400 operation of Qantas for a period of time. When that was occurring we ran the numbers against or we reversed the charges against the seats generated in those windows. Going forward, given the difficulties of separating those aircraft or those passengers that require screening because of the aircraft size and those that don't, it's totally impractical to try and segregate and as of 1 July next year we have made the determination, we will determine to be a fully screened airport and now that will cause a scream from those airlines that have aircraft below the 20-tonne threshold and they will say that they're not required to be screened so therefore they won't contribute.

Nevertheless, that's not recognising the commercial capability and the commercial entitlement of the airport company to actually make a commercial charge and disperse the costs according to the way they will. The airline will then make up its mind as to whether it stays or goes.

DR CRAIK: Okay. Thanks very much, Bill.

MR BURKE (MA): Thank you.

DR CRAIK: Thank you for coming down from Mildura. Thanks for your submission and your comments. We might break now for afternoon tea and come back at 3 o'clock.

DR CRAIK: Thanks for coming along. If you could state your name and your position, and if you would like to give a brief opening statement we'd be happy to hear from you.

MR FELLOWES (HFM): Sure. Thank you. Andrew Fellowes from Hastings Funds Management. I'm an associate director with the infrastructure team there. As some of you may know, Hastings has a range of infrastructure funds that it manages, primarily on behalf of superannuation funds, institutional investors and retail shareholders. We manage across a wide range of infrastructure assets, but in the Australian airport space we have ownership stakes in 12 airports, including a range of major city airports, as well as regional airports - everything from Melbourne Airport, Perth Airport, Gold Coast, down to smaller airports such as Alice Springs, Mount Isa, Cairns and Mackay.

We're quite interested in the Productivity Commission from an investors' perspective. We, of course, work closely with the management teams at our airport but often feel there's a slightly different perspective as an asset owner. Firstly, we'd like to thank you for the opportunity to present. We're very supportive of the initial draft findings. We probably largely agree with you that the current regime has been very successful. We like infrastructure as an asset class because of its stability because of its predictable returns and the lack of volatility in those returns. There are certainly risks involved with investing in infrastructure. There's traffic risks, there's operational risks. You're taking risks on financing, both on the equity side, raising equity capital, as well as on the debt side, making sure that the airports are able to raise their financing when they need to support capital expansions.

It's not an investment without risk but it is still what we consider core infrastructure because of its stability, because of the relatively predictable way that prices are set, and the history of successful commercial agreements that have been set that give some level of price certainty, subject to traffic risk, for the length of contracts, be that five-year contracts or 10-year contracts for terminal agreements or aeronautical service agreements. We find that that stability is something that's very important and therefore is something that needs to be protected and it shouldn't be underestimated, the potential impacts of changing the system or even constantly renewing the system.

It has been good to see the supportive comments made in your draft report. We work very closely with the management teams. In a lot of cases we have board representation on the airports in which we have invested. We see the level of analysis that goes into the negotiations that they conduct with airlines. We know it's not a one-sided battle and that there is certainly a lot of tension there between the market power that airports do have but certainly the countervailing power that the airlines hold.

A lot of that has been talked through in detail before. I guess the key items that we'd like to discuss were the show cause proposal, the commercial guidelines and the degree to which developer contributions might need to be made. The major point around the show cause proposal was that it really just provides a greater level of uncertainty, at least unless there is a very clear list of evidence that is needed, a history of two or three years' worth of clear proof that the ACCC needs before it issues a show cause notice. We are certainly worried about the damage that it might cause from a timing point of view, being able to raise equity, being able to raise debt always with a cloud over you that you might get a show cause notice somewhat out of the blue and that doesn't help the industry. It doesn't help people make the decisions. Given that we're investing generally for superannuation funds or life insurance funds and we're buying things like new runways or terminals, they're 20, 30-year assets, you've got to know that you're going to make money for several years and that the whole system is not going to change next year or even in five years' time.

So the show cause proposal is of some concern to us. We think that from an equity point of view it would probably need to be disclosed to retail investors. It would probably need to be disclosed to our banks if we were raising money either at the fund level or at the asset level and so, therefore, it's of concern because at that - or at least as it's proposed currently, that show cause notice isn't a definitive finding of wrongdoing on behalf of the airport and yet you could have definitive damage done to the airport's reputation, you could have definitive damage done to its ability to raise debt at low prices. If you introduce that in a spectre of potential price inquiries and heighten the risk of potential price inquiries, that could be difference between raising a billion dollars to build a runway for 7 per cent and raising it for 8 per cent and that's really just money lost out of the system because it will eventually have to get recouped from customers and that's borne by everybody effectively.

MR SUTTON: As to notifying the markets, you have both listed and unlisted vehicles, don't you?

MR FELLOWS (HFM): Yes, we do. We tend to be quite open and transparent with our unlisted investors as well so I wouldn't be surprised if we would tell them, although that's a relatively more informal disclosure process. But certainly on the listed side with the Australian Infrastructure Fund, which has a lot of the airports in it, at least our internal thought was that under the existing rule 3.1 you probably have to disclose. At least if it was with the major holdings of Perth and Melbourne but they are also the airports - show cause is more likely to be one of the large airports as well, given the ACCC's lower focus on regionals.

On the commercial guidelines, I guess we always welcome further insight that the commission might be able to provide to speed up the negotiation process. We

agree that it can be somewhat lengthy. You've got airports with one point of view and often multiple different airlines who have got obviously competing interests against airport and also competing between themselves. I think in practice it would be very difficult as a group for the various airlines and airports to all get together and come up with some guidelines and so certainly in our submission we have supported that proposition that yourselves might be a good group to make some guideline recommendations. But as a primary thought we certainly feel like the existing commercial negotiation processes do work and it might take somewhat protracted negotiations in some point but you do end up with outcomes that work, outcomes that support investment and outcomes that have delivered traffic growth, which is really what everyone is after.

The final area where we had commentary was on the developer cost sharing or developer contributions. We have really approached this from a fairness point of view where airports somewhat seem to be singled out as being large developers or multiple, somewhat small developments, it might be a child centre or dog kennel or whatever that get aggregated together because they're an easy target. We think that really there needs to be a clear - the concepts of need and access and equality need to be followed so that airports don't get singled out from developers that might be doing very similar activities off-airport. Just because you're on Commonwealth land shouldn't mean that you have to pay for your traffic intersections if a similar development or a similar sized development is happening elsewhere and isn't paying for that.

In some cases we recognise that, you know, given it's Commonwealth land the circumstances are different but certainly airports are also paying for things that other people don't have to pay for. They're paying sometimes rates without getting services, they're paying for voluntary contributions, they paid for the land in the first place as part of the initial concession purchases so certainly development contributions is a difficult topic and it's probably one that is being dealt with relatively well, but, by the airport management teams and at least from our perspective what looked to be quite good relationships with their local councils and with the local state governments where they are able to quite regularly come up with voluntary contribution payments to infrastructure development. Again, we think that the existing system there is working quite well and is probably a good way to keep going forward.

DR CRAIK: Thanks very much, Andrew, and thanks for your submission. Just the first question, you probably saw the ACCC chairman's recent speech about airports and being monopolies and regulation. Did you have any views about that?

MR FELLOWS (HFM): Yes, we did. Well, we did see it and there was certainly some debate internally about that. The sort of speeches pop up on our radar quite vividly because of the impact that they have to our investors and our investors'

confidence in investing in the sector. Where we haven't been opposed to this productivity commission process, at least as it was initially laid out as being a five-year review, clearly highlighted in advance it will be five years, there was probably some concern from our point of view when it was brought forward a year that that alone brings in some uncertainty. But the regular reviews is probably not a bad system.

From an investor's point of view it's quite disconcerting to see where we have this system in place of an independent group like the Productivity Commission doing an in-depth study with good engagement with a wide group of people that you have a body such as the ACCC not seeming to effectively to be playing an active or a constructive part of the debate and seeming to want to go outside the process. So I guess that is disconcerting, that if we go through this process and we reach a positive finding or a neutral finding, then that might be the end of it, whereas I guess it would be nice to see that we do go through a process, make any constructive or beneficial changes that can be made to the existing regime but that that should give us a period of stability and it's not clear from, I guess, the ACCC's media comments that they're going to let this process reach that sort of an outcome.

DR CRAIK: Thanks. One of the other things the Australian Energy Regulator has been saying is that they believe there is a need for regulatory intervention in the electricity sector in relation to investment and poles and wires and things. It's our understanding that infrastructure investors believe that the airport industry is subject to perhaps more uncertainty than the electricity industry at the moment and I was just wondering whether the AER's comments would influence your views of the relative risk rating of those different classes of assets.

MR FELLOWS (HFM): We do also monitor the AER's comments and we have regulated poles and wires' businesses as well and so I guess they're always front of mind as well, what's going on in that regulated space. I guess at the moment there are risks on both fronts. There are risks on the airports which is largely a partially regulated environment with price monitoring and on the regulator's side as well with the AER. You've also got that level of uncertainty where the building-block approach or the rate-of-return approach that they apply also seems to be subject to change.

DR CRAIK: Okay. In relation to the show cause issue now you've expressed the view that you don't support it, but you've got a comment in your submission that you're concerned that it could be subject to abuse. Can you perhaps explain what you mean by the word "abuse"?

MR FELLOWS (HFM): I guess what we're thinking there is that it will depend on the legislative mandate that the ACCC is given and the restrictions - if there are restrictions - that are placed on them when they're issuing show cause such that it is

based on evidence, that it is based on a history of evidence, that it is issued only after active dialogue with the parties involved and that it doesn't become something that could be used for either - we certainly wouldn't want to say political reasons, but timing reasons, media reasons and that all of the potential implications to commercial negotiations that might be going on are taken into account when show causes might be issued.

DR CRAIK: You've raised this issue of confidentiality or not with the show cause exercise, and our initial thought was that these are public interest issues and that it should be public. Given your comments here that the disclosure obligations of investors and where they're listed companies and things, does that indicate then that it would actually be a better practice to have them publicly disclosed in the first place by the ACCC rather than kind of leaking out to the market somehow, because that would certainly be a clearer process.

MR FELLOWES (HFM): There's probably a grey line somewhere in there, you know, during the discussion process when they're just trying to do the information-gathering, when they're trying to do the timing about when they might issue a show cause notice; or do they have enough evidence to issue a show cause notice; you know, are there circumstances that they weren't aware of, which is why they might be thinking about doing a show cause notice. I think during that discussion process it might be not at that disclosure level here and that there might be cause for it to be private. But I agree, by the time they actually make a firm decision that it's going to get issued I think the damage is probably done, from equity-raising implications to debt raisings and sort of market confidence.

DR CRAIK: Thanks. John?

MR SUTTON: Yes, I was going to explore the area of risk a bit. I think Hastings has been in Perth Airport from day one of privatisation, which is a fair while - what is it, 10, 12 years, or something of that order.

MR FELLOWES (HFM): Yes, probably.

MR SUTTON: You're in a number of these other airports. Is it Melbourne; you've got a fair chunk of Melbourne, or only a little bit?

MR FELLOWES (HFM): Between the two funds, 20 per cent.

MR SUTTON: So you've got a bit of a track record now in Australian airports under this regulatory system. Can you point to any volatility? This word "risk" keeps getting tossed around, but is there any volatility in the last 12 years on these key Australian airport assets? Has there been any major jumps or falls, et cetera?

MR FELLOWES (HFM): We've certainly seen significant volatility from an outlook perspective. Throughout 2009 when the GFC was really hitting there was certainly a big impact on what the forecast passenger numbers were, which had a flow-on effect to distributions for equity and to the valuation of equity, and in a lot of cases the airports' values were written down. So from an investor's point of view they see that and that's real to them.

MR SUTTON: Were there negative returns - - -

MR FELLOWES (HFM): Yes, negative returns.

MR SUTTON: - - - at the time of the GFC?

MR FELLOWES (HFM): What has transpired since then hasn't been as depressed as would have been forecast at the height of the GFC, but the apparent volatility to investors was certainly there and we have certainly seen volatility to passenger numbers throughout the most recent Tiger episode, with changes to the volcanic ash, even Christchurch, a lot of the airports have got quite concentrated exposures to Japan or concentrated exposures to the New Zealand family and friends and tourism markets, Gold Coast airport, you know, correlated with some of those markets, and we have seen volatility on those levels. Again going back to my earlier point, where you're building a terminal you're assuming when you build it that you're going to get decent growth for the next five or 10 years to make that investment worthwhile, and we are taking risks, along with the airlines, that those passengers show up. So we have seen that.

MR SUTTON: You are in other Australian infrastructure asset classes. There was mention of utilities. You might be in toll roads, I'm not sure.

MR FELLOWES (HFM): Yes.

MR SUTTON: But could you tell us what other infrastructure classes that you're in. Let's confine it to Australia. Then could you sort of tell me within that sort of scale, or comparing them, where airports are on the risk barometer.

MR FELLOWES (HFM): Yes, we're pretty much invested across the board in Australia. We have seaports. We have toll roads up in New South Wales. We have distributions. We have got a gas pipeline on one of our listed funds. We do have some generation, more on the renewable gas side, which is probably higher risk than airports. But everything else we certainly view as lower risk in the infrastructure space than our airport portfolio, because it's the one area where you are exposed to traffic risks. You're exposed to quite large customers, but you've got concentration risk.

You've got Virgin, Qantas, Jetstar, you know, Tiger, and if you lose any of them, like happened when Ansett left, you don't get them back straightaway, or you get them back but under very different circumstances. That's not the same case when you're dealing with a mature toll road like the M5 up in Sydney where those cars are going to be there and it's a very stable traffic forecast. Then on the really regulated side of things, with poles and wires, you've got that full effective pass-through of most of your risks and it comes down to just really what your return is, that the AER agrees with you.

Here, with the airports, particularly given the capital expansion programs that are in place, we're seeing amazing levels of capex that's needed. Perth has got its new terminal going in, that will be I think eight or nine hundred million dollars, when the airport itself is only a couple of billion dollars worth. So, relative to the size of the airport, the capital expansion programs are very high as well. So they're businesses that have been around for a long time, but you've got these quite high levels of construction risk associated with them that you don't typically have on the rest of the maturer infrastructure assets that we have.

MR SUTTON: Do you have an international fund? Are you exposed to international infrastructure?

MR FELLOWES (HFM): Yes, we have got one US infrastructure fund that has a couple of assets. Our Australian funds on the unlisted side - or actually even on the listed side - do have international investments as well.

MR SUTTON: What about airports internationally, any exposure there?

MR FELLOWES (HFM): Yes, we have got stakes in Athens Airport, Hamburg and Dusseldorf.

MR SUTTON: Any particular comparisons that are to the point here, on questions of risk? Or, are the regulatory regimes are quite different, I suppose, are they?

MR FELLOWES (HFM): Yes, they're all owned through the Hochtief AirPort group and so we're somewhat removed from that. But across those three airports it's a mix of single till, dual till, and there's so much, you know, political or economic turmoil there that the regulatory side seems to get washed out by the overall - - -

MR SUTTON: I think the Greek asset might have some risk.

DR CRAIK: I was going to say.

MR FELLOWES (HFM): Yes. But again it goes back to your earlier question around you do have risks around your ability to finance the airports in turmoil times;

you've got the risks about traffic, and in that case you've got a pretty weak national carrier with the Greek airlines.

DR CRAIK: Thanks very much, Andrew. That has been really helpful, so thanks for that.

MR FELLOWES (HFM): I appreciate that. Thanks.

DR CRAIK: Thanks for your submission. Thanks for your comments today, and thanks for your answers to the questions.

MR FELLOWES (HFM): Yes, well, we'll look forward to seeing the next steps.

DR CRAIK: Good, thank you.

DR CRAIK: Next up, Adelaide Airport. If you could state your name and position for the record and if you'd like to make a brief opening statement, that would be great. Thank you.

MR YOUNG (AA): Good afternoon and thank you for giving us the opportunity to present today. We do have some introductory remarks but before we do that, I'll introduce myself. My name is Mark Young and I'm the managing director elect of Adelaide Airport.

MR McARDLE (AA): John McArdle, general manager corporate affairs for Adelaide Airport.

DR CRAIK: Thank you. Congratulations, by the way.

MR YOUNG (AA): Thank you. We're broadly supportive of the draft report and we think that the substantial tone of it under the current regime, things have worked reasonably well, we are supportive of, but we do have two points that I'd like to amplify.

The first is in relation to the submission that Adelaide Airport made in relation to it being removed from the price-monitoring regime. We were disappointed with the Productivity Commission draft finding on Adelaide remaining in the price-monitored airports. We felt that for the compelling reasons that we put in our submission and some additional points that I will cover now that that's an area that we would request that could be reconsidered.

In addition to the reasons that we've set out in our submission, both our public and our confidential submission, in addition to that, we have a 15-year agreement which covers approximately 50 per cent of our aeronautical charges. This is an agreement for terminal 1 which was a significant piece of infrastructure, \$260 million piece of infrastructure, that was built by Adelaide Airport and opened in 2006. Those agreements have service-level agreements in them. There are substantial commercial penalties for noncompliance with those service-level agreements and there are dispute resolution clauses. It was that agreement that saw a 25 per cent price reduction at the last price reset, at least a 25 per cent price reduction offered by Adelaide Airport as part of its negotiation and a further 2 per cent price reduction ultimately agreed once the airline and airport negotiations had concluded.

We have heard that there has been in the submissions some qualified airline support for airports that do have service level agreements to opt out, at least respect to the quality of service aspects. Further to support Adelaide Airport's case in terms of not having substantial market power and as evidence of its conduct, during the global financial crisis, Adelaide Airport, notwithstanding that it had a contractual entitlement to increase its landing fees by CPI, voluntarily chose not to do so and

kept its pricing the same, and in the next yearly reset following the recovery, at least what we've seen in Australia, following the aftermath of the GFC, there was a substantial spike in the CPI in the period that Adelaide used in its negotiations or in its price advice to the airlines and we chose not to take what I'll call the inflated - or the spike in the CPI but took a far more average line through it. All of that was done in the context when our passenger traffic was growing at a rate that was less than the rate that was implicit in our agreement with the airlines when we set that five-year landing fee agreement back in 2007.

So for those reasons, we do urge the Productivity Commission to review their recommendation because we believe this submission and the additional clarifications have the propensity to tip the decision to the other side of marginal, to use an expression that was in the PC report.

The other aspect that I'd like to cover is in relation to the show cause. In addition to the remarks made by the AAA submission, which Adelaide Airport supports, I would like to amplify a couple of points. We believe that having an agreement in place that does have service-level standards and with dispute resolution clauses ought to be evidence to say there's no case to answer in terms of show cause mechanism, in particular, when you have an agreement that represents the majority of passengers that use your airport or with airlines that bring the passengers that represent the majority of passengers at your airport.

We believe that the show cause mechanism can give rise to unintended risks. One that I'll amplify is the financing risk. Reasons that have been given here in relation to why the show cause mechanism did not go any further in the last review still abound today. There are really two reasons during the global financial crisis; one was that simply just the competition for capital was in itself a major challenge, but the second was that any perception of regulatory risk would be priced into the price of debt that airlines would raise. That second risk still remains today. The competition for capital is not as fraught as it was during the global financial crisis.

However, the second reason and the larger reason is that any perception about regulatory risk in relation to a show cause mechanism will be priced then by financiers and will ultimately result in that higher cost of capital being used in terms of aeronautical landing fees. Our view is that the threat of using existing legislation is sufficient. We are aware of the costs of using the legislation that is there but in the context of Adelaide Airport and the size of the balance sheet versus the size of the balance sheet of our major customers, the cost to Adelaide Airport of defending any action under existing legislation would be relatively far more expensive.

However, that said, if there were a show cause mechanism and if it were to proceed, we do submit that the agreement should be prima facie cause for there not to be any further action under show cause. We believe there should be a substantial

and retrospective review period to evidence, if there has been, abuse of market power, but we believe that that review should include total aeronautical assets that were invested in but there also should be a fair allocation of the cost of the land and the lease premium costs in any sort of retrospective review and that any returns must include a fair allocation of the cost of funding the aeronautical capex.

In relation to the ACCC and the role of the ACCC in any show cause process, we feel as though the ACCC has its monitoring report. If it so chooses, it ought to be able to make a determination and make whatever recommendation it wants, but to follow that up with a process that then requires airports to submit their argument to the ACCC in advance in our view could almost be likened to a fishing exercise and tending towards discovery before any due process. That's our preliminary remarks.

DR CRAIK: Thanks very much. John, did you want to add anything?

MR McARDLE (AA): No.

DR CRAIK: Okay. I'm curious why you didn't actually mention - in your submission you really effectively only answer the information questions. I'm just curious, given the particular issues that you've raised today.

MR YOUNG (AA): Our follow-up submission?

DR CRAIK: Yes, your second submission didn't address those rather larger issues that you've raised.

MR McARDLE (AA): We're using the opportunity today to do that.

DR CRAIK: Are you going to put in another submission or not?

MR McARDLE (AA): We can.

MR YOUNG (AA): We'll keep that option open, yes.

DR CRAIK: Okay. I don't know if you heard the airlines speak today but they claimed that during the global financial crisis the airports didn't share any of the risk, the airlines wore it all and that airports carried on with their pricing structures showing no relief to the airlines.

MR YOUNG (AA): I think I've given you two examples of what Adelaide Airport did in that situation.

DR CRAIK: Yes.

MR YOUNG (AA): Adelaide Airport in its pricing offers airlines a mix of passengers or maximum take-off weight. It's an annual election that airlines can make and they can do that depending on their own mix and their own dynamics. So where an airline chooses for Adelaide Airport to render its landing fee charge to them on a passenger basis, then Adelaide Airport takes complete passenger risk. In the pricing agreements that we set with airlines back in 2007, the implicit compound average growth rate in passengers was around 5.1 per cent, I think. To date we achieved something just over 4. So during the global financial crisis when Adelaide Airport's traffic was running significantly behind what we expected it to be, Adelaide Airport was also sharing that risk.

DR CRAIK: You have suggested today you'd like to be removed from the price-monitoring regime on the one hand and yet on the other hand we have the ACCC's submission suggesting deemed declaration for at least some of the monitored airports and the statement from the ACCC chairman the other day about airports being monopolies and regulation. Do you have any comments on that?

MR YOUNG (AA): I don't have any substantial comments on that. We believe that the pricing guidelines that are in place have worked reasonably well, they're high level. There has been evidence of efficient airport growth. There has been evidence of high levels of investment, no evidence of market abuse and a favourable trend in agreements. If anything, that's grounds to reduce prescription rather than elevate it.

DR CRAIK: In relation to the show cause, I think I'm correct in saying what you said was that if there were service level agreements with covered a majority of passengers and they were being published that there would be no need for those airports to be part of the monitoring regime.

MR YOUNG (AA): I was reflecting comments of some airlines that there is grounds for airports to opt out at least of the quality service.

DR CRAIK: Okay. Then I think you drew the conclusion that that should make them ineligible for being considered in the show cause process. Is that what I gathered you to say?

MR YOUNG (AA): Making airports ineligible for the show cause process.

DR CRAIK: Yes, those that had the - - -

MR YOUNG (AA): I was making those comments purely in the context of Adelaide Airport and in support of all of the other examples and all of the other conduct that Adelaide Airport has undertaken to enhance its case.

DR CRAIK: I understand. You raised the issue of the previous show cause that

was put up. That was quite a different sort of process from the one - that was a complaints-based process from the show cause that we're currently proposing.

MR YOUNG (AA): Yes. I wasn't going to process there, I was going to the perception of risk by investors and banks in terms of whatever the mechanism, however it's triggered or invoked, the mere existence of its potential will result in financiers pricing that risk into funds that they lend to airports.

DR CRAIK: Our feeling was that at least in the show cause process that we have we're proposing that you would have at least an evidence-based process as opposed to a complaints process which it was and even the complaints being potentially confidential, so a much more transparent process.

MR YOUNG (AA): I understand the distinction about the trigger, it's more the effect.

DR CRAIK: Okay.

MR YOUNG (AA): The confidentiality of it, moot point, I guess, in relation to listed entities versus private entities but the variety in each company is different in terms of its documentation that it has with its financiers but I'm certain that some companies would have an obligation to disclose to their financiers and the effect is then already achieved.

DR CRAIK: I know you don't support the show cause but on that basis - we proposed it as a public process so that the ACCC would make a public statement about a show cause because otherwise it would leak out anyway.

MR YOUNG (AA): Impact was the same. Once disclosure is there, irrespective of the trigger, the disclosure is there and the potential negative impact has been caused.

DR CRAIK: Just one point you make in your submission that borrowing costs are detailed in ASIC accounts. Are they public?

MR YOUNG (AA): Yes.

DR CRAIK: Would that be the case for all?

MR YOUNG (AA): I think that does depend on your company structure. But a large private company or a public company is obliged to lodge their accounts with ASIC and that's public information.

DR CRAIK: Just one other question before I hand over to John. One of the things we have thought about is the possibility of recommending that a draft monitoring

report be published. What do you think about that? It's specified in our report.

MR YOUNG (AA): The draft monitoring report at the moment is provided by the ACCC for comment by individual airports in relation to the facts that end - some of the findings that relate to their airport. They're given the opportunity to comment on that and turn those comments back to the ACCC. What we would propose, though, is that the executive summary section also draft be provided to the airports because what we have found is notwithstanding comments that we may make on the draft ACCC report, many of which aren't picked up in the final report, but notwithstanding all of that there's then an executive summary section, a right of last reply, if you like.

To use an example, in the last one there was a scattergram used in the front to show where airports were rated in terms of their quality of service and the scale of it was such that it showed the majority of airports down in the bottom left-hand corner of the scattergram, which was not the right corner to be in. However, if you applied a different scale to it, you would bring those airports back into the middle which is where most of them turned out, which was satisfactory. But we didn't have the opportunity to comment on that. It was a fait accompli and that is the section that is picked up and commented on by most media and commentators.

DR CRAIK: The other thing we thought is about is recommending including in the final publication the airports' responses to the ACCC in the draft so that what the airports actually said is transparently obvious and whether it's picked up or not is also - - -

MR YOUNG (AA): I don't have a firm view about except that sometimes by analysing the draft report and then the final report and looking at the gaps can introduce even more conjecture. The ACCC does get the comments from the airport. They're entitled to take those comments on board and then make whatever determination they should and in terms of my earlier comments about any further process of discovery, if that were to take place - and don't take that as any support for the show cause mechanism - in our view that should take place in another place. The ACCC should make its determination and be confident its information.

MR McARDLE (AA): Could I also suggest that there would be some discipline in when those drafts would be leaked or given to the public. We would prefer that they be after all of the discussion has taken place and after the comments of the airports are taken notice of by the ACCC or not, as the case might be. But Adelaide Airport also feels that there is possibly some merit in the ACCC looking at some way of individually reporting on individual airports. This league table that they tend to run with confuses the issue because there are no two airports in this country that are the same. In some cases we're serving different market mixes and different categories of airlines services. Adelaide, for example, is a predominant domestic port, whereas some of our other colleagues are a balance of domestic and international so there is a

whole mix.

Adelaide's terminal is an integrated terminal so you get fly in, fly out, charter, regional, domestic and international in the one building. So you're assessing the quality of service against that whole raft whereas the current legislation focuses on those terminals that are run by the airport which ours is actually. So we would like to see, if it's going to continue, that there be some consideration of individually monitoring individual airports and reporting on that.

DR CRAIK: Thanks.

MR SUTTON: As I understand it, Adelaide Airport supports the AAA's position on publication of service level agreement information which again, as I understand it, is that you couldn't actually publish the detail in terms of particular airlines et cetera because that would infringe commercial-in-confidence so there would have to be some publication at some aggregated level, some high-level information and I want to query whether that really amounts to anything that's particularly useful. Is that really going to assist the travelling public and/or regulators? What's your view on that?

MR McARDLE (AA): I think properly constructed service level agreements are all about the one common goal, which is safe, secure and efficient facilitation for passengers. So whether they're public or whether they're an arrangement between the airport and the airline, as long as they're focused on that outcome, that will be achieved. But whether there is public interest in that, I don't know. I can't speak for the public.

MR SUTTON: But in terms of regulators or anyone trying to assess the state of play, transparency is important. I at least perhaps share a view that the primary thing here is to try and get the service level agreements in place that have got recourse to penalties and there is a sharing of responsibility, reward, risk et cetera. That is obviously important but I think there is also some utility in the public awareness of at least some level of the detail but it's not at all clear that there would be much useful detail at all that would be publicly available.

MR McARDLE (AA): I think what is just as important, however, is the construction of service level standards that are appropriate to the airport, that are unique to that position because one size doesn't fit all and each airport is different. In our case we're a common user terminal, we have all of the airlines at the airport using the one terminal, domestic and international. That's completely different to service level standards at other airports, even those that do have some common user terminals.

MR SUTTON: We do raise the issue of some possible additions to the pricing

principals and/or voluntary code of conduct et cetera and there is talk about the idea that if some of the things that currently drag out the negotiations - and often you hear it said that people are reinventing the wheel or they're having the same arguments all over again that they had last time and that's turning into protracted negotiations. If we could highlight or nail down some of those regular issues that get ventilated time and again and turn them into principles and get general acceptance for those principles, then we'd be assisting the industry. So the idea of additional pricing principles and/or a voluntary code, can I ask your views on that.

MR YOUNG (AA): The existing principles have worked reasonably well. They're high level and, as I said in my earlier remarks, given the progress that has been made under the existing principles of efficient airports, high levels of investment, no evidence of market abuse and a favourable trend in agreements, the grounds really are there to reduce the prescription or reduce the principles rather than increase the prescription. One of the dangers in increasing the prescription is that again we tend to one size fits all and each airport is different. In our case an airline that has a network may want to see generic principles applied because that reduces the cost and the time of negotiation.

But from an airport perspective we have a negotiation and we deal with our customers at that time. We have circumstances that are unique to our airport and we have no difficulty under the current principles in terms of talking to airlines and other stakeholders in the airport about our capital expenditure program and when that might be due and what it should look like and the timing of it. So our view is that more prescription is likely to lead to some, again unintended, consequences and in circumstances where there is absolutely no evidence of market failure to make good progress under the current regime.

MR SUTTON: We have an information request about whether non-aero revenues constrain aero prices or charges et cetera and we've had a variety of responses from airports on that. What's your view on that one?

MR YOUNG (AA): I have to say I struggle with the concept of non-aero revenues constraining aeronautical but if I could answer that question in perhaps a slightly different way. Having non-aeronautical revenue and non-aeronautical portfolio spread of investments is a good value add to airport companies because it de-risks the cash flows from a financing perspective and that in itself results in overall lower cost of funding which then, of course, is used in airline or landing fee or aeronautical fee calculation. So having the portfolio mix of a business, albeit there's a geographic concentration of risk, having the portfolio mix does assist in de-risking the business and does assist in airports accessing lower costs of capital which is then spread across the business.

MR SUTTON: I have one last thing. I want to ask you about regional airports but

before I persist with that question, there was some speculation - I saw in the media some time back that the owners of Adelaide Airport were acquiring the major regional airports in South Australia. Did that eventuate or where is that all up to?

MR YOUNG (AA): We talk to a lot of the regional airports in South Australia. We provide assistance to them in different areas. Just the other day we were helping one airport with their looming security requirements in a mentoring role, not a market-participant role. So we have a close association with our regional airports and in due course that may result in some closer relationship but at the moment that is not determined.

MR McARDLE (AA): The way it came about, commissioner, was that one of our senior executives, who is the chairman of the Australian Airports Association, was speaking at a future infrastructure summit for South Australia and the question was put to him to project out to 25 years and what he saw airports and how they would be operating in regional and rural South Australia and he hypothesised that as local governments become more and more involved in providing facilities for their ratepayers such as libraries and swimming pools, carparks, cemeteries, caravan parks and so forth, the business of running an airport may be a little bit beyond their capabilities. We heard a previous speaker today mention that it is a unique part of the local government portfolio but it does need to be able to be run at a - they haven't really come to grips with understanding what their asset value is and what the operating costs are and meeting the ongoing and fast looming regulatory demands on them and we propose that an organisation such as Adelaide Airport Ltd may be able to provide that assistance.

MR SUTTON: If Adelaide Airport were hypothetically to - or if the major metropolitan and regional airports in that state were all under one umbrella, do you share the view that would have some impact on market power?

MR McARDLE (AA): We'd need to be able to assure our shareholders it's in their interests to start with but there's swings and merry-go-rounds, I think, and Mark and a couple of others are talking with a few of the airports in South Australia about them opening their books so we can find out just how much it is costing to run that airport and then sharing with them what it's costing them to run their airport, how it could be done more efficiently. We've had the benefit of being approached by two of the larger regional ports to write their master plan for them, which we're doing as a gesture of goodwill, and in doing that we are finding that there is a lot about their airports that the local elected members don't know. So we'll be able to share that data.

MR SUTTON: Seeing as it's hypothetical I won't pursue it.

MR McARDLE (AA): Thank you.

DR CRAIK: We're trying to get some details on off-airport parking and in your submission you describe the off-airport carparking as a small percentage of those who come to Adelaide Airport. Do you actually have any estimates of the numbers of car spaces off-airport as opposed to on-airport, and we're not really talking CBD, this is - - -

MR YOUNG (AA): We can provide that information and we'll do so.

DR CRAIK: That would be really useful.

MR YOUNG (AA): Adelaide was reported in the media only just two weeks ago as being the most over-serviced capital city for carparks in Australia. But we'll provide that information to you.

DR CRAIK: Do you charge the shuttle buses or whatever they are that come from the carparking arranged places access fees?

MR YOUNG (AA): No.

DR CRAIK: Will you put that in the submission too.

MR YOUNG (AA): No, we don't charge anyone who is coming from another carpark.

DR CRAIK: So if you could let us know so we have all the ground transport access fees so we can compare them and the number of carparking spaces to compare it with Adelaide Airport as a percentage. That would be really helpful, thank you. Do you have anything else?

MR SUTTON: No.

DR CRAIK: I think that's all we've got for you today.

MR McARDLE (AA): If I might, commissioner.

DR CRAIK: Yes, go for your life.

MR McARDLE (AA): There was one issue that's been raised today in respect to aviation noise. Adelaide Airport, of course, is a curfewed airport and whilst we inherited the airport with an administrative curfew, it has since become legislated whilst we have been the operators of the airport. We are aware that as this great country of ours goes forward in carbon taxes and wanting to reduce gas emissions and so forth that we really have to look at more efficient ways of moving our aircraft

into and around our airports and monitoring and all that stuff. Consequently, Adelaide Airport, in partnership with the Australian Airports Association and Airservices Australia is hosting the second of an all of industry noise forum in Adelaide on 4 November to address the very issues of more efficient use of airspace, to accurately reflect the amount of noise reduction there has been in airframe and aircraft engine manufacture over the last 20-odd years, and I notice another airport is going to give you that data.

We're also looking at the more efficient use of the aeronautical technologies that exist in aircraft approaching and departing airports and if that is able to be used - they don't have to do circuits over Wagga or Bathurst or wherever when the aircraft is running on time but because of constraints at a certain airport you are put in a holding pattern which is then burning up more fuel, so that is going to be looked at that. In addition to that the two major airports in this country that are curfewed - there are three, of course, with the Gold Coast - but Sydney and Adelaide, the residents that are in the major and prime area have all had their homes insulated at huge cost and yet there is no recognition of that in the going forward of more efficient use of aircraft and the movement of passengers.

At Adelaide, since we took over the airport our movement numbers have decreased by 4 per cent, yet our passenger numbers have gone up by 70 per cent over the last 13 years. Aircraft are getting quieter, there are less of them, homes are insulated, there is better technologies around, so the three parties I mentioned earlier are facilitating an all of industry workshop to see what we need to do with government to move that forward.

DR CRAIK: Thank you for that. Thank you both very much, thanks for your submission and we look forward to the details you're going to send us.

MR McARDLE (AA): Thank you.

MR YOUNG (AA): Thank you.

DR CRAIK: We might just have a five-minute break while we wait for the next person to come along. Thank you.

DR CRAIK: Thanks for coming along and could you state your name and position and if you'd like to make a few brief opening statements, we'd be happy to hear from you.

MR SIOLIS (RBBE): My name is George Siolis. I'm a partner with RBB Economics. I've worked as a microeconomist for 20 years, advised clients in Australia, Asia and Europe on competition and regulatory issues, both in the public and private sector. I also worked for years at the Productivity Commission in the early 90s. I should say that the submission that we've made is in response to the commission's request for comments. We're not representing any party on any issue in this matter. The comments are made from a private, RBB capacity. I'll just make some brief comments about the submission.

Our submission has focused pretty much just on the question of market power and the implications of any finding market power for government intervention. The submission draws on our experience in undertaking competition assessments and advising clients on abuse of dominance matters and attempts to highlight some of the things that we think could be emphasised by the commission in its final report. The first point we would like to make is that the commission and most parties that have participated in this inquiry seem to agree that public policy has a role to play where a severe market failure exists. Market failure could arise when a firm has significant market power and has misused that market power in a way that reduces economic efficiency.

Assessing when a firm has a significant market power is an important part of any investigation, but it is only the first step. The assessment needs to determine whether that market power is being misused and to assess the seriousness of the market failure. Each of these three elements needs to be shown before intervention should be introduced. This year is broadly consistent with the framework presented by the commission in chapter 11 of the draft report and we agree with that framework in large part. Section 11.1 states that a case must be made that firstly, "An airport is using its market power in a way that creates distortions that detract from community welfare." Secondly, "A regulatory response is the most appropriate response," and, thirdly, "It is feasible to devise a regulatory response that can address market failure without imposing costs greater than those arising from leaving that market failure untreated."

Our submission suggested that an additional requirement be added to this list which is that it needs to be established that airports actually do have significant market power. Our submission highlights what we believe were shortcomings in the way that the commission determined whether airports had such power. Section 2.2 of our submission was critical of the lack of transparency regarding the weight that the commission placed on the factors that could determine whether airports had significant market power or not. We argued that a clearer statement supported by

empirical evidence on whether airports had significant market power was an essential first step before determining whether any further intervention would be needed in this market.

Our submission also emphasised that the commission needed to show that airports were using their market power to sustain prices that were significantly above the level of efficient costs somehow defined. This is equivalent to the first bullet point of the commission's framework, that is, whether an airport is using its market power in a way that create distortions that detract from community welfare. We were not able to identify where in the draft report this had been shown. Chapters 5 through to 8 of the draft report and draft finding 6.1, 6.2, 8.3 and 8.4 in particular did not suggest that there was any misuse of market power, let alone any distortions that were serious enough to warrant intervention.

In our view the commission did not follow the framework it set out in chapter 11 and consequently did not justify the need for its recommendation regarding intervention in this market. Our submission argued that any further recommendations regarding regulation should be applied to airports only after a stringent market power test has been met which gives more explicit recognition to the fact that controls over prices are a last-resort measure that should be applied only when competitive forces have demonstrably failed to operate effectively.

The second point we make in our submission is to amplify a point made by Gary Banks in a speech in 2003. We believe that draft recommendation 11.1 appears to try to resolve a distributional tussle rather than addressing any real competition concerns. Such a tussle should not, without evidence of economic inefficiency, require policy intervention, particularly when that policy intervention proposed is ill suited to deliver clear benefits. There is a risk, therefore, that this will cause airlines and other users of airport services to adopt a culture of complaint rather than a culture of competition and encourage regulators to arbitrate in the distribution of gains in bargaining arrangements where efficiency considerations are not at stake. Such intervention increases the risk of regulatory failure that is worse than the underlying market imperfection.

The final point in our submission is that the resources required for the ACCC to issue a show cause request and for the airport to respond to that request will mean that the parties will need to produce the sort of information that would be required in a full-blown price inquiry envisaged by Part VIIA and would lead to increased compliance of administrative costs with little offsetting benefits to economic efficiency. The commission's proposals could easily be read as an invitation to individual users and special interest groups to complain about unfair or discriminatory tariffs in a context where not even a full-time specialist regulator would be able to determined what an appropriate, non-excessive price would be that an airport should charge for a service. I'm happy to take any questions or comments

regarding our submissions or comments.

DR CRAIK: Thanks very much, George, and thanks very much for your submission. It's actually quite helpful the detailed analysis you've gone through. Thank you for that. Your comment about in the end the show cause potentially leading to a culture of complaint, our view was that the show cause was to be based on the evidence from a more rigorous monitoring program and quality of service or standard of service level agreement KPIs, percentage reporting on those, market conditions and things, so it was an evidence-based show cause rather than a complaints-based show cause which was what was proposed when the government picked up the show cause recommendation in the last inquiry. So why do you suggest that you think this can potentially lead to a culture of complaint?

MR SIOLIS (RBBE): I think for two reasons: firstly, the main point that we made in our submissions and in my opening comments were that any regulation proposed by the Productivity Commission or any intervention by the ACCC should follow a clear, rigorous process and the threshold should be quite high and that threshold should be that the operator has significant market power, that they have misused that market power, that there is significant consumer detriment and that there is a serious market failure that is trying to be addressed. They should be the criteria for guiding any sort of intervention.

Draft recommendation 11.1 doesn't capture those. That framework is there in section 11.1 of the commission's draft report but it's not actually in draft recommendation 11.1. It just says - well, you know what it says but it basically allows the ACCC off its own bat or in response to a complaint to ask the airports to show cause why - - -

DR CRAIK: It's not only in response to complaint, it's in response to the evidence from the price monitoring and the reasonable rate of return and the quality of service, the surveys and things like that and we're proposing what we think are improvements to that monitoring program and taking into account market conditions. So it's not a complaint from an airline or something like that that generates it.

MR SIOLIS (RBBE): But all that evidence is evidence that you have considered throughout the course of this year as you've put together your draft response. I couldn't find anywhere any clear statement saying that airports have misused their market power. I can't see how the same information will essentially then be used by the commission, how the commission will suddenly take that information possibly enhanced and turn that into a view that somehow shows that airports have misused their market power. What it will end up being will just be the type of dispute that you have covered in chapters 5 to 8 of your report and I can't see how any further clarity will come from that.

DR CRAIK: That's a slightly different issue from generating a culture of complaint though, isn't it?

MR SIOLIS (RBBE): Partly. The other point to make is that if the mechanism is there then a party will use it to its advantage. If a party feels that it can get a better outcome by doing that, by triggering that clause, then it will activate that. If it's in its interests to do so, then why wouldn't it? If you can activate that by trying to get the ACCC to ask the airport to show cause, why wouldn't it?

DR CRAIK: Okay. There is a regulatory regime in place now, there's the monitoring regime and the potential threat of - there's a whole range of potential threats. There is the monitoring regime in place. The ACCC concludes sometimes from the monitoring reports, makes suggestions. Certainly in the media and sometimes in the summary chapter, which are generally unqualified suggestions that there is a potential abuse of market power or a suggestion of abuse of market power, and the statement is made by airports that there are a whole range of remedies that are a credible threat for them to behave properly and, therefore, they behave all right whereas the ACCC is saying, "Well, perhaps they don't behave all right."

Our view was we have a monitoring report which leads to these statements that end up in the ether and there is no avenue for a determined action or inaction afterwards because neither the ACCC has taken action at the end of them, nor the government has taken action at the end of it. So what we're trying to introduce into that regulatory environment was so that it was actually a determined response from it so if the ACCC suggested there was an abuse of market power, then they should back their judgment to do that and give the airports a chance to respond. There's a prima facie case established to the ACCC's satisfied according to the criteria that we proposed and give the airports a chance to respond before going to a full Part VIIA inquiry or recommending a Part VIIA inquiry if that's what they think. So what we are trying to do is put a bit more determination in the process that currently exists so that it doesn't end up as these vague statements in the media.

MR SIOLIS (RBBE): I guess I keep going back to our separate point which is that any intervention should follow that clear threshold, that there needs to be significant market power, it needs to be misused, there needs to be consumer detriment and serious market failure. I mean, trying to avoid these open-ended statements and vague determinations - I can see how that might be desirable from an administrative perspective but I don't see that as necessarily a valid reason for intervening in commercial negotiations and we shouldn't think that draft recommendation 11.1 or even the ACCC's proposals to deem this, I don't think either of those are innocuous recommendations. I think they do change the nature of the commercial negotiations between the parties and if we're going to do that with this ultimate threat at the end of the day with a Part VIII inquiry which could lead to more heavy-handed regulation, then I think we need to have clearer, higher thresholds for intervention.

DR CRAIK: Right now the ACCC could recommend a VIIA inquiry and a VII inquiry could lead to deemed declaration or some other regulatory recommendation. I would be interested in your views on the ACCC proposal in their submission and the comments of the ACCC chairman on what appears to be a deemed declaration and then if it's a monopoly, it needs to be regulated.

MR SIOLIS (RBBE): I think there are a few different points there. I guess our view would be in response to the ACCC's view about deeming airports to be declared is that it has the same problems as what we think are the problems with 11.1. Instead of establishing clearly whether a firm has significant market power or whether it's misused that market power or whether there is detriment and whether there is severe market failure it chooses to just deem it, so it hides from those very difficult, very important, very challenging issues. So it asserts or assumes that there is a problem and then skips to the second limb of Part IIIA, which is arbitration. So I see their approach as having, I guess, in many respects the same problems as we'd have with 11.1 and that is that it fails to do what really needs to be done in this area.

DR CRAIK: So you don't see any value in having a staged approach to getting to a VIIA inquiry?

MR SIOLIS (RBBE): No, and ultimately I'm not sure what a VIIA inquiry - I'm not sure what the credibility of that is. I'm not really in a position to judge that because I haven't been involved in the inquiry. But it doesn't seem to me that any party is really arguing that we should move back to price control 2002 world or pre-2002 world. So I'm not sure how credible a threat is that leads to something that no-one actually wants.

DR CRAIK: I think some of the suggestions of the airlines are pretty close to price setting if they want someone to have set guidelines that set parameters and things like that and have a negotiate-arbitrate framework, so it's getting pretty close.

MR SIOLIS (RBBE): I think it is too and that's the third point we made here, that the information that you need to show cause gets you close to that anyway so I'm not sure they're that far apart.

MR SUTTON: George, can I ask, has your firm made this submission because you've been commissioned by a client or stakeholder or someone - - -

MR SIOLIS (RBBE): No, not at all.

MR SUTTON: On page 11 of your submission, third para, you seem to be making the point that we're not dealing with natural monopolies here in the case of the major airports in Australia. Is that your view, they're not natural monopolies?

MR SIOLIS (RBBE): I don't know if they are or not. I think we picked up on a point that you made where I think you said that they didn't appear to be natural monopolies because they exhibited more risk than your pipes, wires and - - -

DR CRAIK: I'm not sure we said that.

MR SIOLIS (RBBE): Yes, it's on page - - -

DR CRAIK: We might have said they exhibited more risk but I'm not sure that we say they were - - -

MR SIOLIS (RBBE): Page 235 of your drat report it said:

Moreover commission consultations with infrastructure investors found that they generally regarded airports as riskier class of assets.

So I think we're picking up the point that, I guess, infrastructure investors were making. I think on that I was struck reading some of the older 2002 PC report and the ACCC submission and some other submissions and I was struck by how much time people spent debating whether airports were natural monopolies or not and I'm not sure that's necessarily such a fruitful thing to do. A natural monopoly has got a certain definition and it's about a cost structure. It doesn't actually tell you anything about the nature of competition in the market. It doesn't actually tell you whether airports will be able to sustain prices above efficient costs or not and I think that's the fundamental question that you need to be - - -

MR SUTTON: However it is described, let me suggest to you it's not a normally competitive environment and let me further suggest that when you said a little earlier something to the effect about people interfering in normal commercial relations or words to that effect, I put to you it's not just a normal commercial environment because if they're not monopolies they're awfully close to monopolies.

MR SIOLIS (RBBE): There are many, in fact probably most markets out there that are not normally or perfectly competitive. Most firms have a degree of market power, most markets are imperfect.

MR SUTTON: We accept that.

MR SIOLIS (RBBE): So I don't think - - -

MR SUTTON: But on a spectrum - I'm not alleging perfect competition, I'm suggesting it's down the other end of the spectrum.

MR SIOLIS (RBBE): It might be but there's a risk that if we focus on cost structure of a particular market, then we might end up deducing that they're misusing their market power because of the cost structure. If you think they're monopolies or closer to monopolies, then I think you need to show that they're misusing their market power by pricing above efficient costs or reducing quality or whatever. I think you still need to do that work. I don't think you can stop by - - -

MR SUTTON: So your view is in the absence of it actually happening, the regulator shouldn't get involved. What if it's demonstrably capable of happening because there is clear market power or market imbalance, the regulator should just get out of the way or - this takes me to a point that I wanted to ask you about. Do you share the view of the PC's 2006 inquiry that in this environment there needs to be a credible threat in existence to help regulate behaviour?

MR SIOLIS (RBBE): Not unless there's - I'll go back to these points - significant market power, there's misuse of that market power, there's consumer detriment and severe market failure. I think in the absence of those, why get involved?

MR SUTTON: But the credible threat theory that was - we again in this report are leaning on that concept and in fact most parties that have been sitting where you are, whether they're airports, airlines, think that in this environment there does need to be a credible threat. The debate usually is the instruments that are in the competition act, they amount to a credible threat or, in the views of other people, they don't amount to a credible threat.

MR SIOLIS (RBBE): I don't think you'd start by putting a credible threat in place. I think you'd start by looking at the competition in a particular market and if you think that competition is not working well, if you think there's misuse et cetera then you'd want to come up with an appropriate remedy. Now, that remedy might be a credible threat, it might be arbitration, it might be price control. But I think the credible threat comes in the assessment of the options, the regulatory options for dealing with a problem that you've identified, not the potential for a problem to exist because of the market structure.

DR CRAIK: I think we - not only us, others preceding us who have looked at this issue before - assess the major airports as having degree of market power and after a period of price setting and the airports are privatised and looking at the results of that, then move to a more light-handed regulation under the arrangements where there was what was believed to be a credible threat. Now, I think the 2006 review which suggested that the countervailing power of airlines perhaps wasn't as great as people thought it had been in the previous report and our own inquiry showing even though we could not detect any abuses of market power, it seemed to us that in fact the arrangements that are in place do not provide a credible threat.

MR SIOLIS (RBBE): Yet there has been no misuse of market power that you could identify.

DR CRAIK: We could not identify a misuse of market power but it's our view that if you're going to say you've got a credible threat, you actually need to have a credible threat and that that needs to be in place.

MR SIOLIS (RBBE): Might that also not suggest that the credible threat that is currently in place is doing its job if there is no misuse of market power?

MR SUTTON: Might it not suggest the reverse that the current instruments, they're not used and yet we have a lot of people sitting where you are complaining about conduct in the industry.

DR CRAIK: Including the ACCC on the assessments that they make; you know, obviously on monitoring they make.

MR SIOLIS (RBBE): But you've been looking at this all year and you haven't been able to identify any misuse of market power. The criticism we made was that we're not even sure how you got to the conclusion that they do have significant market power. It's easy for us to sit here and point and say that you need to do a little bit more work but where's the problem?

DR CRAIK: It's our view that the way the arrangement was set up when it went from price regulation to a more light-handed set of regulatory arrangements, that there was a credible threat in place to mitigate against the use of market power. Now, while you may well be right and we certainly need to look again and how we establish whether the airports have market power to justify that part of the equation, it's our view that if you're going to credible threat you need to actually have a proper credible threat and certainly it was our view that given the lack of response to some of the ACCC's comments and reports on the monitoring reports we needed to look more closely at that and so that's why we proposed the show cause.

MR SIOLIS (RBBE): Look, I can follow that logic. The other comment on certainty I have was what particular problem are you trying to fix here? There's no doubt that the relationship between the airports and airlines seems bad. From the report, from the submissions things don't seem to be going well in terms of commercial negotiations. But in my experience negotiations between parties are often fraught, they're often difficult, they're often complicated and they're often ill-tempered. We all claim to like competition and competition provides benefits to consumers, it lowers prices, provides better quality, promotes innovation, yet it's a ruthless, ugly process. It involves competitors hurting each other. It involves people trying to steal market share from rivals to attract labour and capital from other competitors. It's not a pretty thing to watch but it's effective. I don't see why

commercial negotiations - why we would expect them to be friendly and amicable and for parties to get on.

In fact when you do have a situation where different parties are cosy, that's often when competition concerns can arise. So I don't see that the conduct and the disputes between the parties is something necessarily requiring a policy response.

MR SUTTON: George, not too many in the industry argue with the fact that the 2002 and the 2006 PC inquiries came up with useful, not just suggestions but useful principles that have been incorporated into conduct in the industry, the pricing principles, for instance, and a range of other things that the PC has come up with that has assisted the industry to work these processes. The consequence of all that is we have this light-handed regime. I don't know whether you think it's time to dispense with that and have a totally unregulated model or non-regulated but in any event many in the industry take the view that rather than just leaving it to the parties to battle it out, that the conduct of at least the PC - and may be others too - have facilitated better outcomes in the industry.

MR SIOLIS (RBBE): Given where we started from in 2002, that's probably right and we've got to the situation in 2011 where after 10 months' work you can't identify any examples of misuse of market power, so you must be doing something right. But in terms of whether we would roll back further, I don't know, we haven't got a view on that. When I spoke about the conduct between the parties in terms of negotiation, we're not promoting open slather. If one of the parties has significant market power and is misusing that market power and is causing detriment and there's market failure, we would say, "Get involved, you might need to do more in terms of regulatory interventions." So we wouldn't say, "Pull back," we'd say, "Look at the competitive situation in the market and make the appropriate regulations."

MR SUTTON: The only way you can look at it is with monitoring. You can't put the tools down and then pick it up in 10 years' time. Monitoring is about trying to have a systematic data series and follow things in some kind of systematic way. I think it's hard to do both, dispense with things but also having a good look at things.

DR CRAIK: Can you just tell me who is RBB?

MR SIOLIS (RBBE): RBB is a firm of economists that specialise in providing expert economic advice on all aspects of competition law and economic regulation matters.

DR CRAIK: Were you with someone else before?

MR SIOLIS (RBBE): Sort of. RBB are actually Derek Ridyard, Simon Bishop and Simon Baker who were the competition team at NERA up until 2002 and then

they broke off from NERA and joined RBB or set up RBB. Since then the firms has grown to about 50 people in offices in London, Brussels, The Hague, Johannesburg and Melbourne. We're the newest office, we've been around since July 2009 and there are four of us based just across the road.

DR CRAIK: I've never heard of you before but now we have.

MR SIOLIS (RBBE): We're the new entrants, we're the mavericks.

DR CRAIK: Thanks very much for coming, George. It's very helpful, so thank you. That ends proceedings for today. Does anyone want to make a brief comment at the end of today? No. We will resume again tomorrow in here at 9 o'clock. Thank you.

AT 4.41 PM THE INQUIRY WAS ADJOURNED UNTIL
FRIDAY, 7 OCTOBER 2011