



Australian Mayoral Aviation Council

**Submission in response to the Productivity Commission's
Draft Report**

Economic Regulation of Airport Services

Dated: 21 September 20



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Submission to the Productivity Commission's Draft Report in relation to the Economic Regulation of Airport Services

Introduction

This further submission to the Inquiry is by the Australian Mayoral Aviation Council, (AMAC) in response to the Commission's Draft Report of August 2011.

As advised in AMAC's primary submission, AMAC represents the interests of Local Government Councils and their communities throughout Australia that have airports located within their area or whose communities are impacted by the activities of those airports. Member Councils represent some 3.25 million residents nationally.

Price Monitoring Arrangements

It is noted that the Competition and Consumer Act and the Airports Act presently provide for the ACCC to monitor prices, cost and financial returns relating to the supply of aeronautical and related services at the designated airports. Further, that the relevant services include aircraft movements, passenger processing (including security), landside vehicle access and car parking. It is also noted that retail rental and business park activities are not monitored under the 'dual till' approach taken.

The concept of the "dual till" approach, whereby aeronautical services are treated as stand alone, is understood to be the most effective way of teasing out those costs to allow for cost comparison and assessment of those particular services.

What is at issue is the exclusion of all other on-airport commercial activities from appropriate assessment.

Since the privatisation of the monitored airports there has been a considerable and diverse investment in non aviation activities by each of the lessees. Based on the Commissions own data (Table B), non aviation related earnings as a proportion of total earnings are recorded as:

Adelaide	43.8%
Brisbane	57.5%
Canberra	80.1% (inclusive of terminal services)
Melbourne	57.8%
Perth	64.5%
Sydney	45.7%

To continue to confine monitoring to aeronautical activities alone excludes a major economic driver and appears to reflect the pre-lease era of the Federal Airports Corporation where there was little attention paid to the development of a non aviation income base.

AMAC acknowledges the value of a broader income base, not only in terms of the airport lessee's bottom line but in offsetting what could otherwise be higher aeronautical charges and the potential exposure from fluctuations in returns from those aeronautical services.

It is because of this nexus between aeronautical and non-aeronautical activity and the potential to cross subsidise that exclusion of non-aeronautical activity proves questionable. The fact that the ACCC currently monitors aeronautical services, overall revenues and costs, operating margins and calculation of EBITA but sidelines some 50% of commercial return seems nonsensical.

Further too, as stated in AMAC's original submission, the primary business of airports is, and must remain, the delivery of aeronautical services. For this reason it is critical that the physical capacity to expand delivery of these services to meet forecast growth in demand is protected. In this regard there must be a mechanism to evaluate the impact of non aviation income expansion against the medium to long term capacity to deliver effective core services.

While some of the monitored airports hold substantial tracts of undeveloped or underdeveloped land allowing a certain buffer in the development of non aviation income streams, others do not. Greater attention needs to be given to ensuring that the capability to continue delivery of core services is protected.

Finally, on this point, a substantial amount of non aviation development is in competition with commercial operations off airport. In terms of national competition policy and a 'level playing field' for business, it is important that there are comparative opportunities and constraints available to all parties.

One element of this equity is the notion of 'developer contributions.'

The Commission has expressed a view that '*where infrastructure upgrades provide comparable benefits to airport and non airport related traffic, it would be better funded by government.*'

Further, '*where the benefits are not equally shared, it does not automatically follow that airports should be required to pay developer contributions to contribute to the cost of infrastructure outside the airport boundaries.*' However the Commission is seeking further views on this.

The flip side of this proposition is that, where infrastructure upgrades are required, they must be paid for by local residents through their rates or by State or Federal taxpayers across the relevant States or across the nation.

In the case of major off airport development proposals it is common for the developer to make a contribution to certain assessed additional costs projected to be brought about by their development. Those costs are often assessed across a wide range of both infrastructure and service provision considerations.

If the leased airports are properly viewed as a commercial entity undertaking a range of developments on site that will impact on, not only access infrastructure, but a range of public assets and services, it is reasonable that they make an equitable contribution to the provision of infrastructure or the additional cost of increased service demand. After all, these developments are undertaken with the objective of increased commercial return and are responded to by increased numbers of users and increased staffing levels to service these needs. These in turn place additional demand on a wide range of services and facilities outside of the airport gate.

It is acknowledged that the airport lessee is responsible for the provision of access and other infrastructure within the airport boundary. However, this is no different to the impost on the development of undertakings such as a business park, a shopping centre or a residential estate where those developers are required to make relevant contributions to fund additional demands on infrastructure and services.

It is appropriate that the required construction of assets or the expansion of public services is undertaken by government but that all parties contribute equitably to the cost of increased demand on these facilities or services.

The Commission notes that there are differing regimes in place in various jurisdictions for the calculation and assessment of contributions, suggesting that would add to the complexity of establishing a viable assessment methodology.

The response to this is that the assessment regime for developments in place in each jurisdiction is the most appropriate to apply to both on and off airport development in that jurisdiction. That would allow for equitable rules for commercial undertakings on either side of the airport fence. The basis on which these charges are assessed may need to be reviewed in terms of any unique activity generating development on-airport. However commercial or business park type developments on-airport appear to readily correlate with the same types of developments off-airport.

Non Aeronautical Income as a Constraint to Aeronautical Charges

As already stated in this submission, AMAC acknowledges the benefit to airport lessees of spreading risk/return across a range of income streams. It also acknowledges the need for reasonable commercial return to generate a suitable level of investment.

The issue of whether non aeronautical income will dampen the propensity to increase aeronautical charges will vary between airports and will be dependent on the availability of alternatives and the opportunity cost of accessing those alternatives.

As stated Melbourne and Brisbane have notional competitors in Avalon and Gold Coast respectively. These are notional in terms of the reason for travel and point of destination of the traveller. As an example, a business traveller with business in the Brisbane or Melbourne

CBD is unlikely to be swayed towards use of the notional alternative arrival point unless there is an overwhelming differential in cost. This is due to the greater isolation of the individual business traveller from the direct impact of the cost differential as well as the lost productive involved in increased ground travel time and cost.

Adelaide, Perth and Sydney have no effective competition in terms of proximate alternatives. This, together with the fact that air travel is the most viable, if not only alternative for many intra and interstate travellers and certainly for international travellers, means an effective monopoly control and therefore a substantial capacity to raise both aeronautical and non aeronautical charges above what might be achieved in a truly competitive environment. If people need to fly then airlines need to access those travellers through the most readily accessible airport while the travelling public has little alternative but to meet both the associated and distributed costs imposed.

Capital Cost

The Commissions Draft Report indicates that the costs of capital such as borrowings are not presently incorporated in the ACCC's monitoring charter and goes on to ponder the complexities of assessment, the potential cost to lessee's in providing the information and the fact that an imperfect measure would still be delivered.

The Australian Airports Association informed the Commission that the cost of finance is the highest single expense running at between 50% and 70% of total expenses. As a consequence the servicing of debt must occupy a substantial proportion of the charges passed on to airport users and is therefore a critical element in assessing the equity of any charges so imposed.

As with the present disregard for non aeronautical income monitoring, the 'exclusion' of such a substantial element of the cost of doing business can only adversely impact on an informed review of returns. Furthermore it would be most unlikely that relevant figures are not already provided in order to inform both the holding company's board and shareholders and to meet acceptable commercial accounting standards.

Whether cost comparisons provide any useful information is debatable but the cost of capital is surely an integral element in making any worthwhile critical assessment of individual charging regimes.

Airport Parking

AMAC refers the Commission to its original submission.

While high levels of patronage may, on face value, indicate a cost structure that is 'acceptable' to users, this will not always be the case. The cost of alternatives in some cities and in certain situations means that driving to, and parking at, the airport is the surest and comparatively cost effective means of travel. (For example, Sydney – cost and availability of public transport or outer suburb to airport cab fare alternatives.)

A cost comparison with CBD parking rates is also flawed as there is generally wide spread, accessible and cost effective alternatives for travel from the suburbs to the CBD. The same alternatives to airports are not necessarily similarly available.

In any case airport lessees seem satisfied that paid parking is a viable investment with the majority of airports substantially increasing, or about to substantially increase their capacity.

Ground Transport

As stated in AMAC's previous submission, the integration of efficient and cost effective public transport and criticism of the lack of any semblance of this at Sydney Airport is supported.

The proposition of 'pricing' roads and a congestion tax as a tool to assist in managing congestion around Sydney Airport is both simplistic and repugnant for the following reasons:

- Introduction of a tax to influence a change in behaviour suggests that there are viable alternatives. As already noted by the Commission, public transport to the airport is extremely limited in catchment and availability as well as rail access being prohibitively priced. Furthermore Sydney's public transport system, while servicing the CBD reasonably effectively is generally operating above capacity. At the same time, access via "across town" services from dormitory suburbs to commercial centres other than the CBD are often poor, circuitous or non-existent.
- The geography of Sydney, the designed proximate location of air and sea ports and access corridors from the expanding southern and south western suburbs to centres of employment are planning decisions which were made (or perhaps neglected to be made) in the design and capacity of transport corridors. There has been little past understanding or regard for the consequences. While there now appears some increased semblance of understanding of the problems already upon port, airport commuters and residents alike, there is still little or no direct action to address the burgeoning problem in a sustainable way.
- Even if a congestion tax was viable, who would it be imposed on? Daily commuters with no viable alternative? Airport users and workers with no viable alternatives? Individual shipping containers entering or leaving the Port Botany and the airport when the corresponding use of rail in comparison to road is effectively reducing in real terms?

Clearly any such proposition would add an inequitably cost in the form of a penalty on individuals for past government indecision. In the case of Sydney the cost of the present predicament and the efficiencies to be gained by appropriate investment in sustainable infrastructure based solutions clearly has positive State and national productivity benefits for governments and business alike - particularly for the operators of the two ports.

Noise Management

The Commission has indicated that it has approached its review from an economy wide economic perspective through an 'efficiency lens.' The Commission then goes on to query the use of a blunt instrument such as a curfew to curtail night time operations and suggests that a suitable pricing regime may provide a more efficient means of management.

In this regard it is interesting to note that the Associate Commissioner identified a conflict of interest and stood aside from consideration of matters relating to both the curfew and the operating cap. This clearly suggests far wider matters need to be taken to account with regard to these issues than pure economic efficiency.

If economic efficiency can be equated to improved productivity and is our only focus then there are any number of activities which would have the potential to derive greater economic

return should regulation be weakened or abandoned. Certainly this may very well result in a huge range of social and other costs, but potential for getting more people and products from 'A' to 'B' could definitely be improved.

The proposition of removing the curfew and substituting it with suitably framed pricing is a curious one. If one were to introduce a penalty pricing regime sufficient to actively prevent activity during the curfew period then the outcome, and the resultant impact on productivity, should deliver the same result as that which is presently produced by the curfew. The reality though is that there will always be the occasion, the incentive, or potential users who are prepared to pay the price and so the level of certainty which exists for effected communities around curfew airports at present would dissolve into an incentive based case-by-case commercial assessment of viability.

The Commission has also noted a differential between the Act and the Regulation in relation to shoulder operations at Sydney. In this regard it should be noted that this was done consciously to further restrict these movements and provide improved amenity.

The Commission has also referenced the move to quieter aircraft and concluded that the noise impact is therefore reduced and so controls could be either relaxed or abandoned in favour of the new technology.

In this regard there is undisputed evidence that a new technology aircraft, when compared directly with its predecessor, is quieter. However what this conclusion neglects to recognise is that a 'quieter' aircraft is still noisy - noisy enough to disrupt amenity, particularly during night hours and during periods of sleep. It also neglects to acknowledge that increased numbers of flights and projected increases in passenger numbers and air-freight volumes must lead to increased frequency of over-flight and subsequently to more frequent and sustained impact. Finally it must be recognised that, while new technology aircraft numbers will infiltrate commercial fleets, this will occur over a lengthy period of time, and so 'old' technology aircraft will continue to operate for some time.

This results directly from:

- Operators maximising the return from current aircraft investment;
- Limited capacity of operators to finance new, more expensive replacement aircraft;
- Lead time in development and certification of new technology aircraft and their components; and
- Industries finite and diminishing capacity to build numbers and mixes of aircraft at a rate capable of meeting industry demand.

An example of a possible lead time is the fact that an aircraft which complied with a 1970's operating standard was finally precluded from operating into and out of Sydney as recently as September 2009.

The Sydney Operating Cap is similar directed. It is not only an effort to balance commercial operations with community amenity but also recognizes the constraint on operations as a result of the inability for independent concurrent operation of the parallel runways due to unacceptably reduced runway separation.

Conclusion

AMAC does not propose to appear at the forthcoming public hearings. However, should the Commission wish to explore elements of this submission further, the Commissions representative is invited to contact AMAC's Executive Director as follows:

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