

Attached is a Newcastle Airport Limited discussion paper concerning a proposal by Airservices Australia (AA) to establish a framework of cross-charging with the Department of Defence (DoD) for en-route, terminal navigation (TN) and air rescue and fire fighting services (ARFF). Defence will pay AA for its use of these services, and in return will levy charges for TN and ARFF services for civilian aircraft landing at Defence airfields. The resulting AA revenue will be applied to reduce en-route navigation charges and some TN and ARFF charges to commercial users.

The AA proposal is put forward purporting to lead to increased competition through the application of user-pays charges based on location-specific pricing. As NAL's analyses shows, the proposed charging framework in fact ignores the principles on which it is supposedly based.

NAL's analysis further shows that the brunt of the Defence charges will be borne by regional airlines, the main users of Defence joint-user airports. On the other hand, the principal benefit of reduced en-route charges will obviously accrue to the main users of air routes, ie, the major airlines. Similarly, the beneficiaries of the only substantial reduction of TN and ARFF charges (at Canberra Airport) will be the main users of that airport – again, the two major airlines. Effectively, therefore, the proposed framework will benefit the two largest airlines (albeit through no fault of their own) at the expense of regional airlines, regional passengers and, potentially, regional growth.

AA, because of its imminent corporatisation and consequent dependence on user-pays revenue, is effectively forcing DoD to apply user-pays charges for services for which it is fully funded. Moreover, at Newcastle Airport at least, the civilian operation results in no marginal cost to Defence. NAL already pays a percentage of air-side income for access to defence airside services and facilities and, so far, the RAAF has had to make no special provision to support the civilian air operation. Indeed, at the current aircraft size and frequency of commercial operations, there is no regulatory requirement for TN or ARFF services – as welcome as this support may be. Furthermore, a substantial proportion of commercial air operations occur outside of RAAF working hours under Mandatory Broadcast Zone rules when the RAAF control tower is unmanned.

In summary, because of the blind application of the user-pays principal, regional airlines using Newcastle Airport will be forced to pay for services not required by regulation. Services for which Defence is fully funded and which, in any case, are provided by RAAF at no marginal cost. The burden of these costs will be borne by regional airlines, potentially at the expense of regional growth. The main beneficiaries of reduced costs will be the major airlines (recognising that this consequence is not of their own making).

NAL and its shareholders, the councils of Port Stephens and Newcastle, seek your support in preventing the introduction of the proposed Airservices/Defence cross-charging framework.

**NEWCASTLE AIRPORT DISCUSSION PAPER**  
**AIRSERVICES AUSTRALIA/DEFENCE DEPARTMENT PROPOSED CROSS- CHARGING**  
**FRAMEWORK**

**BACKGROUND**

As part of the on-going implementation of measures 'to increase competition across a range of aviation of air services', Airservices Australia (AA) and Defence are examining a system of cross-charging for aviation-related services. A discussion paper entitled 'A User Pays Charging Framework for the Department of Defence and Airservices Australia' outlines the proposal, including a suggested framework of charges. (The paper is not attached but is available at [www.airservices.gov.au](http://www.airservices.gov.au)).

AA levies charges for air navigation or en-route services for aircraft flying in air routes in Australian airspace and for Terminal Navigation(TN) and Aviation Rescue and Fire Fighting Services (ARFF) for aircraft landing at airports where AA is the service provider. Currently, AA does not apply charges to military aircraft, and Defence does not apply TN or ARFF charges to civilian aircraft landing at military bases.

In essence, if implemented, the proposal will result in a substantial levy on Defence for the services provided by AA, mainly en-route charges, which, the paper argues, will result in a reduction in en-route and terminal navigation charges for all other users. However, Defence will recoup this by levying TN and ARFF charges on civilian aircraft landing at military airfields. At the indicative levels proposed in the paper, this will result in airlines using Newcastle Airport paying Defence an additional fee of \$16.15 per landed tonne or \$1.6 million pa at current forecast traffic rates for 1999/2000. Presumably, this cost will be passed on to passengers.

While the proposal might be viewed as a matter between AA, Defence and the airlines, its potential impact on NAL's commercial interests is obvious. Moreover, noting NAL's council ownership, the councils' community-service ethos, and the importance of the airport as the regional gateway, NAL and the Councils have a substantial and important interest in the eventual outcome.

**This paper examines the issues and attempts to derive the implications for NAL and its council shareholders.**

**The Commonwealth/Council Lease**

Under the existing lease NAL is required to pay an indexed annual base fee and a percentage levy of all air-side income in return for land use and access to RAAF facilities. In addition, annexed to the lease document is an amplifying letter from RAAF to the councils stating '*Councils will be responsible for any requirements necessary to permit operation of civil aircraft which might be necessary over and above Defence requirements.*' This provision has not been implemented to date. The same letter makes it clear that the councils are responsible for '*landside facilities in the civil area,..., and airside for the civil apron and taxiways (including lights and civil services) to the edge of the runway.*'

**The important implications, in the context of the cross-charging debate, are:**

- **So far, RAAF Williamtown has had no requirement to make special provisions for civilian operations, ie, there has been no marginal cost.**
- **The income-based levy is tied to air-side income, reflecting that the lease allows both land use and access to the RAAF facilities and services for which the new charges are proposed.**

**ISSUES**

**Location-Specific Pricing**

In para 2 the AA paper notes that '*The new aviation charging system ....builds on the Minister's reform initiatives and extends the principles of **location specific** pricing introduced in July 1998, to provide a fair, equitable and transparent system of charges...*'. However, in its key principles, the paper bases the

proposed charging system on 'market prices' determined 'by comparing Defence ports to Airservices ports with similar activity levels'. This does not seem to fit in any way with location-specific pricing principles:

- For TN charges the paper lumps Williamtown with all other airports and proposes \$7.42 which is the standard minimum (subsidised) price for general aviation users at regional and general aviation airports across the country. Again, a standard, across-the-country price does not seem to fit the 'location-specific' principles.
- For ARFF prices the paper lumps Williamtown with seven other joint-user bases, none of which compare closely, most having negligible civilian traffic. The only bases where any attempt seems to have been made to apply any location specificity are Darwin and Townsville – by far the major joint facilities, but neither of which is similar to Williamtown. The proposed charge of \$8.73 is more than twice the Defence charge for these services at Townsville(\$3.82). Presumably, this reflects the high tonnage throughput at Townsville vis-à-vis the cost of the fire services. If this is the case, then NAL's much higher usage compared with other smaller ports in its group should result in a comparatively lower charge? The point seems to be, there is no consistency in application other than the blanket use of standard charges. This ignores that the subject locations are vastly different.

#### **Williamtown-Specific Considerations**

- As noted earlier, Defence has never billed NAL for provision of services over and above that required for the RAAF's normal operation. The real or marginal cost to RAAF of NAL's air services is therefore presumed and, in fact, known to be negligible.
- Apart from Darwin and Townsville, NAL has by far the largest RPT traffic of all other ports at which these charges proposed. NAL services should therefore attract a lower per-tonne rate.
- At current frequency and aircraft type, NAL's Air services, do not require either TN or ARFF services under the regulations. In fact, many services operate outside of normal RAAF hours under MBZ rules when there are no TN services. The RAAF always maintains a level of ARFF service outside normal hours, but this is for domestic purposes and has nothing to do with civil air operations. Having said this, obviously it is advantageous for these services to be available for NAL's commercial operations, but they are not required.
- There is obvious potential for airlines to avoid the new charges by rescheduling into unmanned periods, at best inconveniencing the public and at worst leading to safety risks as pilots hasten or delay to avoid the manned periods.
- NAL's lease arrangement with Defence already takes into account the proposed charges in that the percentage income levy is based on airside revenue in return for access to RAAF facilities.
- NAL is responsible for all maintenance to the edge of the runway. At the current size and frequency, NAL's commercial operations would inflict little wear on the runway itself in comparison to the RAAF.
- Admittedly, the proposed charges do not involve NAL directly. Nevertheless, the nature of the lease charging arrangements are such as to strongly imply that Defence presumed them to be fair recompense for the services which are now the subject of the new charging proposals.

#### **Cross-Subsidisation**

The paper makes it quite clear that the total transaction is as follows:

- AA levies charges for all military traffic. ( Given that Defence traffic is mainly to and from Defence bases, by far the main charges to Defence will be en-route charges. )
- Defence recoups these costs by charging commercial rates for civil aircraft landing at RAAF Bases, irrespective of the actual costs to Defence and whether or not the services are required. Other than landing charges, this is the only avenue open to Defence given that it controls virtually no air-route traffic as such.
- The income AA receives will be used to reduce charges to all users, the main effect of which under the structure proposed will be to reduce en-route charges.
- In essence this means that aircraft landing at Williamtown will be levied TN and ARFF charges, the main effect of which will be to reduce air navigation or en-route charges. Cross-subsidisation?

It is understood that RAAF's intention is only to break even in the overall transaction ie, to recoup an equivalent amount to the impost placed on the RAAF by AA's charges (but will in fact gain about \$1.1

million pa). This might suggest that the total transaction will have little impact. However, even a cursory look at the airports involved reflects that regional airlines will be those most affected. Conversely, the principal users of AA services, particularly air-routes - the major airlines - will be the main beneficiaries, albeit unintended, of any reduction in charges. Similarly the major beneficiaries of the only substantial reduction of TN and ARFF charges (at Canberra Airport) will be the major users of that airport – again the two major airlines. Consequently, while the total transaction may essentially be zero-sum for AA and Defence, there will be a significant impost placed on regional airlines and, ultimately, the regional traveller. In the end, the big losers in this bureaucratic sophistry will be regional airlines, regional travellers, regional airports and regional development.

### **Regional Implications**

NAL already pays for its access to and facilities usage at Williamstown. To date there has been no marginal cost to RAAF. When and if a cost does arise, NAL's lease requires appropriate payment. Given this and that, in the end, the main beneficiaries of this proposal will be the major airlines through their use of the air routes, the whole exercise seems counterproductive. This is particularly so considering the impost will be borne ultimately by regional air travellers.

**Regional Air Fares:** As the foregoing analysis indicates, regional airlines and their passengers will suffer the main impact of this proposal. Almost inevitably an increase in regional air fares will result, just at the regions were beginning to benefit from improved competition in the domestic market.

**Regional Growth:** Since the earthquake and the closure of BHP, the Federal Government has recognised the need for special assistance for the Hunter Region. This has led to important support for recognised growth centres within the local economy. Newcastle Airport has been one such centre with a proven track record as a catalyst for growth. Passenger throughput has increased from 56,000 pa to 200,000 pa since the councils created NAL to manage and develop the airport in 1993. Over the same period on-airport jobs have grown from one or two to close to 400, including the BA LIF activity, Impulse Airlines' Regional Maintenance Centre, Newcastle Helicopters, and airport support staff. There are imminent prospects of a high-quality on-airport hotel, a further regional airline and additional aerospace facilities for Impulse. Recent analysis indicates realistic prospects for Newcastle as a trans-Tasman link. A downturn in air traffic due to such a dramatic hike in air charges could place all this development in jeopardy, negating State and Federal investment to date in the airport. The State Government now recognises that, in terms of regional development, Newcastle Airport and the sea port are the most significant pieces of infrastructure within the Hunter.

**NAL's Future:** NAL has just completed a \$5 million redevelopment to cope with growth so far and to position the airport to continue to develop as the regional gateway and to support regional growth. This included \$1.5 million of Federal Government Hunter Reconstruction funding. This proposal jeopardises that investment.

### **Relief of Sydney**

NAL's direct-route strategy provides an important contribution to the relief of congestion at Sydney Airport. More than 100,000 of NAL's passengers fly directly to Melbourne and Brisbane, saving over 200,000 passenger movements annually through Sydney. The AA proposal is inimical to this important and largely unrecognised contribution of Newcastle Airport.

### **Generating Policy**

The discussion document, which may be summarised as proposing market-based pricing that will considerably disadvantage regional aviation is purported to build on the Deputy Prime Minister's November 1999 policy on aviation reform. That statement is fully entitled 'A Measured Approach to Aviation Safety Reform' and may be found at <http://www.dotrs.gov.au/aviation/safety/>. As the title suggests, the paper deals almost entirely with air safety rather than cost recovery issues. In the section discussing AA the concept of competition to AA services is introduced linked to a subsequent winding down of AA responsibilities. A new regulatory framework would see the Civil Aviation Safety Authority (CASA) having the responsibility to oversight AA's activities. Specifically the policy statement notes:

- *'The Government has given CASA a 30 June 2000 deadline to finalise standards for air traffic control services and the provision of rescue and fire-fighting services.'*
- *'The new regulatory framework will make it possible for new operators to provide control tower and rescue and fire fighting services in competition with Airservices.'*
- *'The introduction of competition is aimed at producing a reduction in the cost of providing tower services at regional and general aviation airports. The Government currently subsidises these control towers, because it would be too expensive for the aviation industry to use the airports otherwise.'*
- *'Airservices is developing, for the Government's consideration, a program of airspace reform.....to address timeframes, priorities, and mechanisms for implementation. It will be developed in close consultation with industry and other key stakeholders including the Department, CASA, ATSB and Defence. The program will be ready for consideration by Government by the end of 1999.'*

Neither the CASA standards for provision of services nor the AA program of reform have been developed.

The clear intent of the policy is that regional aviation should not be disadvantaged by any changes; that changes should only be introduced in pricing terms where they are cost-based, not market-based; and that lower costs should become possible through competition - which may not be feasible at Defence bases. The proposed cross-charging framework does not measure up to the policy on which it is allegedly based.

#### **Cross-charging and Government-Funded Departments**

AA is an authority in the final stages of preparation for corporatisation and self-funding through user-pays revenue. On the other hand, Defence remains largely government-funded. This proposal results in a Government-funded department being forced to apply user-pays charges for fully funded services which are provided at no marginal cost, simply to defray costs imposed by an authority which depends on user-pays revenue. There is probably no marginal cost to AA in the provision of the services to Defence. Moreover, the complete equation is reported to result in a net loss to AA of \$1.1 million pa. The question arises – is the user-pays principle out of control?

#### **CONCLUSION**

This proposal will have little or no effect on the income or expenditure of either the RAAF or AA. However, for a small degree of benefit for the principal users of AA-controlled air routes, it will place a significant burden on regional airlines and regional air travellers. As a consequence, there is a very real prospect of an adverse impact on regional airports and regional growth, a consequence probably unforeseen by AA and, no doubt, unintended by Government.

Despite the high-sounding principles expressed in the preamble of the AA paper, the fact remains that this proposal has nothing to do with location-specific pricing and perpetrates a classic example of cross-subsidisation of major airlines' en-route charges (albeit unintended by them and probably not very significant to them) at the expense of regional airlines and, potentially, regional growth. More specifically in relation to Newcastle, the proposed framework will result in a significant and inimical change to the environment which existed when the councils agreed to lease the airport from the Commonwealth.

**RJ Bomball, Chairman, NAL, 30 November 2000**