Department for **Planning and Infrastructure**
Government of **Western Australia**

Aviation

Your ref:
Our ref: DPI/04/0666
Enquiries: Sean David

14 September 2004

Ms Margaret Arblaster
General Manager – Transport and Prices Oversight
Australian Competition and Consumer Commission
Box 520J
Melbourne VIC 3001

Dear Ms Arblaster

Airservices Australia Draft Price Notification – August 2004

The Australian Competition and Consumer Commission (ACCC) have issued a paper seeking public comment on a pricing proposal by Airservices Australia (Airservices). The Department for Planning and Infrastructure (DPI) has consulted with stakeholders at Perth and Jandakot airports in Western Australia (WA) in relation to the pricing proposal, however this submission represents the view of DPI, not the aviation industry in WA.

As DPI is not an operator, either of an airport or an aviation service, we are unable to comment on some of the issues you have asked to be considered in relation to the efficiency and costs of Airservices operations. DPI has only commented on issues relevant to its areas of interest. In respect to issues the ACCC have identified in relation to the proposed pricing structure, DPI offers the following comments:

1. *The ACCC seeks comment on the effectiveness of Airservices consultation processes and its development of the draft price notification and the extent to which the proposal is supported by you or your organisation.*

   Response

   DPI is concerned that the level of consultation undertaken in WA in relation to long term pricing was insufficient. It is understood by DPI that there was limited consultation with organisations at Perth Airport, being the airport owner and one airline. Similarly, feedback from stakeholders at Jandakot Airport indicated that the consultation with them was not comprehensive. Neither the Minister for Planning and Infrastructure's office or DPI was consulted by Airservices during their visit to WA between 16 and 18 June 2004.

   Following the feedback provided by DPI and stakeholders at Perth and Jandakot airports on location specific pricing, there was no consultation by Airservices on the current price proposal with DPI prior to submission to the ACCC.

Jandakot Airport Holdings (JAH), the owner of Jandakot Airport, purchased the lease at Jandakot Airport in 1997 in good faith on the understanding that affordable air traffic control services would be provided. The Memorandum of Understanding accompanying the lease documents indicates that Airservices would negotiate any price increases with the airport owners. It does not appear that this process has been followed. In addition, reductions in operations will affect JAH's return on investment and their charges are likely to rise as a result.

Whilst the most current proposal (August 2004) delivers significantly lower price increases for users at Jandakot Airport (71% over 5 years, down from 500% over five years under location specific pricing), DPI does not support the current proposal, believing that there is a public interest case for preserving General Aviation (GA) activity and in this regard, DPI prefers a National Network Charge that would take advantage of economies of scale at international airports.

2. *The ACCC seeks comment on the appropriateness of the risk sharing arrangements embodied in the proposal, in particular relating to the activity trigger mechanism, the approach taken to changes in Airservices' capital expenditure program and changes in regulation.*

<u>Nil Response.</u>

3. *The ACCC seeks comment on the efficiency with which Airservices provides its services, including:*

- *the level of estimated operating costs reflected in Airservices' proposal*
- *Airservices' incentives to, and effectiveness in, containing and reducing costs*

<u>Response</u>

Airservices is a monopoly service provider for terminal navigation services in Australia. On this basis, DPI believes it would be appropriate for Airservices to demonstrate some comparible benchmarking to similar service providers in other countries.

4. *The ACCC seeks comment on the efficiency of Airservices' proposed capital expenditure program, including:*

- *the appropriateness of the capital projects included within the proposal*
- *the level of the estimated costs of the capital expenditure proposed*
- *the approach taken to determining the capital expenditure program over the period covered by the pricing proposal*

<u>Nil Response.</u>

5. *The ACCC seeks comment on:*

- *the efficiency of Airservices' asset base*
- *the appropriateness of Airservices' new values for its asset base*
- *the appropriateness of revaluing assets which previously had a zero written down book value*

Response

DPI notes that the current tower at Jandakot Airport was built in 1963 and contains only basic infrastructure for Terminal Navigation. Airservices have not indicated what value the tower asset has been assigned in determining the asset costs at Jandakot Airport, however DPI suggests that it should be minimal.

6. *The ACCC seeks comment on:*

- *the appropriateness of Airservices' proposed rate of return on capital*
- *the proposal to apply a transition to a higher WACC by different rates of return in each year*
- *the extent to which the proposal will act as an incentive on Airservices to achieve increases in productivity*

Nil Response.

7. *The ACCC seeks comment on the reasonableness of Airservices' activity estimates.*

Response

DPI and the major operators at Jandakot Airport and JAH consider that implementation of the proposed price at Jandakot Airport would result in a significant decrease in total activity at the airport. This would appear to indicate that the future volumes might be significantly less than forecast, which will impact on Airservices cost recovery.

There is potential for Australia to lose all international airline flight training schools to overseas competitors if the proposed prices at GA airports are implemented. At Jandakot Airport, this would have a significant impact on Airservices assumptions for activity and cost recovery, as the international flying schools currently account for over 40% of aircraft movements. This would also have serious implications for JAH, who as indicated above, may have to raise prices for remaining operators, which would lead to a further decrease in activity.

It is noted that Airservices estimate for activity do not appear to be dependant on price. The estimated activity at Jandakot Airport under the current proposal of $12.69 per tonne is 77,000 tonnes in 2008 and is not significantly different from the estimate under location specific pricing of 76,000 tonnes at a price of $44.64 per tonne. It is also noted that Airservices have stated in their draft price notification that determining the reaction of the market to this pricing proposal in isolation would be extremely difficult. However, it appears shortsighted to not make some reasonable adjustment given the magnitude of the price increases.

Airservices have stated that significant changes in activity levels will trigger potential courses of action including agreement to change cost levels via a change in service levels, a rescheduling of capital expenditure or seeking a price variation through the normal price notification process. There is no detail in regard to who the parties to any agreement to change service levels or what consultation Airservices would undertake if it was to consider cutting costs. It is assumed that the 'normal price notification process' refers to Airservices seeking approval from the ACCC.

8. *The ACCC seeks comment on whether the proposed method of cost allocation is appropriate.*

Response

As indicated previously, DPI supports a National Network Charge that would take advantage of economies of scale at international airports. There are a number of options in structuring a National Network Charge:

- Networking across all airports, both GA and international, enabling Airservices to recoup costs with little or no increase in fees at GA airports and removing the need for any Commonwealth subsidy. Options within this are to:

  i. network terminal navigation costs across all airports and separately network aviation fire and rescue services across the airports that receive those services; or

  ii. network both costs across all airports.

  Both options provide significant price reductions at the majority of airports. Based on the figures provided by Airservices for location specific pricing, DPI estimates that the cost per landed tonne for terminal navigation services only would be less than seven dollars.

- Recognise the fundamental differences in aviation activity at GA and international airports and network each separately. This option would require continuation of the Commonwealth's subsidy currently funded from the aviation fuel levy to ensure affordable prices at GA airports.

According to Airservices draft price notification the allocation of indirect costs in the current proposal is based on the landed tonnage at each airport. It is the State's preference to see all Airservices costs distributed on this basis as a National Network Charge.

9. *The ACCC seeks comment on the appropriateness and efficiency of the application of a capital city 'basin' approach to charging for terminal navigation services.*

Response

Whilst the basin approach provides significantly lower prices for GA airports, it still presents a number of problems in WA:

- After five years there will be a significant variance in price between Perth and Jandakot airports, with terminal navigation prices being 47% greater at Jandakot Airport. Perth Airport does not present as an alternative to Jandakot Airport for operators affected by the increased costs.

  It is more likely that activity will migrate to uncontrolled airfields, putting greater price pressure on the operators remaining at Jandakot Airport, and reducing safety in WA.

- Perth Airport does not gain any benefit from economies of scale as landed tonnages increase at the airport over the life of the agreement. Perth Airport's price is fixed at October 2004 and as tonnages increase over subsequent years, the increased revenue is used to subsidise operations at Jandakot Airport. Operators at Perth Airport have indicated that they do not use, or have the option to use, any facilities at Jandakot Airport and are therefore disadvantaged by the cross subsidy.

- Perth Airport, as the sole international airport in WA, competes for international services with international airports located on the eastern seaboard. Perth is disadvantaged under the current proposal, with its prices being significantly higher than Brisbane, Sydney and Melbourne airports.

DPI sees little difference between cross subsidisation at a national level and within a state basin. Airservices have indicated that the basin approach offsets the risk of operations migrating from Jandakot Airport to Perth Airport, however the DPI believes that there is little risk of this as the nature of the operations at each airport is fundamentally different.

10. *The ACCC seeks comment on the appropriateness of the phasing in of proposed price increases stemming from both changes in the structure of charging and from projected cost (operating and capital) increases.*

<u>Response</u>

Airservices draft price notification states on page 12 that at some small ports the transition to assessed revenue target may take more than five years and further, on page 28 it states that most regional terminal navigation services will reach or be close to full cost recovery.

Stakeholders in WA have received contradictory advice in relation to Airservices pricing model beyond the five year proposal submitted to the ACCC. Whilst it is recognised that phasing in price increases is preferable to the previous proposal of increasing prices by 454% in one year, the uncertainty in regard to the long term price model makes planning future infrastructure and development at airports difficult.

Airports are required under the Commonwealth *Airports Act 1996* to develop Master Plans every five years forecasting development out to plus 20 years, however at this stage, Airservices has provided no clear information in regard to their philosophy with regard to a pricing model beyond 2008/09.

Issues that Airservices need to clarify in relation to the current model include:

- Is it intended under the current proposal that prices at GA airports will continue to rise after 2008/09?
- What are the anticipated maximum prices at GA airports?
- When are they expected to occur?
- What happens to prices when full cost recovery is reached within each basin?

11. *The ACCC seeks comment on the appropriate method of achieving Airservices stated aim of avoiding cross-subsidies and on the appropriateness of the levels of cross-subsidies between services and between user groups contained in the pricing proposal.*

More generally, the ACCC seeks comment on:

- *whether the proposed prices provide appropriate incentives for Airservices to provide services at particular locations;*
- *whether the proposed prices provide appropriate incentives for users of Airservices' services to provide services at particular locations.*

Response

It appears that major airlines will benefit from operating at international airports where the price per tonne is significantly lower that at GA airports. Under Airservices proposal, operators at Jandakot Airport are charged prices 47% higher in 2008/09 compared to operators at Perth Airport.

The major airlines, because of the high volume of flights and passengers have much greater capacity to absorb price increases than flying schools or charter operators operating at GA airports, however it is the latter who are facing the greatest impost under Airservices proposal.

Further comments on the impact on users of Airservices services are provided under point 12.

12. *The ACCC seeks comments on the likely impact of the proposed prices on the users of airports and air traffic control services. In particular, the ACCC seeks comment on the likely impact on:*

- *demand for air travel*
- *airline scheduling decisions*
- *providers of other aviation services*
- *airfares*

Response

As outlined previously, there is unanimous agreement from stakeholders at Jandakot Airport that the demand for services would significantly decrease if the new pricing proposal is introduced. This would severely affect the businesses at Jandakot Airport and surrounding areas that rely on the aviation activity at the airport. Many businesses at Jandakot Airport have long term lease agreements with the airport owners that would preclude them from relocating.

In the case of those businesses without restrictive leases, it may not be possible for them to relocate to Perth Airport due to the nature of their business.

The price of aviation services would almost certainly rise, as a result of the combination of recovering the increased tower charges from users and the reduction in economies of scale through the decrease in operations. Non-profit organisations such as the Royal Flying Doctor Service would be severely affected by the impost of the new charges.

Furthermore, the effects of the proposed pricing increase would flow on to the support and maintenance operations at the airport as well as other ancillary services in surrounding areas, and would also most likely affect air charter services to regional centres.

Jandakot Airport currently employees almost 750 people at over 200 businesses, contributes approximately $500 million to WA's economy and generates $40 million in export income annually. As indicated previously, there is a significant risk that the proposed price increases could reduce operations at Jandakot Airport by over 40%, resulting in significant job losses and economic impact to the State. This is compounded by the fact that JAH would be forced to increase its prices to obtain a return on their investment, or ultimately close the airport, as it would be uneconomic for them or any other operator to manage.

Jandakot Airport is an important piece of transport infrastructure servicing Perth and the entire State. DPI is most concerned that if charges at Jandakot Airport continued to rise, where Jandakot Airport was more expensive than Perth Airport, then ultimately the airport would be no longer viable and would be forced to close, which would be unacceptable for the State.

DPI urges the ACCC to consider the long term and approve a charging structure that is considerate of the general operation at an airport, whether it is GA at Jandakot Airport, or passenger operations at Perth Airport and where costs to businesses are affordable and non-discriminatory.

The State has an interest to ensure that Jandakot Airport can continue to operate as the main GA airport serving Perth and DPI feel sure that JAH, on accepting the ownership of the airport from the Commonwealth, had an expectation to retain ownership for the full term of the lease, 50 years, with a 49 year option.

DPI is willing to meet with the ACCC to discuss these issues. If you believe that this would be appropriate, please contact Sean David, in the Aviation Policy Branch on (08) 9216 8731.

Yours sincerely

Greg Martin
Director General