



10 September 2004

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

Dear Ms Arblaster

Airservices Australia – Draft Price Notification (August 2004)

The RAAA is of the view that the ACCC should object to this Draft Price Notification.

On 31 August 2004, the Minister for Transport and Regional Services issued a directive to Airservices pursuant to the Airservices Act 1995 in relation to the provision of ATC control towers and approach radar control services. Airservices is reported as saying that complying with that direction will cost as much as \$150M.

This direction was given without any consultation with industry, would appear to fly in the face of over nine months consultation with the industry on NAS Stage 2b, has not been subjected to any safety case or cost/benefit analysis that the RAAA is aware of and would appear to be politically motivated.

The introduction of such a massive cost at this late stage, without any indication as whether or not and to what extent the Government will back this intrusion into the proper safety or economic driven provision of air traffic services with a subsidy to Airservices, destroys the whole basis of Airservices costings in the current Draft Price Notification.

For these reasons alone, the ACCC should object to the Draft Price Notification.

Should the ACCC not object to the Draft Price Notification on this basis, our views on the Notification before the unwarranted intrusion are detailed below.

The RAAA responded to the draft long term pricing proposals which Airservices put out in June 2004, to the effect that the Association was genuinely fearful that those proposals, if put into effect, would have effectively decimated regional aviation and thereby have destroyed essential services to rural and remote communities in Australia.

The modified proposals in Airservices current notification to the ACCC, in our view only, delay and drag out that decimation.

Unless there is both a concerted effort to reduce or terminate services where they are not justified and there is rigorous cost control within Airservices, the prices as now proposed will over time drive general aviation out of the GAAP and towered regional airports. A majority of the business driven out will not survive elsewhere. The impact on the few businesses which remain will be a significant downturn. That inevitable downturn will reduce the number of users paying Airservices charges and, if past performance is any guide, Airservices will seek further price increases.

The RAAA's views in relation to the matters on which the ACCC has sought comment in its Issues Paper are –

The effectiveness of Airservices' consultation processes in its development of the draft price notification and the extent to which the proposal is supported by the RAAA.

To the extent that Airservices is constrained to take its costs and divide them by its perception of the prospective usage to reach a price, Airservices has been reasonably open. However, too many of the issues, such as tower closures or levying charges on a per passenger basis, have been left over for consideration during the life of the arrangement.

The proposal is not support by the RAAA.

The appropriateness of the risk sharing arrangements embodied in the proposal.

If Airservices were a genuine competitive provider of services and potential users had a real choice to reject its services, there would be no risk sharing with the so-called "customers". In a proper competitive market the risk taker would be the shareholders. If there is a risk to a monopoly provider that risk should be borne by its "shareholder", ie, the Government. This is more particularly so when that "shareholder" directs the providing of services which are not justified on economic or safety grounds and which are not requested or required by "the customers".

The efficiency with which Airservices provides its services.

Airservices notes at p22 of it Draft Price Notification

The focus of regional and GA concerns with regard to the cost effectiveness of the organization was on overall affordability and the concern that as a monopoly, there were few incentives to operate efficiently. These concerns should be ameliorated to a large extent by the targeting of a lower WACC and a proposal that offers affordable prices.

Notwithstanding the modifications made to Airservices original proposals, the affordability issues still remain – see above. We would dispute that the revised proposals offer affordable prices.

Simply delaying the full impact of the proposed WACC by phasing it in over several years does not adequately address the efficiency issue. There simply are no proposals in the Draft Price Notification, other than vague intentions to review or to address the provision of services where the volume of traffic does not justify them. Moreover, Airservices maintains its intention to bring all towers to "profitability", even beyond the five years covered by the Draft Price Notification.

The efficiency of Airservices' proposed capital expenditure program

Given that this program appears to have been turned on its head by the Minister's direction of 31 August 2004 – an apparent addition of several tens of millions to a proposed \$542M program – there is little basis on which one can comment.

One detailed issue that concerns RAAA is the provision of for upgrading Class D towers, particularly at Albury where RAAA considers the tower should be closed.

The efficiency of Airservices asset base, the appropriateness of Airservices new values for its asset base and the appropriateness of revaluing assets which previously had a zero written down book value

No Comment.

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.

In RAAA's view this issue should be approached only after one has decided whether you wish to compare Airservices with a commercial operation subject to the full competitive force of an open market or with a government monopoly service provider. In the RAAA's view, Airservices can only be regarded from the latter view, no matter what the Government's intention might be, because that is the reality.

From that perspective, there is no justification for such a high rate of return. Anything above a reasonable return on investment to permit cost efficient replacement of assets and sensible provision of services, which allows a dividend to be paid to Government, is effectively double taxation.

The phasing in of such a high WACC does not alter this basic situation.

A guaranteed rate of return, albeit phased in, also seems to the RAAA to remove any incentive for Airservices to make their operations more efficient.

The reasonableness of Airservices' activity estimates.

The RAAA notes that the IATA forecasts in Appendix 5 to the Draft Price Notification were not categorized in the same manner as Table 4 on p25. The growth predicted for Regional Airports and General Aviation Airports seems intuitively to be wrong. From BTRE AVSTATS, Regional Airline hours flown decreased by 6.6% between 2001/02 and 2002/03 and in the same period all General Aviation hours flown (excluding Agriculture, which would not normally use towered airports) increased by only 1.3%.

The RAAA continues to believe, that notwithstanding the changes in the current proposals, the price increases are still more than sufficient to dampen demand at towered regional and GAAP airports. Accordingly, the RAAA thinks the comment at p25 –

Consultation with airports and other customers...has suggested that the regional and GA airport forecasts are optimistic, as significant price increases are likely to result in a contraction in demand.

remains correct.

Whether the proposed method of cost allocation is appropriate

The RAAA considers the “basin” approach is preferable to full location specific pricing. The RAAA, however, considers that network pricing is the most appropriate method – particularly at regional airports where the level of service is dictated by the major users (eg. the level of ARFF services), but the smaller users are forced to pay for the higher level.

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.

The proposed phasing is much preferable to the “big bang” originally proposed.

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

The RAAA believes this request for comment is based on a false presumption. Simply because services are or must be provided for the major carriers does not mean that, when they are used by others who neither need them nor request them, that those other users are being subsidized by the major carriers. In the RAAA’s view such charges should be imposed differentially or not at all on those other users. Especially where the level of service is dictated by the requirements for the major carriers, it may well be argued that anything other than differential charging, in the absence of network pricing, is the subsidization of the majors by the operators who can least afford it.

Network pricing is the best way in which to balance the issue of fairness and efficiency.

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 to provide services at particular locations

The RAAA fears that the proposed prices encourage Airservices to provide services at locations where the provision of services is not justified on either a cost/benefit or safety basis.

The RAAA notes that in the original proposals Airservices stated that –

From January 2005, the minimum level of ARFF service provided at each aerodrome will be determined by the largest passenger aircraft scheduled to land at the aerodrome, irrespective of the number of movements.

This comment does not appear to have been withdrawn in the revised proposals.

The “irrespective of the number of movements” means that Airservices may well be supplying, and charging for, a level of service not legally required.

The likely impact of the proposed prices on the users of airports and air traffic control services – in particular, the likely impact on demand for air travel, airline scheduling decisions, providers of other aviation services and airfares.

The RAAA believes the impact of these proposals will be a decrease in the use of towered regional and GAAP airports which will flow through to an increase in airfares. Both of these effects will lessen the demand for air travel and will have adverse effects on aviation associated businesses and their employment levels.

Yours sincerely

Brian J Candler
Chief Executive Officer